



Mutual Fund Advisor's Guide

 **KARVY** *the* **Finapolis**
Your Personal Finance Advisor

Objective

The objective of this document is to act as a guide to all branches for not only understanding the nuances of mutual funds, but also for providing effective knowledge-based advice to the clients. The guide covers mutual fund categories, their suitability and recommended picks under each category.

**“There is a time to let things happen,
and a time to make things happen.”**

Contents of the report

Table of Contents	II - III
Glossary	35 - 38

Table of Contents

1. Introduction to Mutual Funds	1 - 3
1.1. Introduction	
1.2. What is a mutual fund?	
1.3. How is mutual fund investing different from investing in stock markets?	
1.4. Benefits of mutual fund	
2. Categories of Mutual Funds	5 - 14
2.1. Introduction	
2.2. Equity funds	
2.3. Balanced funds	
2.4. Debt funds	
2.5. Risk-return grid	
2.6. Innovative funds	
2.6.1. Fund of funds	
2.6.2. Derivative funds	
2.6.3. Internationally diversified funds	
2.6.4. Capital protection funds	
3. Shape Your Wealth through SIP	15 - 16
3.1. Introduction	
3.2. Benefits of SIP	
3.3. Recommended schemes for SIP	

4. Mutual Funds – Tax Perspective	17 - 18
4.1. Individual residents	
4.2. Non resident Indians	
5. Performance Review of Recommended Schemes	19 - 28
5.1. Equity funds	
5.2. Balanced funds	
5.3. Debt funds	
5.4. ELSS	
6. Model Portfolio	29 - 31
6.1. Equity :	
6.1.1. Aggressive	
6.1.2. Moderate	
6.1.3. Conservative	
6.2. Debt :	
6.2.1. Highly liquid	
6.2.2. Moderately liquid	
6.2.3. Less liquid	
7. Investment Mantras	33 - 34
7.1. Learning from investment gurus	
7.2. Few words from the authors	

Chapter 1

Introduction to Mutual Funds

1.1 Introduction

While everyone dreams of a luxurious life, very few fulfill them. A luxurious life is generally linked with wealth. So, the question most people would like to know is: How do I create wealth? Or how can I get rich? It's really not that difficult to create wealth. It's just a matter of systematic planning and disciplined approach.

Once you have small amounts saved up, then you can start looking into ways to use that money to create more money. Money can multiply through investments in the stock market, real estate, commodities, etc. One avenue which invests in all is mutual funds. Therefore, one of the crucial ways, people can build their core capital is by investing in a mutual fund.

1.2 What is a Mutual fund?

A mutual fund basically pools the money of investors, who share some common financial objective. This money is invested in capital market instruments like shares, debentures and other securities and also in other investible avenues such as real estate, commodities etc. Income thus earned and the capital appreciation realised, are shared by its unit holders (investors) in proportion to the number of units owned by them.

1.3 How is mutual fund investing different from investing in stock markets?

The following table lists down the advantages and disadvantages associated with adopting the two approaches to investing.

Investing through mutual funds	Investing in stock markets directly
Positives	Positives
1: An investor with small amount can invest small amount and can have exposure to large number of stocks.	1: Investor with reasonable investment surplus can pick stocks according to his discretion.
2: Fund manager takes care of the portfolio performance through his expertise in analysing the company's performance and the outlook on market scenario. So the investor just has to track the fund's performance.	2: The right calls in the right stocks offer better returns.
3: The cost of churning is low when investment are made through mutual funds.	3: The investor can exploit the right opportunities (such as bonus/dividend, selection of appropriate IPOs issues) according to his choice of time and money from the universe of stocks.

4: Investors can geographically diversify their portfolio by putting their money in funds which invest in international markets.	4: The investor can earn higher return through future and options. But it involves higher risk compared to equity market.
5: SIP approach, which is a practical tool for long-term wealth creation, can be opted in mutual funds.	
6: With the usage of derivative instruments (which help limiting the downside), the investor benefits by earning higher risk-adjusted returns than the market.	
7: By investing through mutual funds which invest in IPOs, retail investors can invest in a large number of IPOs, for whatever amount he is ready to invest.	
Short comings	Short comings
1: Investor doesn't have the freedom of getting a desired allocation to specific stocks and sectors as it is decided by the fund manager.	1: It doesn't offer a user-friendly environment for the investment in IPOs due to following reasons. <ul style="list-style-type: none"> ❖ The investor can't invest in large no of IPOs at the same time due to the high up front application amount. ❖ There is a limit on the investment amount in IPOs. ❖ The investor may not be allotted the desired number of shares applied by him due to oversubscription.
2: Mutual fund investors have to shell out loads and bear the fund management fee charged by the mutual fund house and the AMC.	2: Investor has to keep a track of the market and the individual stocks as well. This whole process requires more of time, efforts and expertise.
	3: To limit his downside through F&O market, investor has to pay a hefty sum as margin money. Further, F&O trading requires constant market tracking which is a very time consuming task.
	4: Investing in international market might prove to be an expensive affair for retail investors.
	5: Relatively high cost of churning, as short-term capital gains tax comes into picture.

1.4 Benefits of mutual funds

1. Sets the investor free from four main constraints:
 - a. **Convenience and Knowledge** : The investor need not go through the tedious task of research and stock selection and need not track the market to manage the portfolio.
 - b. **Time**: Frees one from spending his precious time to track his portfolio everyday.
 - c. **Complexity**: Frees from the complexity involved in equity and debt markets.
2. **Diversification**: Investing in mutual funds enable a well-diversified portfolio, with a very small amount of investment. Diversification across various securities lowers the risk associated with investment.
3. **Higher risk-adjusted returns**: Majority of equity funds have outperformed indices while other avenues like fixed deposits, post-office schemes etc. have delivered lower returns.
4. **Professional management**: Investors purchase funds because they do not have time or expertise to manage their own portfolio. A mutual fund is relatively an inexpensive way for a small investor to get a full-time manager to create and monitor his portfolio.
5. **Low entry barrier**: Any investor can invest in mutual funds. He need not open a broking or a demat account to invest in mutual funds. Further, investment can be made in mutual funds with an amount as low as Rs. 500.
6. **Liquidity**: Easy and fast redemption leads to high liquidity. Also, one can enter and exit the fund (open-ended) depending on his discretion.
7. **Transparency**: The transparency levels are very high in this industry. Investors can view his fund's NAV on a daily basis. Also, majority of the funds disclose their portfolio holdings on a monthly basis.
8. **Tax-saving**: Mutual funds are exempted from capital gains arising out of portfolio churning. If an investor shifts his holdings, he will have to pay these taxes. Thus, mutual funds are a cost-efficient way of portfolio management. Also, there are ELSS funds (tax saving funds) which help availing the benefit of tax-saving u/s 80C. As compared to other tax saving avenues, they have lowest lock-in period and also offer higher return potential.
9. **Innovative schemes to suit unique needs of different investors**: There are schemes that offer international diversification to reduce the geographical risk. There are derivative funds which adopt various derivative strategies to gain from the either side movement of the market. Capital protection funds offer a unique feature of capital protection coupled with market linked returns.

Chapter 2

Categories of Mutual Funds

2.1 Introduction

In terms of ease with which investors can enter and exit funds, mutual funds are broadly divided into two classes-

- ❖ **Open-ended funds:** Investors can buy and sell the units from the fund, at any point of time.
- ❖ **Close-ended funds:** These funds raise money from investors only once. Therefore, after the offer period, fresh investments can not be made into the fund. If the fund is listed on a stocks exchange the units can be traded like stocks (E.g., Morgan Stanley Growth Fund). Recently, most of the New Fund Offers of close-ended funds provided liquidity window on a periodic basis such as monthly or weekly. Redemption of units can be made during specified intervals. Therefore, such funds have relatively low liquidity.

