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RESEARCH ARTICLE

MUTUAL FUNDS PERFORMANCE EVALUATION IN INDIA

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ABSTRACT

In recent years, credit inter-mediation is shifting, with the traditional dominance of the banking sector yielding ground to non-bank intermediaries, including the asset management industry. In addition, mutual funds play an important role in equity, debt and money markets as efficient allocates of resources. The debt portfolio of mutual funds mainly comprises corporate debt instruments, which include floating rate bonds, non-convertible debentures and public sector undertaking bonds. In the money market segment, mutual funds are the major lenders in the collateralize borrowing and lending obligation segment, accounting for over 60 per cent of lending in this segment. As major domestic institutional investors, they operate in both primary and secondary segments of the capital market, providing a buffer against market volatility. AUM of MFs in India has registered a compound annual growth rate of 25 per cent over the last five years, outstripping the compound annual growth rate of only 11 per cent registered by aggregate bank deposits of scheduled commercial banks. With growing formalization and financialisation of the Indian economy, household savings have been shifting from physical assets to financial assets and within financial assets, from bank deposits to securities.

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INTRODUCTION

A mutual fund is a professionally managed investment fund that pools money from many investors to purchase securities. These investors may be retail or institutional in nature. Mutual funds have advantages and disadvantages compared to direct investing in individual securities. The primary advantages of mutual funds are that they provide economies of scale, a higher level of diversification, they provide liquidity, and they are managed by professional investors. On the negative side, investors in a mutual fund must pay various fees and expenses. The first introduction of a mutual fund in India occurred in 1963, when the Government of India launched Unit Trust of India. UTI enjoyed a monopoly in the Indian mutual fund market until 1987, when a host of other government-controlled Indian financial companies established their own funds, including State Bank of India, Canara Bank and by Punjab National Bank. Larger Indian Mutual Fund Industry has benefited from outsourcing the activity of servicing their investors to two of the leading Registrar and Transfer Agents in India namely CAMS and Karvy. While CAMS commands close to 65% of the Assets servicing, rest is with Karvy. Mutual fund investments done online are also quicker and do not require you to step out of your comfort zone for any document verification or fund transfer. The entire process is handled efficiently online. Funds India has an award-winning team of market research analysts, financial gurus and investment experts who will direct your funds into the most rewarding mutual funds.

Definition

A mutual fund is an investment security that enables investors to pool their money together into one professionally managed investment. Mutual funds can invest in stocks, bonds, cash or a combination of those assets. The underlying security types, called holdings, combine to form one mutual fund, also called a portfolio. In simpler terms, mutual funds are like baskets. Each basket holds certain types of stocks, bonds or a blend of stocks and bonds to combine for one mutual fund portfolio.

Objectives

- To study the organizational structure of mutual funds, marketing as well as the regulatory framework operating in India for mutual funds in India.
- To know about the performance evaluation of mutual funds.
- Top mutual funds in India.
- To Study evaluate and compare the performance of different mutual fund in India with reference to different performance indicators.

Structure of Mutual Funds in India: The structure of Mutual Funds in India is a three-tier one. There are three distinct

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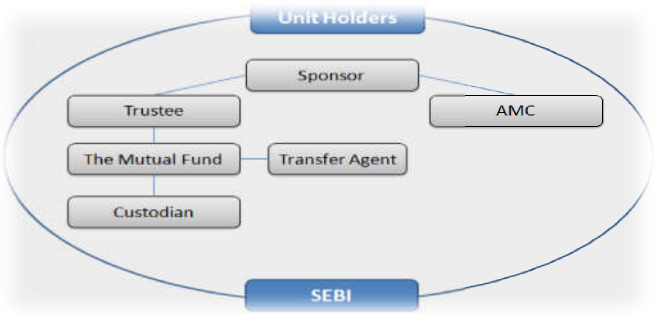
entities involved in the process – the sponsor who creates a Mutual Fund, trustees and the asset management company which oversees the fund management. The structure of Mutual Funds has come into existence due to SEBI Mutual Fund Regulations, 1996. Under these regulations, a Mutual Fund is created as a Public Trust. We will look into the structure of Mutual Funds in a detailed manner.



Fund Sponsor is the first layer in the three-tier structure of Mutual Funds in India. SEBI regulations say that a fund sponsor is any person or any entity that can set up a Mutual Fund to earn money by fund management. This fund management is done through an associate company which manages the investment of the fund.