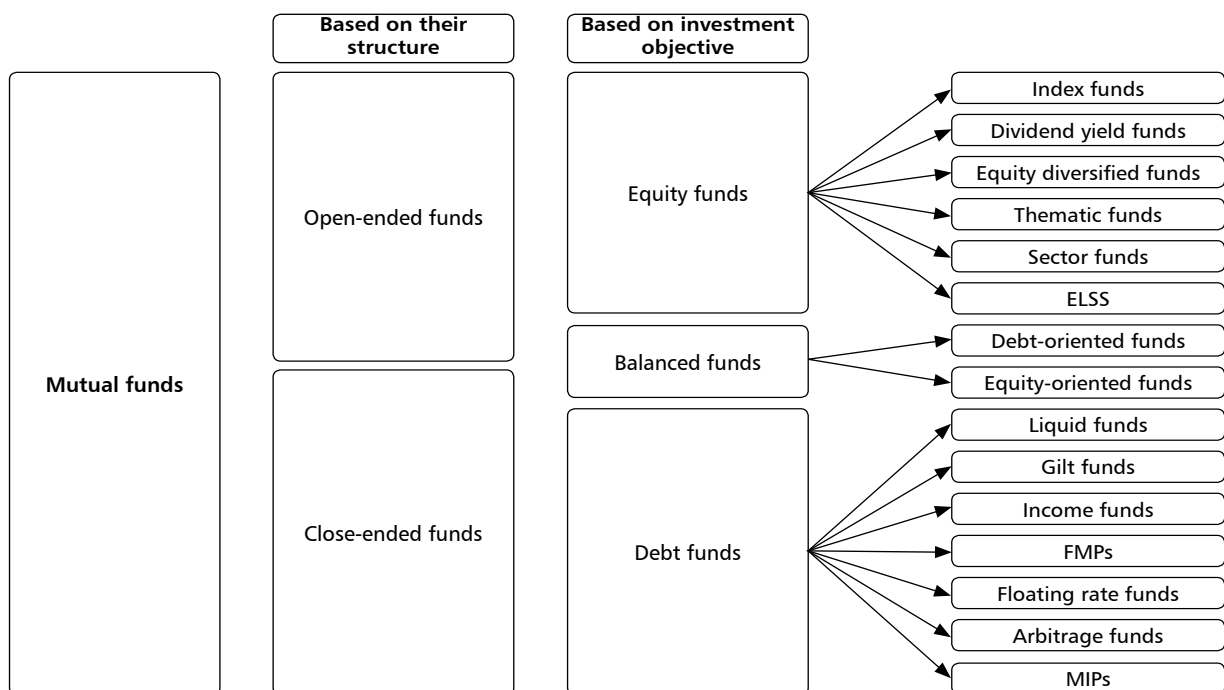
There are various classes of mutual funds depending upon the nature of investments. Here are three broad classes from

which one can choose to invest, depending upon his risk-return profile.

- ❖ Equity funds
- ❖ Debt funds
- ❖ Balanced funds

2.2 Equity funds

These funds invest in equities and equity related instruments. With fluctuating share prices, such funds show volatile performance, even losses. However, short term fluctuations in the market, generally smoothens out in the long term, thereby offering higher returns at relatively lower volatility. At the same time, such funds can yield great capital appreciation as, historically, equities have outperformed all asset classes in the long term. Hence, investment in equity funds should be considered for a period of at least 3-5 years.

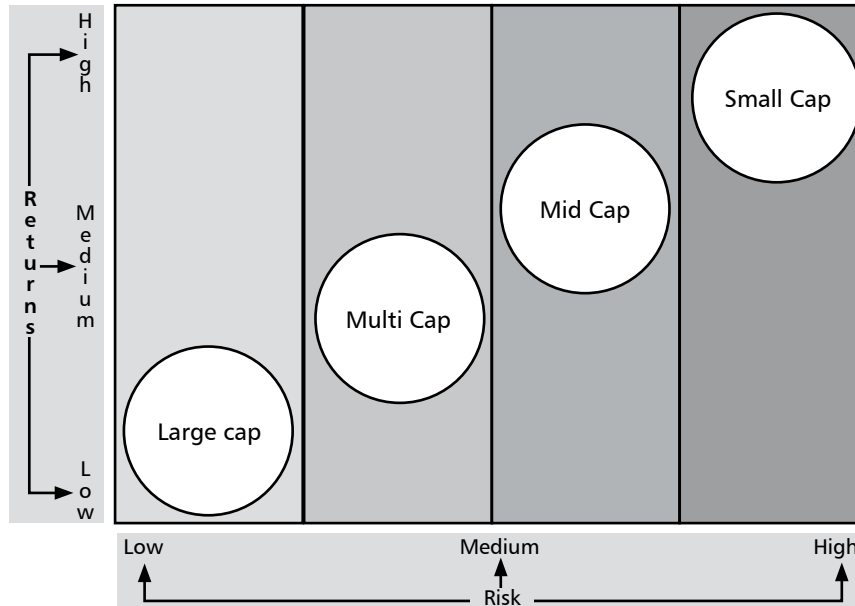


Equity funds	Portfolio Allocation	Advantages	Drawbacks	Risk-return profile	Suitability for investors	Preferred investment duration
Index funds	Track a key stock market index, like BSE Sensex or Nifty. Their portfolio mirrors the benchmark index both in terms of composition and individual stock weightages.	A convenient way of investing in equity index	Since it is more of a passive strategy of portfolio management, the returns are highly linked with index returns. In India, active funds offer higher risk-adjusted returns than index funds.	Low risk-return profile amongst equity funds	Suitable for investors who want to earn index linked returns	Equity index investing should preferably be for long-term.
Dividend yield funds	Similar to the equity diversified funds except that they invest in companies offering high dividend yields.	Since dividend yield stocks are less volatile such funds are associated with low level of risk. Less risky than a diversified equity fund.	As appreciation in the value of a dividend yield stock is not very high, these funds offer lower return than equity diversified funds.	Low risk-return profile compared to equity diversified fund	Apt for conservative equity investor	Long term horizon is preferred (at least 3 years)
Equity diversified funds	Invest 100% of the capital in equities spreading across different sectors and stocks.	-Purely diversified across stocks and sectors Such funds are known to be less volatile than sector and thematic funds	-Limits the return potential compared to other aggressive equity funds such as sector and thematic funds.	Diversification across sectors moderates the risk-return profile as compared to sector and thematic funds.	Suitable for an equity investor seeking to invest in moderately aggressive scheme within the category of equity funds	Long term horizon is preferred (at least 3 years)

Thematic funds	Invest 100% of the assets in sectors which are related through some theme. Example-An infrastructure fund invests in power, construction, cements sectors etc.	Offer higher potential returns than equity diversified funds by taking advantage of boom in various sectors.	High risk is involved because if the selected sectors perform poorly, the fund suffers.	High risk and high return category. Less aggressive than sector funds.	Suitable for aggressive investors.	Since they invest in a set of sectors and industry cycle of all sectors may not be of the same duration, it is preferred that investment should be made for ideally 3-5 years.
Sector funds	Invest 100% of the capital in a specific sector. Example- A banking sector fund will invest in banking stocks.	Have potential to offer higher returns than other diversified equity funds by taking advantage of boom in a particular sector.	High risk is involved because if the sector performs poorly, the fund suffers.	Falls in high risk-high return category.	Suitable for aggressive investors.	Investment in sectors funds should be made with a long-term horizon; say at least five years.
ELSS	Equity funds that offer tax benefits to investors	Offer tax deductions u/s 80C up to Rs. 1 lakh. Have the lowest lock-in period with high return potential among all tax saving instruments.	Low liquidity due to 3-years' lock-in	Depends upon funds portfolio concentration and exposure to various market capitalisations	Suitable for investors willing to enjoy tax benefits with equity-linked returns	Since there is a lock-in period of 3 years, investment in ELSS funds is made for a period of 3 years or more.

Fund classification based on capitalisation focus :

There are also funds based on capitalisation which invest in companies falling within a certain segment of market capitalization. Based on capitalization, equity funds can be placed on the risk return grid as shown below:



2.3 Balanced funds

Their investment portfolio includes both debt and equity. As a result, on the risk-return ladder, they fall between equity and debt funds. Balanced funds are the ideal mutual funds vehicle for investors who prefer spreading their risk across various instruments. Following are balanced funds classes:

- ❖ Debt-oriented funds
- ❖ Equity-oriented funds

Balanced funds	Portfolio Allocation	Advantages	Drawbacks	Risk-return profile	Suitability for investors	Preferred investment duration
Debt-oriented funds	Investment below 65% in equities.	They are less risky as compared to equity-oriented balanced schemes.	Limited opportunities of capital appreciation due to less involvement in equities.	These funds are less aggressive and hence offer lower risk and lower return than equity-oriented funds.	Suitable for those, who want to invest in moderately risky fund	More than one year.
Equity-oriented funds	Invest at least 65% in equities, remaining in debt.	A balanced fund with higher allocation to equities. Have the potential to generate higher returns than debt oriented balanced funds.	Higher risk due to equity-market orientation.	Due to investment in debt market, they are less aggressive than equity funds.	Suitable for those, who want to invest in moderately risky fund with higher equity allocation.	Investment in these funds should be made for long term, say 2-3 years.

2.4 Debt Funds

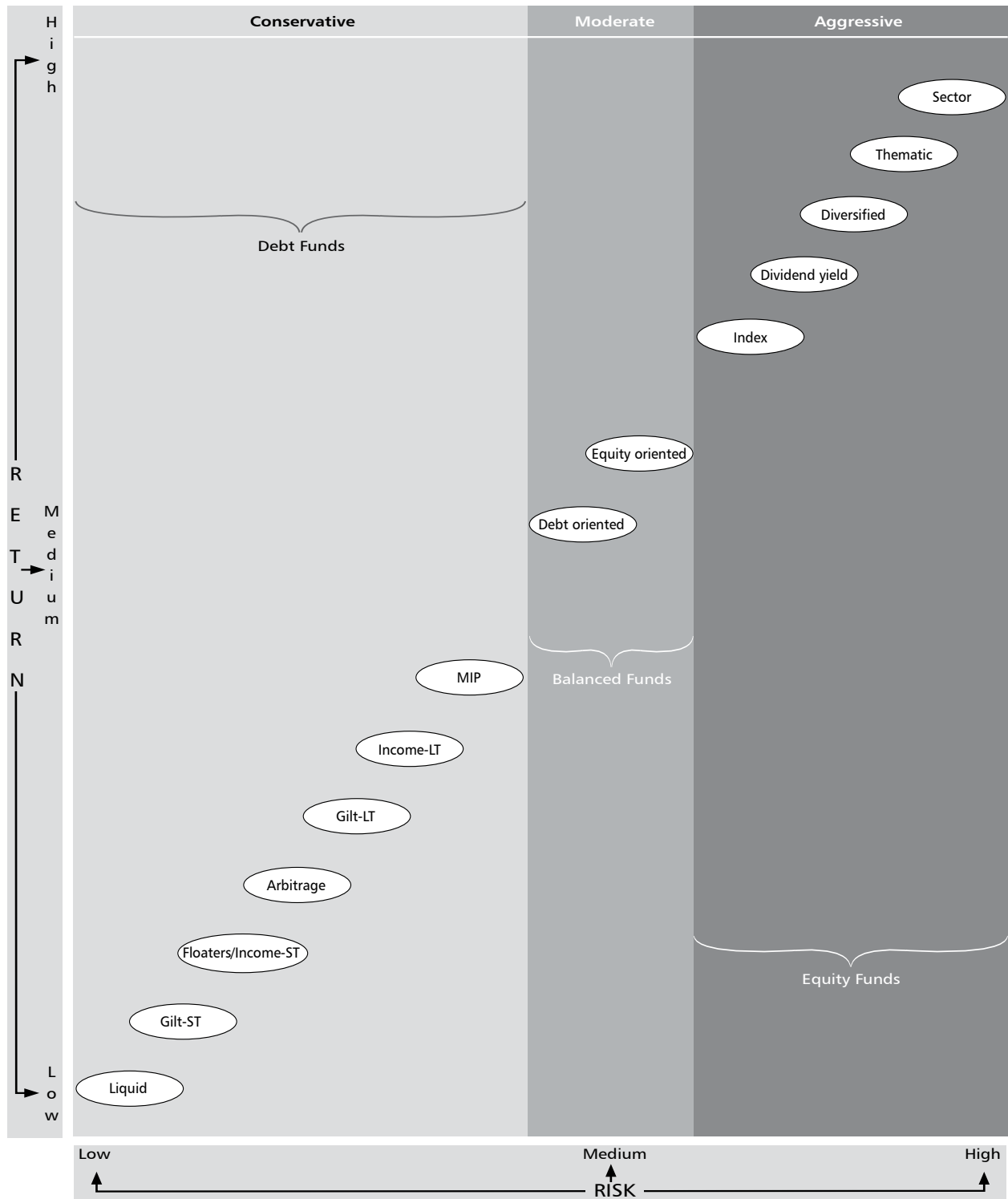
They invest only in debt instruments, and are a good option for investors averse to idea of taking risk associated with equities. Therefore, they invest exclusively in fixed-income instruments like bonds, debentures, Government of India securities; and money market instruments such as certificates of deposit (CD), commercial paper (CP) and call money. Put your money into any of these debt funds depending on your investment horizon and needs.

- ❖ MIPs
- ❖ Arbitrage Funds
- ❖ FMPs
- ❖ Arbitrage Funds
- ❖ Income Funds
- ❖ Floating rate funds
- ❖ Gilt funds
- ❖ Liquid funds

Debt funds	Portfolio Allocation	Advantages	Drawbacks	Risk-return profile	Suitability for investors	Preferred investment duration
Liquid funds	These funds invest 100% in money market instruments, a large portion being invested in call money market.	They offer a high degree of safety as well as quick maturity. Not only do liquid funds offer higher returns than bank deposits, there's no tax deduction at source (TDS) on them, unlike bank deposits.	They, however, give the lowest of returns among all the classes of mutual funds.	They offer the lowest return and have the lowest risk involved.	They are suitable for highly risk averse investors who want to park their surplus for a short period of time.	Investment duration in liquid funds should be short term, 1-3 months.
Gilt funds ST	They invest 100% of their portfolio in government securities of and T-bills.	Level of risk associated is very low. Advantageous to invest in short term gilt fund when the interest rates are likely to go up.	Return potential is very low. Investing in long term gilt funds when the interest rates are predicted to fall could give poor returns.	Since they invest in government securities and T-bills, negligible credit risk is associated with them. They lie in low risk-low return category.	Good for conservative investors who would like to avail the benefits of capital safety with government security.	Investment duration could be short or long. It is advisable to invest in short term gilt funds when the interest rates are predicted to go up.
Floating rate funds/ short-term income funds	Invest in short-term debt papers. Floaters invest in debt instruments which have variable coupon rate	Apt avenue during rising interest scenario, as interest rate risk is minimal	Typically, returns on such funds are lower than long-term funds when interest rates are falling	Interest rate risk is very low	Suitable for highly conservative investors	Investment duration could be short, medium or long. Long term implies duration of greater than 1 year. Medium term is a period of 6 months- 1 year. Short term is considered as 1-3 months.

Arbitrage funds	They generate income through arbitrage opportunities due to mispricing between cash market and derivatives market. Funds are allocated to equities, derivatives and money markets. Higher proportion (around 75%) is put in money markets, in the absence of arbitrage opportunities.	Due to the usage of arbitrage strategy, equity risk is negligible. Hence they can deliver superior risk-adjusted returns than other short term debt funds.	Attractive arbitrage opportunities may not occur always. Assets are therefore allocated to money markets. This lowers the return potential. Some funds do not offer the facility of redeeming units on any working day, thus reducing the liquidity associated with the fund.	These funds are less risky than MIPs since their exposure in equities is hedged.	Suitable for conservative investors who would like to avail better returns than debt funds.	Suitable for short as well as long term investment. Some funds charge exit loads if redeemed before a specific period. This factor should be considered before making an investment in a fund.
Gilt funds LT	They invest 100% of their portfolio in long-term government securities	Level of credit risk/ default risk is very low. Offer good returns with low risk when interest rates are falling	Give slightly lower return than other long-term income funds which invest in corporate bonds Returns not favourable when interest rates are rising	Credit risk is minimal Interest rate risk in these funds is higher than short-term income funds.	Suitable for highly conservative investors (like trusts, pension funds etc.) not willing to invest beyond govt. securities	Depends on factors like outlook for interest rate, investor's investment horizon etc.
Income funds LT	Typically, such funds invest a major portion of the portfolio in long-term debt papers.	They offer better return than other short-term income funds in falling interest rate scenario	In a rising interest rate scenario, income funds may not give fruitful results.	Interest rate risk in these funds is higher than short-term income funds.	Apt to invest in long term funds in a declining interest rate scenario.	Depends on factors like outlook for interest rate, investor's investment horizon etc.
MIPs	Have an exposure of 70%-90% to debt and an exposure of 10%-30% to equities.	Offer better returns than income funds due to their gain from the upside of stock market.	Low return potential as compared to equity oriented funds	They are the most aggressive among all debt funds, due to their exposure to equities.	Suitable for conservative/debt investors who do not mind a small exposure to equities.	More than one year.
FMPs	They invest in debt papers whose maturity is in line with that of the fund	Interest rate risk is almost nil Due to favourable tax treatment of debt funds against bank fixed deposits, post tax returns are usually higher One can lock-in prevailing yields in the market by investing in the fund	Illiquidity due to lock-in period	Very low risk	Suitable for fixed deposit investors willing to have better post tax returns	FMPs offered for varying durations, such as 1 month, 3 months, 6 months, 1 year, 3years etc. Should be chosen based on one's requirement

2.5 Risk-return grid



ST : Short term ; LT : Long term.

Notes:

Arbitrage funds here include funds which do not indulge in shorting (selling futures without holding the stock) and do not have naked equity positions. They can have upto 50% (as per previous SEBI regulation) or 80% (as per latest SEBI regulation) allocation to equity and equity related instruments.