- A sponsor can be seen as the promoter of the associate company. A sponsor has to approach SEBI to seek permission for a setting up a Mutual Fund. Once SEBI agrees to the inception, a Public Trust is formed under the Indian Trust Act, 1882 and is registered with SEBI.
- Trustees are appointed to manage the trust and an asset management company is created complying with the Companies Act, 1956. There are eligibility criteria given by SEBI for the fund sponsor.
- The sponsor must have experience in financial services for a minimum of five years with a positive Net worth for all the previous five years.
- The net worth of the sponsor in the immediate last year has to be greater than the capital contribution of the AMC.
- The sponsor must show profits in at least three out of five years which includes the last year as well. The sponsor must have at least 40% share in the net worth of the asset management company.
- Any entity that fulfills the above criteria can be termed as a sponsor of the Mutual Fund. Trust and Trustees Trust and trustees form the second layer of the structure of Mutual Funds in India.
- A trust is created by the fund sponsor in favor of the trustees, through a document called a trust deed. The trust is managed by the trustees and they are answerable to investors.
- They can be seen as primary guardians of fund and assets. Trustees can be formed by two ways a Trustee Company or a Board of Trustees.
- The trustees work to monitor the activities of the Mutual Fund and check its compliance with SEBI (Mutual Fund) regulations.
- They also monitor the systems, procedures, and overall working of the asset management company. Without the trustees' approval, AMC cannot float any scheme in the market.
- The asset management company acts as the fund manager or as an investment manager for the trust. A small fee is paid to the AMC for managing the fund.
- The AMC is responsible for all the fund-related activities. It initiates various schemes and launches the same.
- The AMC is bound to manage funds and provide services to the investor. It solicits these services with other elements like brokers, auditors, bankers, registrars, lawyers, etc. and works with them.

Advantages of Mutual Funds: To summarize, the advantages of mutual funds can be described in four words simplicity, versatility, diversity, and accessibility:

Simplicity: Most investors do not have the knowledge, time or resources to build their own portfolio of stocks and bonds. Stock investors often have extensive knowledge of fundamental analysis or technical analysis. However, buying shares of a mutual fund enables an investor to own a professionally managed, diverse portfolio, although the investor may have little or no knowledge of investing concepts and strategies. Mutual funds are professionally managed, which means the investor does not need knowledge of investing in capital markets to be successful with them.

Diversity: All investors, beginners and pros alike, know that putting all of their eggs into one basket is not wise. This speaks to the wisdom of diversification with mutual funds. To diversify with stocks, an investor may need to buy 20 or more securities to reach sufficient diversification. However, many mutual funds offer complete diversification in just one security that can be easily purchased. Therefore, a mutual fund investor can break the eggs-in-one-basket rule with mutual funds, at least when getting started, and then add more mutual funds later to increase diversity in the mutual funds portfolio. For more on this idea, be sure to read our article on how to get started investing with just one mutual fund.

Versatility: There are so many types of mutual funds that investors can gain access to almost any segment of the market imaginable. For example, sector funds make it possible for investors to buy into focused areas of the market, such as healthcare, technology, financials, and even social media. Beyond sector funds, investors can also access other asset types, such as gold, oil and other natural resources. This versatility can be used for further diversification as an investor's portfolio grows. Professional money managers often use sector funds for this purpose in building client portfolios.

Accessibility: With as little as $100 an investor can get started investing with mutual funds. And the fact that mutual funds hold dozens, hundreds, or even thousands of other securities, an investor can gain access to an entire market of investable securities. For example, an investor buying shares in one of the total stock market index funds, gains exposure to over 3,000 stocks in just one fund. This returns to the simplicity and diversification of mutual funds. Although investing concepts and strategies are rarely taught in schools, the beginning investor can find easy tips about how to buy mutual funds online or in bookstores and get started investing within minutes or just a few hours. And, when it comes to certain types of assets, like foreign equities or exotic commodities, mutual funds are often the most feasible way – in fact, sometimes the only way for individual investors to participate.

Economies of Scale: Mutual funds also provide economies of scale. Buying one spares the investor of the numerous commission charges needed to create a diversified portfolio. Buying only one security at a time leads to large transaction, which will eat up a good chunk of the investment. Also, the $100 to $200 an individual investor might be able to afford is usually not enough to buy a round lot of a stock, but it will buy many mutual fund shares. The smaller denominations of mutual funds allow investors to take advantage of dollar cost averaging.

Professional Management: Most private, non-institutional money managers deal only with high net worth individuals – people with six figures (at least) to invest. But mutual funds are run by managers, who spend their days researching securities and devising investment strategies. So these funds provide a low-cost way for individual investors to experience (and hopefully benefit from) professional money management.

Individual-Oriented: All these factors make mutual funds an attractive options for younger, novice and other individual investors who don't want to actively manage their money: They offer high liquidity; they are relatively easy to understand; good diversification even if you do not have a lot of money to spread around; and the potential for good growth. In fact, many Americans already invest in mutual funds through their 401(k) or 403(b) plans. In fact, the overwhelming majority of money in employer-sponsored retirement plans goes into mutual funds.

Style: Investors have the freedom to research and select from managers with a variety of styles and management goals. For instance, a fund manager may focus on value investing, growth investing, developed markets, emerging markets, income or macroeconomic investing, among many other styles. One manager may also oversee funds that employ several different styles.

Disadvantages of Mutual Funds

Fluctuating Returns: Like many other investments without a guaranteed return, there is always the possibility that the value of your mutual fund will depreciate. Equity mutual funds experience price fluctuations, along with the stocks that make up the fund. The Federal Deposit Insurance Corporation (FDIC) does not back up mutual fund investments, and there is no guarantee of performance with any fund. Of course, almost every investment carries risk. But it's especially important for investors in money market funds to know that, unlike their bank counterparts, these will not be insured by the FDIC.

Cash: As you know already, mutual funds pool money from thousands of investors, so every day people are putting money into the fund as well as withdrawing it. To maintain the capacity to accommodate withdrawals, funds typically have to keep a large portion of their portfolios in cash. Having ample cash is great for liquidity, but money sitting around as cash is not working for you and thus is not very advantageous.

Costs: Mutual funds provide investors with professional management, but it comes at a cost – those expense ratios mentioned earlier. These fees reduce the fund's overall payout, and they're assessed to mutual fund investors regardless of the performance of the fund. As you can imagine, in years when the fund doesn't make money, these fees only magnify losses.

Diversification: Many mutual fund investors tend to overcomplicate matters – that is, they acquire too many funds that are highly related and, as a result, don't get the risk-reducing benefits of diversification; in fact, they have made their portfolio more exposed, a syndrome called diversification. At the other extreme, just because you own mutual funds doesn't mean you are automatically diversified. For example, a fund that invests only in a particular industry sector or region is still relatively risky.

Lack of Transparency: One thing that can lead to diversification is the fact that a fund's purpose or makeup isn't always clear. Fund advertisements can guide investors down the wrong path. The Securities and Exchange Commission (SEC) requires that funds have at least 80% of assets in the particular type of investment implied in their names; how the remaining assets are invested is up to the fund manager. However, the different categories that qualify for the required 80% of the assets may be vague and wide-ranging. A fund can therefore manipulate prospective investors via its title: A fund that focuses narrowly on Congo stocks, for example, could be sold with the grander title "International High-Tech Fund."

Evaluating Funds: Researching and comparing funds can be difficult. Unlike stocks, mutual funds do not offer investors the opportunity to compare the P/E ratio, sales growth, earnings per share, etc. A mutual fund's net asset value gives investors the total value of the fund's portfolio, less liabilities.

Best Performing Mutual Funds India last five years

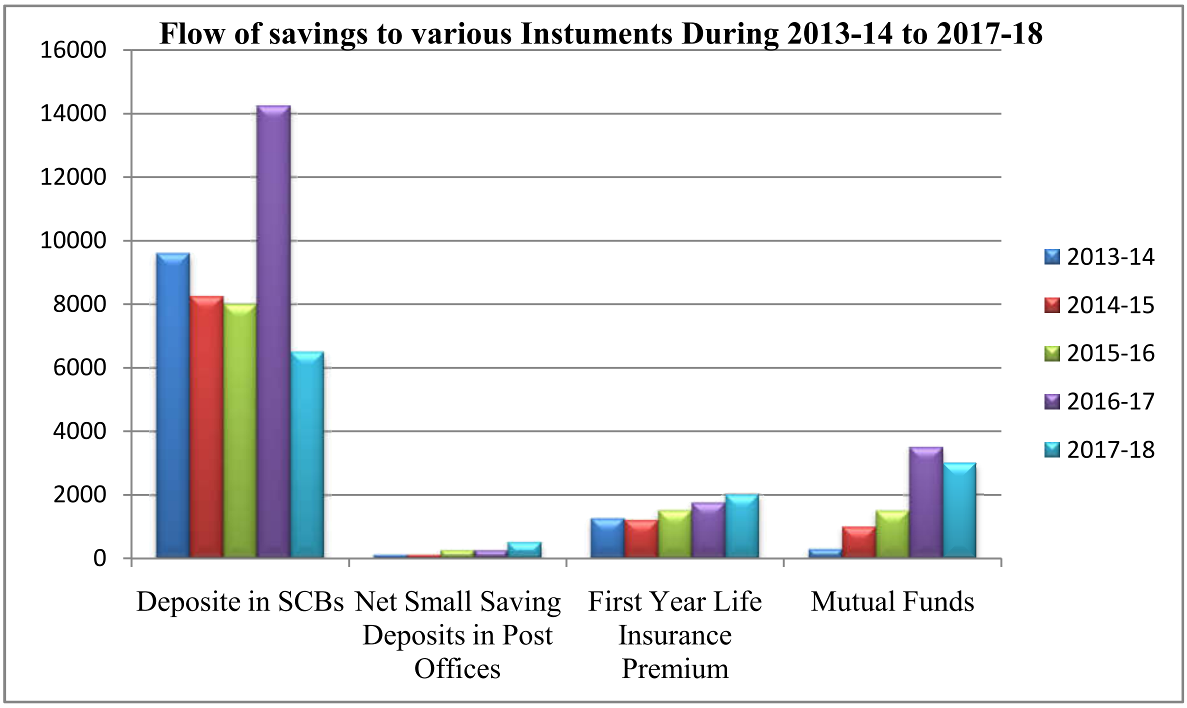
Mutual funds are one of the best investment options for the long-term wealth generation. However, the biggest problem is to identify best mutual fund for the investment. There are thousands of mutual funds which make the task of investor difficult when it comes to actual investment.