The risk-return profile of FMPs depend upon prevailing interest rate scenario, duration of the scheme and outlook on interest rates.

2.6 Innovative funds

2.6.1 Fund of funds

A fund of funds is a mutual fund scheme that invests primarily in other schemes of the same mutual fund or other mutual funds. Hence, it is a step ahead of mutual fund in the sense that while a mutual fund keeps a track of the stocks it invests, a fund of fund keeps track of the mutual funds it invests and hence manages the portfolio on behalf of investors. Such funds are treated as a debt-oriented fund for tax purposes.

Advantages

1. Convenience

- ❖ Investors switch between different funds at different times, and dynamically manage their portfolio in an endeavour to achieve high risk-adjusted returns. This task of managing the mutual funds portfolio is done on their behalf by fund of funds.
- ❖ Instead of having different account statements for different funds, investing in a fund of fund offers the convenience of having a single consolidated account statement, while still maintaining a diversified portfolio across various schemes.

2. Flexibility

- ❖ Investors can spread their money across different strategies/managers.
- ❖ An investor may not be able to sell off when markets fall in the direct stock market. A fund of fund can easily switch from one fund to another.

3. Cost factor

- ❖ For an investor, who actively manages his portfolio, cost of execution and tax impact on short term switches could be a constraint. In such a case, investment in a fund of fund could prove to be an efficient route.

Disadvantages

1. Fee structure

- ❖ Expense fees on fund of funds are typically higher than those on regular funds because investors have to bear expenses for the main fund of fund and other funds it invests into.

2. Stock-wise portfolio tracking

- ❖ Since a fund of funds buys many different funds which further invest in many different stocks, it is possible for the fund of funds to own the same stock through several different funds. Thus, it may be difficult for an individual investor to keep a track of the overall stock holdings.

Risk-return profile

Its position in the risk-return grid depends on its allocation to equity and debts funds.

2.6.2 Derivative funds

They invest in the derivative market which limit the downside risk by selecting hedging approach and also offer additional return through shorting procedure.

Advantages

1: Limit the downside risk

Derivatives are generally used for hedging purpose so that they can limit the downside risk of equities. Hence this fund will be suitable in a falling market

2: Higher potential in generating returns

It can offer higher return through short or long positions. But this involves high risk.

Disadvantages

The investor has the possibility of losing his money if the fund takes unhedged positions.

Risk-return profile

If the fund follows only hedging procedure then it can be termed as low risk - low return category. But if it takes short positions or unhedged positions then it can fall under high-risk, high-return category.

2.6.3 Internationally diversified funds

They invest in equities and equity related instruments of companies listed overseas.

Advantages

- ❖ Geographical diversification to investors
- ❖ It provides additional diversification and flexibility to overcome country-specific factors

Disadvantages

- ❖ It can lead to volatility if it is exposed to expensive markets like Brazil or Russia

Risk-return profile:

It depends on the foreign market it is exposed to.

2.6.4 Capital protected funds (CPFs)

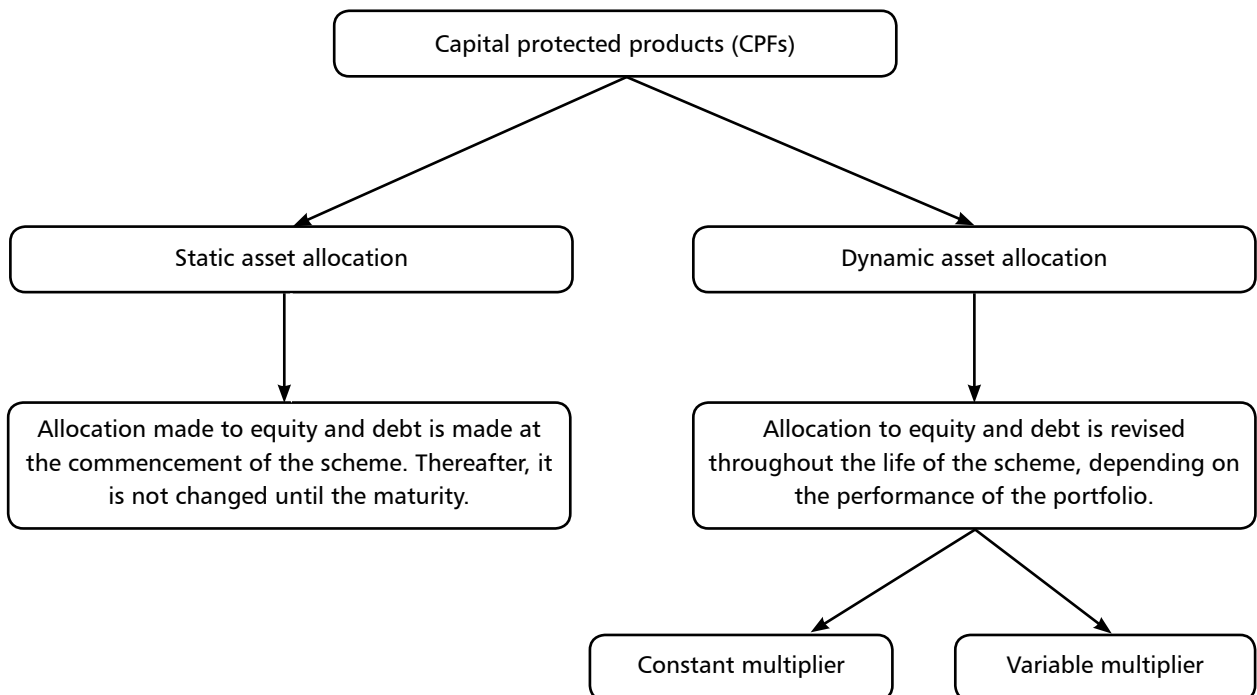
These funds intend to offer reasonable return while protecting the capital.

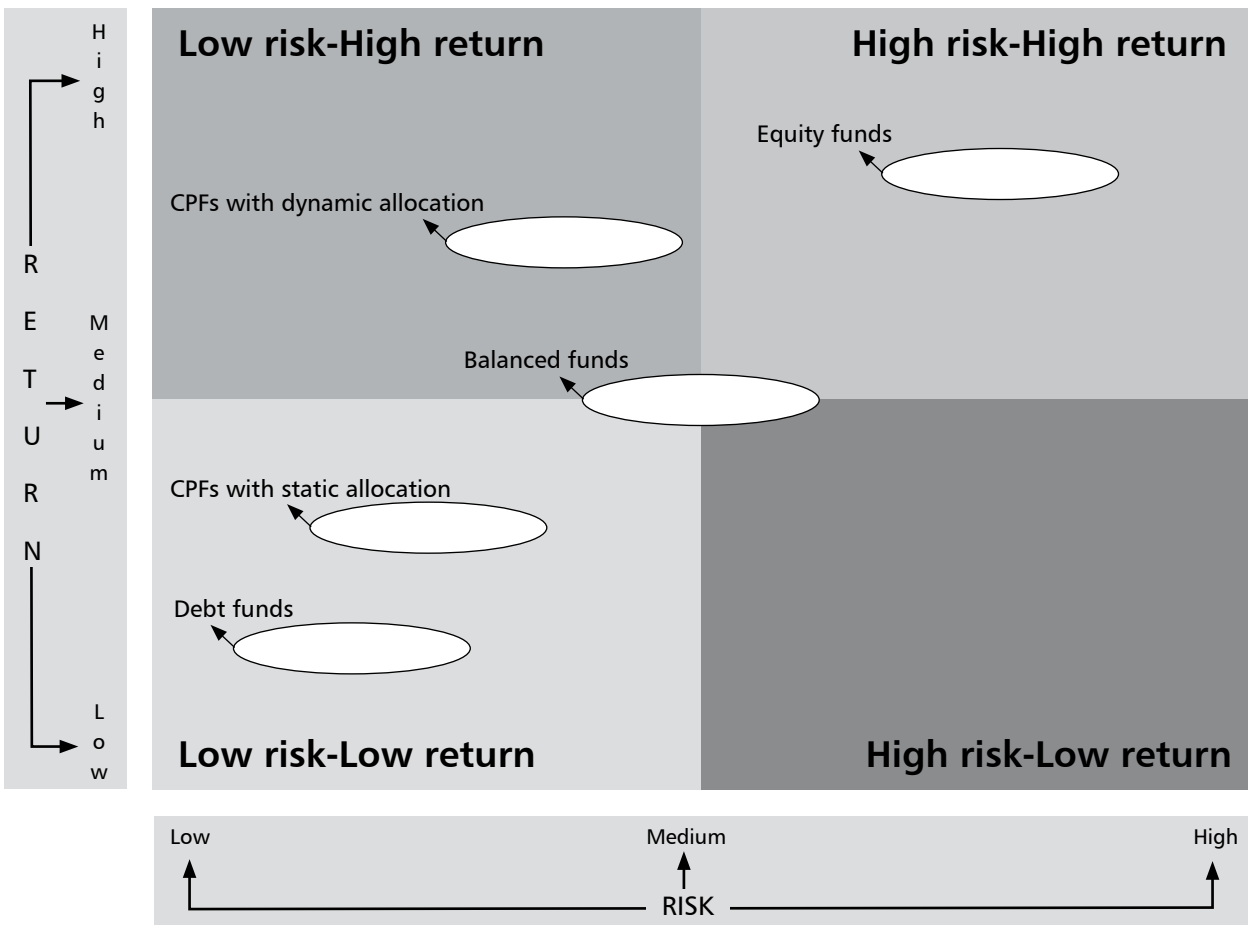
Trying to understand capital protection strategies using financial jargons is like cracking a puzzle. But these strategies are based on one simple formula which can be adopted by anyone. Let us consider a case where one wants to invest Rs. 100 for a period of 3 years. Assuming debt paper return of 8% p.a., one can invest Rs. 80 in such paper for three years. This will grow to Rs. 100.77 at the end of 3 years. He can use the remaining Rs. 20 to invest in other risky avenues which has the potential