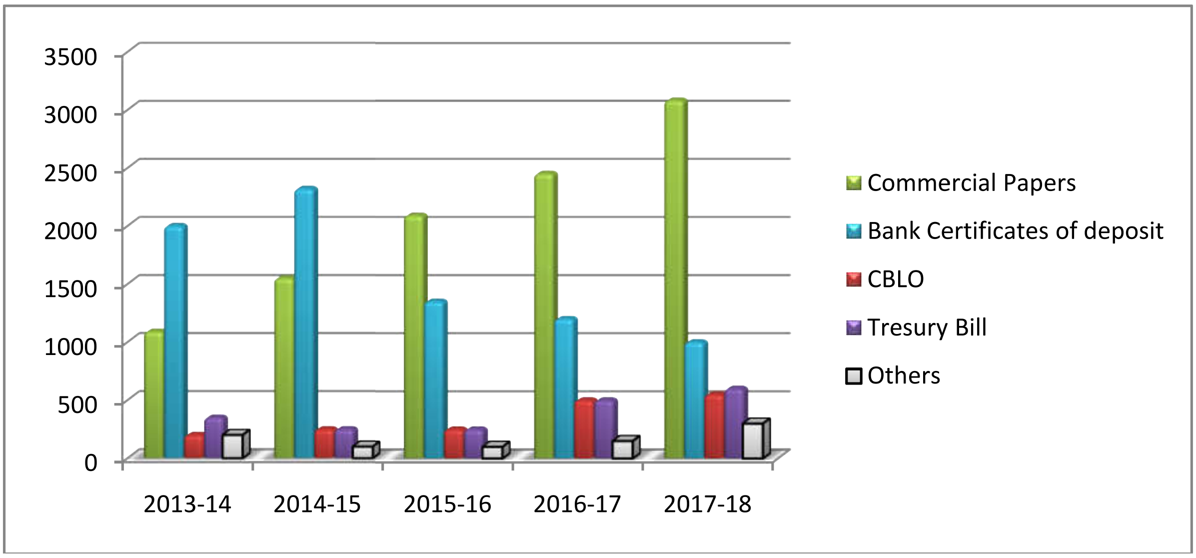
Mutual Funds Performing Analysis

Resource Mobilization: MFs appear to have emerged as a preferred investment avenue for individuals as well as corporate. While the flow of resources to banks generally declined during the period 2013-18, the flow of resources to small savings schemes registered modest increase. In comparison, the flow of resources to MFs and insurance companies registered a significant increase during the period (Chart 3). During the period 2013-2018, the CAGR of bank deposits and small savings were 11 per cent and 6 per cent, respectively, which was much lower than CAGR of AUM of MFs (25 per cent). Bank term deposits by corporate registered a much lower CAGR of 2 per cent during 2013-2017. Along with increasing levels of economic development, deep and liquid capital markets and sound regulations are catalyzing the change in preference of investors not only from metro cities but also from small cities. MF investments are also becoming broad-based in terms of spatial distribution and investor profile.

India's Mutual Fund Industry in the Global Context: The global MF industry has witnessed steady expansion in size over the years on the back of higher levels of economic development, deep and liquid capital markets and emergence of defined contribution systems that encourage participants to invest in MFs in an atmosphere of investor friendly robust regulation.

Scheme	Category	1 Year (Return %)	3 Year (Return %)	5 Year (Return%)
Birla Sun Life Top 100 Fund	Large Cap Fund	15.7	13	19.9
SBI Blue chip Fund	Large Cap Fund	12.9	14.4	20.1
Birla Sun Life Frontline Equity Fund	Large Cap Fund	14	13.1	19.7
ICICI Pru Value Discovery Fund	Diversified Fund	6.2	10.9	21.8
HDFC Balanced fund	Balanced Fund	15.4	13.9	19.3
Birla Sun Life Advantage Fund	Diversified Fund	20.4	20.5	25.2
DSPBR Small and Midcap Fund	Small and Midcap	19.1	20.2	25.4
Franklin India Smaller Companies Fund	Small and Midcap	17.8	20.2	31.5
Mirae Asset Emerging Bluechip Fund	Small and Midcap	26.5	25	31.9
HDFC Midcap Opportunities Fund	Small and Midcap	16.4	19.1	26.3





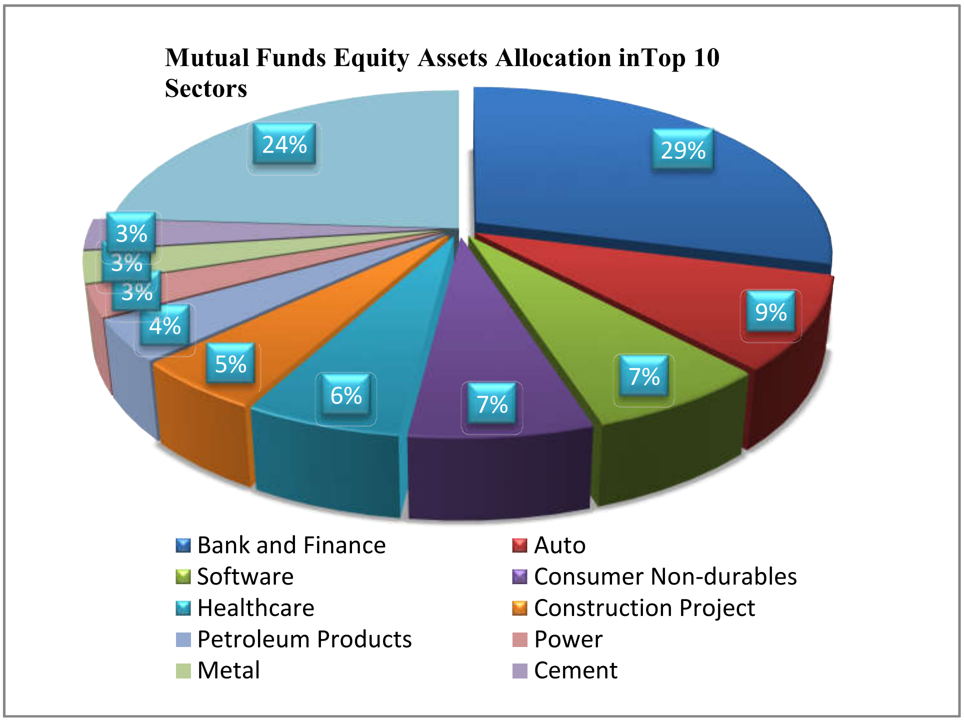
According to the Investment Company Institute, global MF assets open-end fund registered an increase of 16.2 per cent in 2017-18 to reach a level of $53.9 trillion at end-March 2018. Top 5 countries accounted for 69.1 per cent of total global assets of MFs at end-March 2018. With assets of $24.3 trillion, the US MF industry was the largest in the world, accounting for a share of 45.1 per cent of the total global MF assets at end-March 2018. In comparison, MFs in Asia accounted for 12.7 per cent of total global MF assets. At end-March 2018, there were 45 MF companies registered with the SEBI which managed an AUM of ₹21,360.4 billion.

Of the total AUM, 83 per cent was held by private sector MFs and 17 per cent by public sector MFs. The ratios of AUM of MFs to GDP and net mobilization by MFs to gross domestic savings have increased significantly over the years.

Investments in Equity, Debt and Money Market Instruments in India: MFs' investment in equities stood at ₹8.9 trillion at end-March 2018, which accounted for 6.2 per cent of market capitalization of the BSE listed companies 2.8 per cent at end-March 2014. Of the total free float market capitalisation[3], the share of MFs was about 15 per cent.