of generating higher returns. If the risky avenues yield favorable returns, he will receive Rs. 100 plus gains on Rs. 20 invested in risky avenues. On the other hand if he loses his entire Rs. 20, he still manages to secure Rs. 100 at the end of three years. Thus, initial investment once made in debt and equity (in the report risk-free portion will be referred as debt and risky avenue will be assumed as equity) is not changed over the life time of the fund and it remains static. Therefore, it is known as Static Asset Allocation

In one more type of capital protection strategy, the allocation to debt and equity is revised and changed periodically (daily, weekly, fortnightly or monthly). It is known as dynamic asset allocation.

Multiplier: It is an implied leverage which is applied to the portfolio, which decides the risk that a portfolio can be exposed to. It generally varies from 2 to 5. Higher the multiplier, higher will be the portfolio's equity exposure in rising markets.





Chapter 3

Shape your Wealth through SIP

3.1 Introduction

Which ever way you choose to invest your money to create wealth, one thing is for sure, the sooner you start the better off you will be. Once your investment returns start compounding year after year, you will really start to see the effect it has on your wealth creation activities.

Uncertainty is the basic nature of stock markets. Time and again, the markets have proved investors wrong by showing their unpredictable nature. This impact is most crushing on retail investors. Is it possible to ride on the stock market volatility, without getting hurt? Yes, it is! For this two simple principles need to be followed religiously.

- 1: Stay invested for long term.
- 2: Adopt a systematic and regular approach towards investment.

SIP is one approach which lets the investors follow the two basic principles of investing at one go.

3.2 Benefits of SIP

- ❖ Monthly contribution: Investing at one go proves to be a burden on the pockets of investors. On the other hand, monthly investments in small amounts is more feasible for them. SIP provides this benefit to retail investors, wherein they can invest a part of their monthly savings regularly. The initial investment amount may be as low as Rs. 500.
- ❖ Systematic approach: SIP helps in investing consistently in a disciplined manner and further it helps in compounding returns as well.
- ❖ Rupee-cost averaging: Any market witnesses ups and downs over a period. The best investment approach to be followed in such cases is a SIP. Here, irrespective of the NAV movement an investor acquires more units compared to a one time investor. Successively, this means higher gains. The following table illustrates the same.

Month	NAV (Rs.)	Amount invested in SIP (Rs.)	Units allotted in SIP	Amount invested in lump sum	Units allotted in lump sum investment
1	10	5000	500.00	25000	2500
2	8	5000	625.00	-	-
3	10	5000	500.00	-	-
4	12	5000	416.67	-	-
5	10	5000	500.00	-	-
Total		25000	2541.67	25000	2500

SIP approach lets the investor to **buy more units** when the prices are low, thereby bringing down the **average cost for the investors**.

- ❖ Timing the market approach: Consider three cases. Sehwag invests Rs. 5,000 at the index level on the

first day of every month. Dhoni, being lucky, invests the same amount at the lowest value of the index every month; and Kaif, unfortunately invests the same amount but at the highest level of the index during that month.

Investment made	Sehwag (indifferent)	Dhoni (most lucky)	Kaif (unlucky)
BSE Sensex returns	20.02%	20.87%	19.09%

Note: An investment of Rs. 5,000 is made monthly for a period of 10 years (June'96 to June'06). Returns are XIRR of investments.

The returns in the above three cases differ by a very small margin, showing that while investing for long term, it doesn't really matter whether you are investing at market peaks or market lows.

Hence time in the market is more important than timing the market. Investing through SIP frees you from timing the market because over a long horizon, SIP investment evens out the market ups and downs.

3.3 Recommended schemes for SIP

The following table lists recommended equity diversified funds for the SIP approach. Equity diversified funds which have been in existence for more than *five years* have been considered

Schemes	SIP Return* (May '01 to May '06)	Entry load on SIP
Templeton India Growth Fund - Growth	41.33	2.25%
Sundram Growth- Growth	44.62	Nil
Principal Growth Fund - Growth	43.6	Nil
HDFC Capital Builder Fund - Growth	50.45	1%
Reliance Vision - Growth	58.51	2.25%
Birla SunLife Equity Fund - Growth	51.19	Nil
DSP ML Opportunities - Growth	51.87	1%
SBI Magnum Contra- Growth	66.98	2.25%

* XIRR in % as on June 1, 2006

The Funds which have a track record less than five years and have been chosen for recommendation due to their fundamentally strong portfolio holdings and futuristic outlook on that specific theme are as follows.

Schemes	Entry load on SIP
Fidelity Equity	1.25%
JM HiFi	Nil
Sundaram Select Mid-cap	Nil
SBI Bluechip	2.25%
Templeton India Equity Income Fund	2.25%
DSP MI Top 100	1%

Chapter 4

Mutual Funds Tax Perspective

For the purpose of tax-treatment, all funds are classified as equity oriented or debt oriented funds. An equity oriented fund means a fund where investments in equity shares in domestic companies is more than 65% of the assets. If a fund is able to meet this condition, it is treated as equity oriented fund, else as debt oriented fund.

4.1 Individual residents

Applicable tax rates :

Fund type	Long Term Capital Gains	Short Term Capital Gains	Dividend Distribution Tax (DDT)	Securities Transaction Tax (STT)
Equity Oriented Funds	Nil	11.22% (10% plus surcharge and educational cess)	Nil (for both open and close ended schemes) Dividends are completely tax-free	STT at 0.25% is being levied on the redemption value
ELSS	Nil	Not applicable as the fund has a lock-in period of three years	Nil Dividends are completely tax-free	STT at 0.25% is being levied on the redemption value
Debt Oriented Funds	20% with indexation or 10% without indexation (plus applicable surcharge and educational cess)	Normal slab rate plus surcharge and educational cess. Amounting to 33.66% for investors falling under highest tax bracket	DDT at 14.025 % (12.5% plus surcharge and educational cess) is deducted at source. Therefore, dividends are tax-free in the hands of investors.	N.A.
Fund of Funds	Treated as a debt oriented fund			
Capital Protected Funds	Whether the fund qualifies as an equity-oriented fund or a debt-oriented fund would depend upon its investment pattern for a period preceding the maturity period. However, if an investor redeems before the maturity period, decision whether it is equity-oriented or debt-oriented would depend upon its investment pattern for a period preceding redemption.			

Applicable tax deductions :

ELSS	Eligible for tax deduction u/s 80 c for an amount up to Rs. 1 lakh
------	--

4.2 Non-residents Indians

Applicable tax rates :

	Long Term Capital Gains	Short Term Capital Gains	Dividend Distribution Tax (DDT)	Securities Transaction Tax (STT)	TDS
Equity Oriented Funds	Nil	11.22% (10% plus surcharge and educational cess)	Nil (for both open and close ended schemes) Dividends are completely tax-free	STT at 0.25% is being levied on the redemption value	STCG → 11.22% LTCG → Nil
ELSS	Nil	Not applicable as the fund has a lock-in period of three years	Nil Dividends are completely tax-free	STT at 0.25% is being levied on the redemption value	LTCG → Nil
Debt Oriented Funds	20% with indexation or 10% without indexation (plus applicable surcharge and educational cess)	Normal slab rate plus surcharge and educational cess. Amounting to 33.66% for investors falling under highest tax bracket	14.025% (12.5% + 10% surcharge + 2% education)	N.A.	STCG → 33.66% LTCG → 20% (after providing for indexation) DDT → 14.025%
Fund of Funds	Treated as a debt oriented fund				
Capital Protected Funds	Whether the fund qualifies as an equity-oriented fund or a debt-oriented fund would depend upon its investment pattern for a period preceding the maturity period. However, if an investor redeems before the maturity period, decision whether it is equity-oriented or debt-oriented would depend upon its investment pattern for a period preceding redemption.				

Applicable tax deduction :

ELSS	Eligible for tax deduction u/s 80 c for an amount up to Rs. 1 lakh
------	--

Performance Review of Recommended Schemes

5.1. Equity Funds

Aggressive schemes

Schemes	Crisil Ranking#	Return(%)*				Risk				Load Structure	
		6-months	1-year	3-year	5-year	Std. deviation	Downside probability	Sortino	Entry load	Exit load	
DSP ML Small & Midcap	N.A.	New Fund				New Fund				2.25%	0.05% if redeemed within 3 months
DSP ML Opportunities	2	6.31	43.38	50.94	48.83	28.90	0.23	1.50	2.25%	Nil	
JM Hi Fi	N.A.	New Fund				New Fund				2.25%	Nil
Kotak Life Style	N.A.	New Fund				New Fund				2.25%	1% if redeemed within 6 months
Reliance Diversified Power Sector	N.A.	0.38	39.01	N.A.	N.A.	34.21	0.26	1.37	2.25%	Nil	
Reliance Growth	1	3.76	29.83	61.77	63.83	31.96	0.27	1.12	2.25%	Nil	
Sundaram BNP Paribas Capex Opportunities	N.A.	5.29	N.A.	N.A.	N.A.	36.66	0.24	1.34	2.25%	3% if redeemed within 6 months	
Sundaram BNP Paribas Rural	N.A.	New Fund				New Fund				2.25%	3% if redeemed within 6 months
Sundaram BNP Paribas Select Midcap	1	16.23	54.58	67.91	N.A.	28.40	0.27	2.11	2.25%	Nil	
Tata Infrastructure	N.A.	8.37	46.58	N.A.	N.A.	34.46	0.25	1.54	2.25%	0.5% if redeemed within 3 months	

Moderate Schemes

Schemes	Crisil Ranking#	Return(%)*				Risk			Load Structure	
		6-months	1-year	3-year	5-year	Std. deviation	Downside probability	Sortino	Entry load	Exit load
Birla Sunlife Equity	3	3.60	34.77	56.65	45.30	31.13	0.24	1.23	2.25%	Nil
DSP ML Equity	1	7.72	38.52	51.52	43.09	33.45	0.33	0.57	2.25%	Nil
Fidelity Equity	N.A.	5.87	35.69	N.A.	N.A.	29.59	0.24	1.24	2.25%	1% if redeemed within 6 months
Fidelity India Special Situation	N.A.	New Fund				New Fund			2.25%	1% if redeemed within 6 months
Franklin India Flexicap	N.A.	6.87	47.53	N.A.	N.A.	29.01	0.23	1.62	2.25%	Nil
HDFC Capital Builder	3	-3.46	16.30	50.62	42.36	31.43	0.28	0.69	2.25%	Nil
HDFC Core & Satellite	N.A.	4.05	41.37	N.A.	N.A.	31.53	0.25	1.34	2.25%	1% if redeemed within 12 months
HDFC Top 200	3	7.87	49.89	48.85	48.74	26.97	0.22	1.79	2.25%	1% if redeemed within 12 months
Reliance Equity	N.A.	New Fund				New Fund			2.25%	Nil
Reliance Vision	3	7.31	44.21	51.48	62.11	30.67	0.23	1.46	2.25%	Nil
SBI Magnum Contra	1	9.01	42.86	73.18	60.42	30.70	0.20	1.35	2.25%	1% if redeemed within 6 months and 0.5% if redeemed between 6 months and 12 months
SBI Magnum Multicap	N.A.	5.34	N.A.	N.A.	N.A.	30.47	0.25	1.52	2.25%	1% if redeemed within 6 months and 0.5% if redeemed between 6 months and 12 months

Conservative schemes										
Schemes	Crisil Ranking#	Return(%)*				Risk			Load Structure	
		6-months	1-year	3-year	5-year	Std. deviation	Downside probability	Sortino	Entry load	Exit load
DSP ML Top 100	3	8.84	49.55	46.71	N.A.	28.97	0.22	1.68	2.25%	Nil
Franklin India Bluechip	4	7.18	44.06	46.37	43.03	28.71	0.22	1.52	2.25%	Nil
SBI Magnum Bluechip	N.A.	2.35	N.A.	N.A.	N.A.	31.91	0.36	-0.26	2.25%	Nil
Sundaram BNP Paribas India Leadership	2	0.07	34.88	N.A.	N.A.	31.20	0.26	1.29	2.25%	Nil
Templeton India Equity Income	N.A.	N.A.	N.A.	N.A.	N.A.	16.56	0.33	2.05	2.25%	0.5% if redeemed within 6 months

Notes:

1. Some new funds have been chosen on the basis of their investment philosophy and fundamentally strong portfolios.
2. Entry and exit load have been mentioned for the amount less than Rs.2 crores. The amount restriction for the load structure may vary according to the AMC.
3. Risk analysis is computed on a daily 1-month rolling return for the period of the last 1-year as on September 1, 2006.

*Returns as on September 1, 2006. 6-months returns are absolute, rest are annualised.

CRISIL rankings for quarter ending June, 2006

The fund selection approach

We have followed the top-down approach for fund selection.

1. First step includes short listing of funds based on the outlook with reference to specific sectors, industries and market segment (large, mid and small capitalisation). This step generates a list of funds whose portfolio looks attractive and is likely to be among the top performers in its category.
2. Further, we have classified these funds into three categories based on the risk associated with them. The criterion for assessing the risk associated includes portfolio concentration, sectoral focus, exposure to various market capitalisations and investment philosophy (growth and value).
3. Under each category, funds have been further filtered based on their performance and consistency in returns.
4. Some new funds which could not be assessed based on their historical performance have also been included as we remain bullish on their portfolio holdings.

Aggressive Funds

These funds are considered as high risk-high return equity funds. Funds focusing on one specific sector, theme or having mid and small cap orientation fall under this category. Also, funds which invest in a limited number of sectors depending upon the fund manager's outlook like opportunities fund fall under this category.

Moderate Funds

These funds are considered as moderate risk-moderate return equity funds. Funds which invest across all market segments such as multi-cap funds and contra funds fall under this category. Further a fund may also fall under this category due to its structuring, investment strategy and stock universe such as large-cap oriented derivative fund.

Conservative Funds

These equity funds offer low return with low risk. Selection of these funds mainly depends on the defensive strategy taken by mutual funds. Like large cap funds are exposed to large companies which generally offers a low return and the risk involved in these funds are low.

5.2. Balanced funds

Schemes	Crisil Ranking#	Asset allocation (% of corpus) @		Return (%)*				Load structure	
		Equity	Debt	6-months	1-year	3-year	5-year	Entry load (%)	Exit load (%)
DSP ML Balanced	3	66.7	28.44	5.7	33.49	33.87	31.37	1%	1.25% if redeemed within 12 months
HDFC Prudence	1	75.18	19.76	9.66	33.27	39.9	41.43	2.25%	1% if redeemed within 1 year
JM Balanced	N.A.	69.88	9.14	8.07	34.12	28.05	22.97	2.25%	0%
SBI Magnum Balanced	1	66.96	18.06	5.99	28.81	46.16	33.64	2.25%	1% if redeemed within 6 months and 0.5% if redeemed within 1 year

Notes:

*Returns as on September 5, 2006. 6-months returns are absolute, rest are annualised.

CRISIL rankings for quarter ending June, 2006

@ As on Aug 31, 2006

1. Entry and exit load have been mentioned for amount less than Rs.2 crores. The amount restriction for the load structure may vary according to the AMC.
2. Any debt-oriented balanced scheme has not been listed. When the portfolio requires more than 50% exposure to debt, we recommend investing separately in equity and debt funds to achieve a desired debt-oriented asset allocation than investing in such balanced fund. This will result in a more tax efficient portfolio.

The fund selection approach: Balanced funds

Asset allocation and risk adjusted performance are primary factors for the selection of balanced funds.