Ratios of MF AUM as per cent of GDP and Net Mobilization by MFs as per cent of Gross Domestic Savings

Year	MF AUM % of GDP	Net Mobilization by MFs as % of Gross Savings
2011-12	6.7	-0.7
2012-13	7.1	2.3
2013-14	7.3	1.5
2014-15	8.7	2.6
2015-16	9.0	3.1
2016-17	11.5	7.5

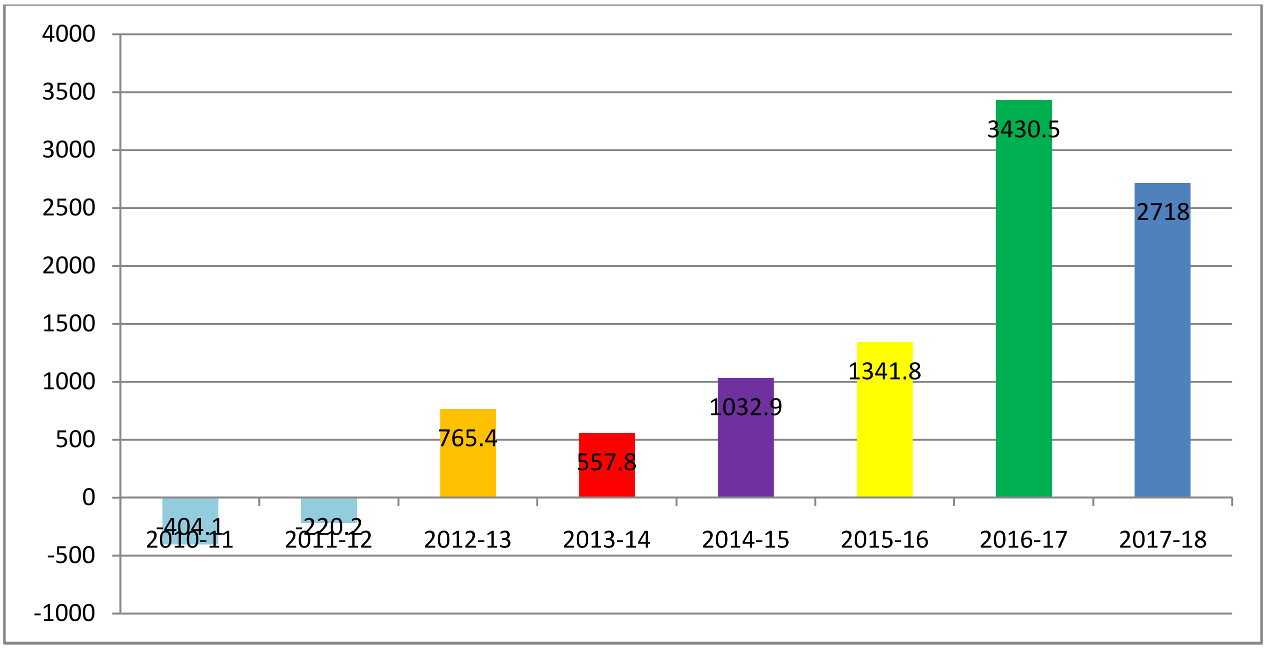


This increase has mainly been due to higher investments by MFs in equities in the last few years on the back of higher mobilizations by equity-oriented MF schemes. Top 10 sectors accounted for 76 per cent of the total equity assets of MFs. The banking and finance sector has the highest weight in MFs' portfolio.

Investor Profile: During the period 2013-18, average yearly funds mobilized by MFs was significantly higher at ₹1,812.2 billion as compared with ₹119.8 billion during 2008-13. Fund mobilization by MFs reached a record in 2016-17, increasing by almost 3 times over the previous year, in the wake of demonetization in November 2016. However, there was a decline in fund mobilization in 2017-18 mainly on account of higher net outflows from debt/income schemes on higher redemptions by corporate/institutional investors.

Findings

- Mutual fund's assets under management as a percentage of GDP growth is a typical indicator used to show low penetration of mutual funds of a country
- Year 2018 was an action-packed year for the Rs 23 lakh crore Indian mutual funds (MF) industry as well as for its investors. Funds got friendlier as costs were pushed down and steps were taken to further curb misselling. Fund categories - and all schemes within - got standardized. This made it easier for investors to compare one fund with another. Perhaps the only piece of bad news was the introduction of long-term capital gains tax (LTCG) on equity funds in Budget 2018.
- Flows remained strong through the year: in November 2018, close to Rs 8,000 crore came into MFs through systematic investment plans (SIP); compare this with December 2016 when inflows stood at under Rs 4,000 crore.
- Flows were strong despite equity markets remaining volatile throughout the year. While the S&P BSE Sensex gained 5.6 percent year to date (as on December 14), equity funds disappointed.
- Large-cap funds fell by 4 percent on an average in 2018, mid-cap funds were down 14 percent while small-cap funds were off a steep 21 percent, as per Value Research.
- Budget 2018 introduced long-term capital gains tax at 10.4 percent, including the cess for equity MFs and direct equities. Equities and equity MFs had been exempt from LTCG tax since 2004 when LTCG tax was abolished.
- The holding period beyond which LTCG tax has been imposed, continued to remain at one year. However,
- all capital gains till Rs 1 lakh was made exempt from LTCG tax. All long-term gains until January 31, 2018 were also protected. Debt funds continued to be charged 20.6 percent LTCG tax after three years.
- To ensure that investors do not switch to dividend plans to escape paying the tax since dividends from equities and equity MFs were, earlier, tax-free as well, Budget 2018 also imposed an 11.648 percent dividend distribution tax. Both the LTCG and dividend distribution tax came into effect April 1, 2018.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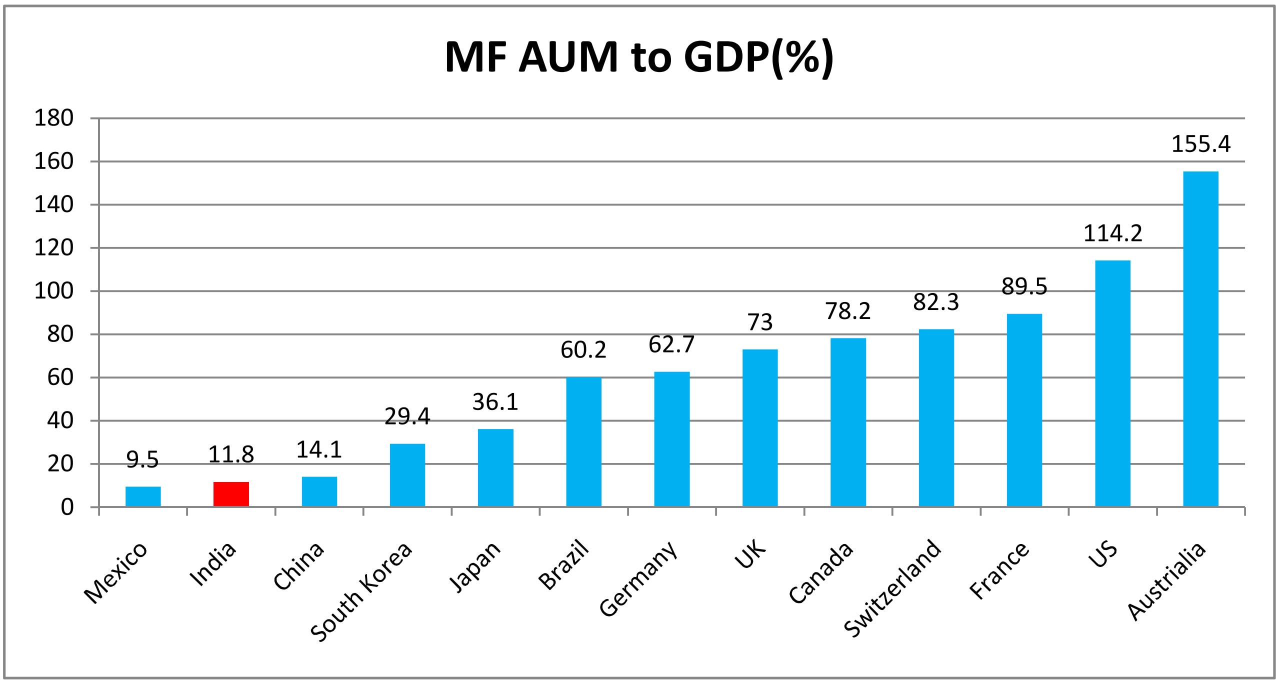
MF AUM to GDP(%)
180
160
140
120
100
80
60
40
20
0
9.5
11.8
14.1
29.4
36.1
60.2
62.7
73
78.2
82.3
89.5
114.2
155.4
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Canada
Switzerland
France
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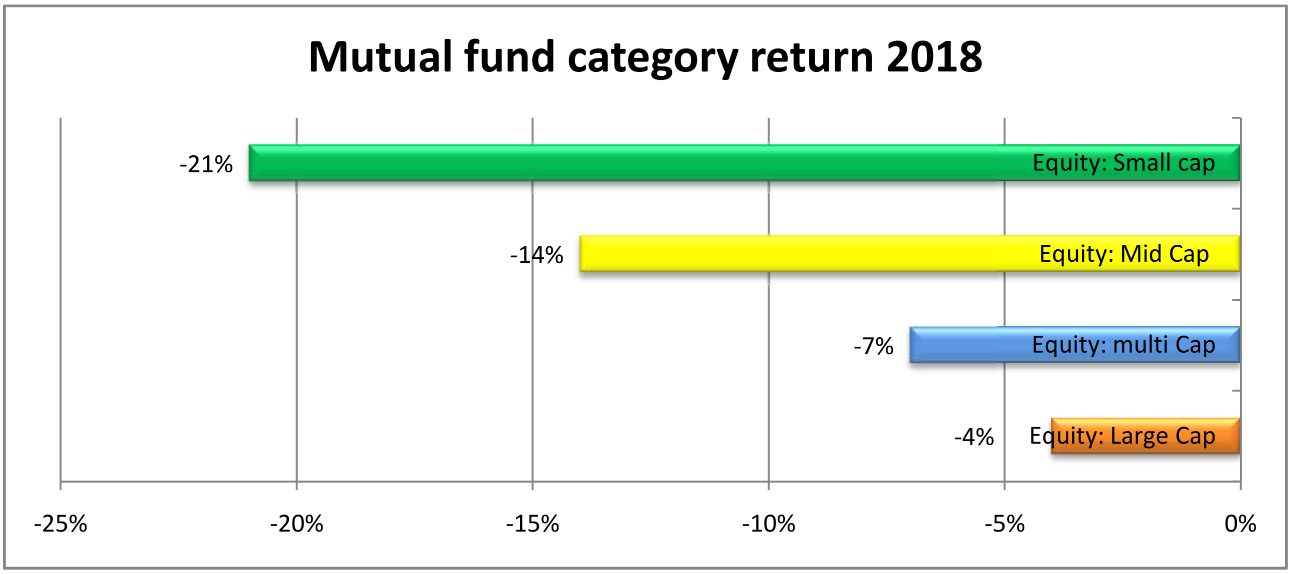
Austrialia