5.3 Debt Funds : For long-term (more than 1 year)

Schemes	Crisil Ranking#	Asset allocation (% of corpus)@			Return (%)*				Expense ratio (%)	Average maturity (Years)	Load structure	
		Equity	Debt	Others	1-month	3-month	6-month	1-year			Entry load	Exit load
Birla MIP II Wealth 25	2	17.13	65.99	16.88	2.64	3.28	3.51	11.41	2.25	1.01	Nil	1% if redeemed within 12 months
DSP ML Savings Plus Moderate	4	13.01	79.33	7.66	2.02	2.99	3.96	10.54	2.07	0.175 (duration)	Nil	0.6% if redeemed within 30 days, 0.5% if redeemed between 31-60 days, 0.4% if redeemed between 61-90 days, 0.3% if redeemed between 91-120 days, 0.2% if redeemed between 121-150 days, 0.1% if redeemed between 151-180 days, nil after 180 days
MIP												
HDFC MIP Long-term	1	25.25	62.65	12.10	3.1	4.31	4.44	14.35	1.91	1.35	Nil	0.5% if redeemed within 6 months
Reliance MIP	3	18.82	63.56	17.62	3.64	4.11	6.54	11.87	2	1.31	Nil	0.75% if redeemed within 3 months, 0.6% if redeemed between 3-6 months, 0.5% if redeemed between 6-9 months, 0.25% if redeemed between 9-12 months
Arbitrage												
JM Arbitrage Advantage	N.A.	67.58	0	31.77	0.51	N.A.	N.A.	N.A.	N.A.	N.A.	Nil	1% if redeemed within 3 months
Pru ICICI Blended Plan B	N.A.	14.47	76.43	9.10	0.53	1.3	3.72	6.36	1.5	0.23	Nil	0.5% if redeemed within 30 days
Birla Sunlife Income	3	0	78.8	21.20	0.98	1.99	3.77	5.16	1.52	2.22	Nil	0.6% if redeemed within 90 days
Pru ICICI Long-term	3	0	35.66	64.34	0.71	1.87	3.73	5.60	0.75	0.51	Nil	Nil
Income-LT												
Reliance Income	2	0	100	0	1.18	1.62	2.88	4.35	1.5	2.49	Nil	0.5% if redeemed within 6 months

For medium-term (6 months to 1 year)

	Schemes	Crisil Ranking#	Corpus size@	Return (%)*				Expense ratio (%)	Average maturity Years	Load structure	
				1-month	3-month	6-month	1-year			Entry load	Exit load
Floater-LT	Birla Floating Rate LT	N.A.	97.67	0.56	1.41	2.83	5.46	0.65	0.24	Nil	1.00
	HDFC Floating Rate Income LT	3	230.73	0.55	1.59	3.16	5.77	0.89	2.04	Nil	0.5
	Kotak Floater LT	2	479.78	0.6	1.76	3.34	5.96	0.72	0.5	Nil	0.5
	Principal Floating Rate Flexible Maturity	1	207.94	0.61	1.72	3.37	6.04	0.84	0.89	Nil	0.25
Income-ST	Birla Bond Plus Retail	2	509.16	0.61	1.72	3.92	6.1	0.8	0.83	Nil	0.25
	Grindlays SSI ST	4	580.62	0.58	1.62	3.47	5.36	0.47	0.81	Nil	Nil
	Reliance Short Term	1	341.78	0.68	1.83	3.59	6.1	0.62	0.93	Nil	Nil
	UTI Liquid ST Regular	1	60.44	0.63	1.75	3.53	6.41	0.64	0.25	Nil	Nil

For Short-term (1 month to 3 months)

	Schemes	Crisil Ranking#	Corpuse size@	Return (%)*				Expense ratio	Average maturity	Load structure	
				1-month	3-month	6-month	1-year			Entry load	Exit load
Floaters-ST	DSP ML Floating Rate-ST	5	815.78	0.51	1.47	2.92	5.68	0.72	0.2	Nil	Nil
	Grindlays Floating Rate-ST	4	545.16	0.56	1.55	2.96	5.59	0.32	0.3	Nil	Nil
	JM Floaters ST	3	367.08	0.57	1.63	3.21	6.16	0.5	0.36	Nil	Nil
	Templeton Floating Rate-ST	4	1,176.79	0.57	1.56	2.93	5.64	0.75	0.49	Nil	Nil
	Birla Cash Plus-Retail	2	8871.00	0.56	1.59	3.19	6.04	0.34	0.24	Nil	Nil
Liquid	Canliquid Retail	4	1,645.80	0.55	1.63	3.3	6.33	0.22	0.27	Nil	Nil
	DSP ML Liquidity	1	3,674.71	0.53	1.57	3.22	6.19	0.47	N.A.	Nil	Nil
	HDFC Cash Management Savings	2	4,027.75	0.58	1.66	3.28	6.15	0.38	0.32	Nil	Nil

Notes:

1. Others include cash and money market instruments
2. Entry and exit load have been mentioned for the amount less than Rs. 2 crores. The amount restriction for the load structure may vary according to the AMC.

*Absolute returns as on September 5, 2006

CRISIL rankings for quarter ending June, 2006

@ Corpus size in Rs. Crores as on Aug 31, 2006

The fund selection approach: Debt Funds

MIPs: Asset allocation between debt and equity, and performance analysis are the main criteria for fund selection. Further, funds having low exit load and low CDSC period have been preferred.

Arbitrage Funds: Suggested asset allocation and performance of the funds have been factored in while suggesting arbitrage funds. While the limit for exposure to equities and derivatives for JM Arbitrage Advantage Fund is 80% of the portfolio, it is 49% in case of Pru ICICI Blended Plan B.

Income funds and floaters: Historical returns, average maturity of the portfolio held and expenses ratios have been considered for the selection of funds. The weight assigned to each parameter differs for different categories. While expense ratio has been assigned more weight in short-term funds, average maturity has been assigned more weight in case of long-term income funds.

Liquid funds: Performance, expenses ratios and corpus size of the fund are the main parameters for the selection of the funds.

5.4 ELSS

	Crisil Ranking#	Return*				Risk			Load Structure	
		6-months (abs.)	1-year	3-year	5-year	Std. deviation	Sortino	Downside probability	Entry load	Exit load
Fidelity Tax Advantage	N.A.	4.59	New Fund			New Fund			2.25%	Nil
Franklin India Taxshield	3	-0.80	29.44	45.76	40.99	23.58	2.19	0.23	2.25%	Nil
HDFC Tax saver	2	5.70	31.74	61.68	51.89	25.96	2.62	0.22	2.25%	Nil
SBI Magnum Taxgain	1	5.80	28.63	79.92	54.89	32.70	1.47	0.27	2.25%	Nil

Notes:

1. Some new funds have been chosen on the basis of their investment philosophy and fundamentally strong portfolios.
2. Entry and exit load have been mentioned for the amount less than Rs. 2 crores. The amount restriction for the load structure may vary according to the AMC.
3. Risk analysis is computed on a daily 1-month rolling return for the period of last 1-year as on September 1, 2006.

* Returns as on September 1, 2006

CRISIL rankings for quarter ending June, 2006

The fund selection approach

Fund selection has been made on the basis of consistent performance, AMC track record and futuristic outlook on fund's holdings.

Chapter 6

Model Portfolio

6.1 Equity :

6.1.1 Aggressive*

	Fund name	Recommended exposure as % of portfolio	Degree of aggression	Fund category
1	DSP ML Opportunities [mainly large+mid]	10	Aggressive	Equity diversified
2	Fidelity Equity [mainly large+mid]	7	Moderate	Equity diversified
3	JM Hi Fi	10	Aggressive	Thematic
4	Reliance Diversified Power Sector [Large+mid]	10	Aggressive	Thematic
5	Reliance Equity [Large+ derivatives]	7	Moderate	Derivatives fund
6	SBI Magnum Contra [Large+mid]	7	Moderate	Contra
7	Sundaram Rural	7	Aggressive	Thematic
8	Sundaram Select Midcap [Midcap]	20	Aggressive	Midcap
9	Tata Infrastructure [Large+mid]	12	Aggressive	Thematic
10	Templeton India Equity Income Fund [international stocks not > 50%, remaining Indian stocks]	10	Conservative	Exposure in international markets
	Total	100		

*Aggressive [70%] + (Moderate and Conservative) [30%]

6.1.2 Moderate*

	Fund name	Recommended exposure as % of portfolio	Degree of aggression	Fund category
1	DSP ML Opportunities [mainly large+mid]	12	Aggressive	Equity diversified
2	Fidelity Equity [mainly large+mid]	10	Moderate	Equity diversified
3	Franklin India Bluechip	10	Conservative	Equity diversified
4	JM Hi Fi	7	Aggressive	Thematic
5	Reliance Equity [Large+ derivatives]	10	Moderate	Derivatives fund
6	SBI Magnum Contra [Large+mid]	10	Moderate	Contra
7	Sundaram Rural	7	Aggressive	Thematic
8	Sundaram Select Midcap [Midcap]	12	Aggressive	Midcap
9	Tata Infrastructure [Large+mid]	12	Aggressive	Thematic
10	Templeton India Equity Income Fund [international stocks not > 50%, remaining Indian stocks]	10	Conservative	Exposure in international markets
	Total	100		