Mutual fund category return 2018
-21%
Equity: Small cap
-14%
Equity: Mid Cap
-7%
Equity: multi Cap
-4%
Equity: Large Cap
-25%
-20%
-15%
-10%
-5%
0%

- The cost that you pay to your mutual funds, as part of the total expense ratio, came down significantly in 2018 and is set to go down further as your fund's size goes up, as per a revised SEBI formula.
- Earlier, your fund house charged 30 basis points over and above the total expense ratio limits as an incentive to get inflows from beyond top 15 cities. In 2018, SEBI tightened the norm and said the extra charge can be imposed only if the fund house gets new inflows from beyond top 30 towns. Further, only retail inflows will make the MFs eligible to charge extra. One basis point is one-hundredth of a percentage point.
- Similarly, the extra 20 basis points charged earlier in lieu of the exit loads have now been brought down to five basis points. Schemes that don't have exit loads, including closed-end schemes, cannot collect exit load charges, anymore.
- Later in 2018, through a series of reforms, it mandated that fund houses will have to meet all their expenses from their respective schemes (no more dipping into their own balance sheets to dole out incentives to distributors) and ensuring that direct plan fees do not reflect any hidden distributor commission.
- Mutual funds lapped up significant portions in smaller banks like RBL Bank and City Union Bank where their holdings increased by 12 and 8 percentage points from October 2017 respectively. Fund go-to banks ICICI Bank, SBI and HDFC Bank also saw an increase of 1-2 percentage points in their holdings. Among NBFCs, a noteworthy pick is Bharat Financial Inclusion whose MF shareholding increased from 9.6% to 28% between October 2017 and 2018.
- Telecom stocks took a beating this year. S&P BSE Telecom lost 40% in one year which decreased its exposure in market-cap weighted BSE 500 index from 2% to 1.32%. But mutual funds, on the other hand, have been buying, resulting in a marginal increase in exposure despite the fall in price. Bharti Airtel's MF shareholding jumped from 3.4% to 7.4% between October 2017 and October 2018.

Conclusion

Mutual Funds are a vehicle that collects money from investors to buy securities. It is very safe to invest in mutual funds. There are thousands of mutual fund schemes in which you can invest. There are funds that expose your invested amount to a minimal amount of risk, but generate relatively lower returns and on the other hand, there are some funds that expose your invested amount to a lot of risk for potentially greater reward. The riskiness of the investment is always mentioned clearly in the scheme offer document. The past year has seen the market take unexpected turns. Global events have kept it on its toes while domestic factors struggled to find stability. Different sectors have shown divergent performance. Some came as a surprise, like the revival of IT stocks which found solace in the weakening rupee and pharmaceutical stocks for a brief while. Some came as a support, like the steady growth of FMCG stocks. Simply ask one of Funds India's investment experts and market analysts which are the best funds to invest in at any particular time. At any given time, there will be certain funds performing poorly and certain funds performing exceptionally well.

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