*Aggressive [50%] + (Moderate and Conservative) [50%]

6.1.3 Conservative*

	Fund name	Recommended exposure as % of portfolio	Degree of aggression	Fund category
1	DSP ML Opportunities [mainly large+mid]	10	Aggressive	Equity diversified
2	Fidelity Equity [mainly large+mid]	10	Moderate	Equity diversified
3	Franklin India Bluechip [Large]	8	Conservative	Equity diversified
4	HDFC Capital Builder [large+mid]	10	Moderate	Equity diversified
5	Reliance Equity [Large+ derivatives]	8	Moderate	Derivatives fund
6	Reliance Vision [Large+mid]	10	Moderate	Equity diversified
7	SBI Magnum Contra [Large+mid]	12	Moderate	Contra
8	Sundaram India Leadership [Large+mid]	10	Conservative	Equity diversified
9	Sundaram Select Midcap [Midcap]	10	Aggressive	Midcap
10	Templeton India Equity Income Fund [international stocks not > 50%, remaining Indian stocks]	12	Conservative	Exposure in international markets
	Total	100		

*Aggressive [20%] + (Moderate and Conservative) [80%]

6.2 Debt :

6.2.1 Highly liquid*

	Fund name	Recommended exposure as % of portfolio	Liquidity	Fund category	Category exposure
1	Grindlays Floating Rate ST	0	High	Floater	10
2	JM Floater ST	10	High	Floater	
3	Templeton Floating Rate-ST	0	High	Floater	
4	Birla Cash Plus-Retail	30	High	Liquid	90
5	HDFC Cash Mgt-Savings	30	High	Liquid	
6	DSP ML Liquidity	30	High	Liquid	
	Total	100			100

*very short-term investment

6.2.2 Moderately liquid*

	Fund name	Recommended exposure as % of portfolio	Liquidity	Fund category	Category exposure
1	JM Arbitrage Advantage Fund	20 if FMPs are available, else 40	Moderate, once in a month	Arbitrage	40
2	FMPs depending upon the availability	20 if available	Low	FMPs	
3	Grindlays Floating Rate ST	10	High	Floater	60
4	JM Floater ST	10	High	Floater	
5	Templeton Floating Rate-ST	10	High	Floater	
6	Birla Cash Plus-Retail	10	High	Liquid	
7	HDFC Cash Mgt-Savings	10	High	Liquid	
8	DSP ML Liquidity	10	High	Liquid	
	Total	100			100

*40% invested for 3 to 6 months, 60% can be redeemed anytime

6.2.3 Less liquid*

	Fund name	Recommended exposure as % of portfolio	Liquidity	Fund category	Category exposure
1	JM Arbitrage Advantage Fund	10	Moderate, once in a month	Arbitrage	80
2	MIPs or fixed duration funds depending upon availability (with slight exposure to equities)	50	Ideal for long duration	Hybrid	
3	FMPs depending upon the availability	20	Low	FMPs	
4	Grindlays Floating Rate ST	10	High	Floater	20
5	JM Floater ST		High	Floater	
6	Templeton Floating Rate-ST		High	Floater	
7	Birla Cash Plus-Retail	10	High	Liquid	
8	HDFC Cash Mgt-Savings		High	Liquid	
9	DSP ML Liquidity		High	Liquid	
	Total	100			100

*20% liquid, 80% to be invested for 2-3 years

Chapter 7

Investment Mantras

7.1 Learning from investment gurus

Be greedy. But be long-term greedy.

- Warren Buffet

What we buy is important; at what price is most important

- Rakesh jhunjhunwala

Be fearful when everyone is greedy and be greedy when everyone is fearful

- Warren Buffet

Always expect something over a time, not overnight

- Anonymous

Have conviction. Be patient. Your patience may be tested, but your conviction will be rewarded.

- Warren Buffet

Spending hours on fancying marvelous returns on an investment does not guarantee the same. Investments made with logic and rationale have a better chance of faring well.

- Anonymous

Contrarian investing is not rule, but can't be ruled out

- Rakesh jhunjhunwala

Price is what you pay. Value is what you get.

- Warren Buffet

7.2 Few words from the authors

Before investing, answer these...

- ❖ Can you afford volatility in your investment or are you a low-risk investor?
- ❖ Would you be satisfied if your fund yields low but sure-shot returns?

Your investments should reflect your risk-taking capacity. So, choose a fund whose investment objective matches yours.

Investment horizon :

Do you wish to invest for a long term or for a short duration? Invest in an equity fund only if you are willing to stay on for a long term. For income and gilt funds, have at least a one-year perspective. But all this while keeping in mind your risk profile!

Selecting appropriate scheme :

Read the offer document carefully which contains essential details regarding the fund, such as , the type of scheme, name of the asset management company and price of units, among other things, investment objectives and investment procedure,

Glossary

Average Maturity

This term is used in the context of debt funds. It indicates the average life of the debt securities held in a fund's portfolio. If the fund has mainly invested in long-term debt papers, the average maturity will be high and vice versa. Generally, average maturity of a long-term income fund is higher than that of the short-term income fund. A fund having high average maturity is more prone to interest rate risk than the fund having low average maturity.

Capital Gains

Gain made by an investor when he sells an investment at a price higher than the acquisition price.
Capital Gains = sale price - purchase price

Credit Risk/ Default Risk

It is the risk associated with a debt instrument which arises out of the probability of the issuer of a fixed income security defaulting on payment of interest and repayment of principal. Generally, government securities are known to have low level of credit risk when compared to that of corporate bonds.

Downside Deviation

This tool measures the downside movement of the Fund NAV from a specified level. Some experts opine that downside deviation is a better tool for measuring volatility for an investor than standard deviation. This is because standard deviation includes both upside movement (profits) and downside movement (losses). Any investor always welcomes gains but averse to losses. Downside deviation only considers downward movement of the fund NAV, which represents true risk for an investor.

Downside Probability

It calculates the probability that the portfolio would get a negative return.
$$\text{Downside Probability} = \frac{\text{Total number of negative returns in a period}}{\text{Total number of returns in a period}}$$
While higher figure is considered bad, lower figure is considered favourable.
A statistical tool, frequency distribution method is generally used for computing the probability.

Duration

Duration measures the debt portfolio's sensitivity to changes in interest rate. In other words, it shows how much the value of a debt portfolio changes with a change in interest rates. It is calculated as the per cent change in the portfolio's price with a change in the yield of 1 per cent. Funds which mainly invest in long-term bonds have higher duration than funds investing in short-term papers. Therefore, short-term funds have low level of interest rate risk.

Expense Ratio

Expense ratio is defined as the ratio of total expenses of a fund to the net assets of the fund. An expense ratio of 1.45 means that the fund spends Rs. 1.45 per Rs. 100 of the net assets, towards operating expenses and management fees to service providers and AMC. Expense ratios are also sensitive to the size and type of fund. Larger the fund, lower the expense ratio. Equity funds have higher expense ratio than bond funds.

Hedging

It is a strategy used to off-set market risk whereby one position protects another. Typically, equity funds will use hedging when they expect that the prices will fall. It results in reduced equity exposure of the overall portfolio. Strategies adopted could be: Selling stocks futures, when the same stock is held in cash market; buying a put option when stock is held in the portfolio.

Indexation

Indexation means Adjusting the Long Term Capital Gains for inflation by applying an appropriate factor from Cost Inflation Index (notified by Govt), to the original investment. Indexation helps to lower capital gains and hence lower the tax. With the help of FMPs investors can get Indexation benefit, which is not available in case of fixed deposits. One needs to stay invested with that avenue for more than 365 days to avail the benefit of indexation.

Initial Issue Expenses

Expenses incurred towards sales, marketing and other promotional expenses of a new fund are known as initial issue expenses.

Interest Rate Risk

The change in the price of a debt security due to changes in the market interest rates is the interest rate risk. For debt oriented mutual fund schemes, this interest rate risk affects the NAV of the fund. A rise in the interest rates leads to a fall in the price of a fixed income security.

Loads

- ❖ **Front-End Load / Entry Load:** A commission or sales fee charged at the time of the initial purchase of a mutual fund. Due to this, the initial amount which finally gets invested in a fund is reduced to the extent of entry load.
- ❖ **Back-End Load / Exit Load :** It is a kind of redemption charge that an investor has to pay for withdrawing his money from the mutual fund. It is basically imposed to discourage investors from exiting the fund. This amount is deducted from the redemption proceeds.

- ❖ **Contingent deferred sales charge (CDSC):** Some funds may also charge different amounts of loads to the investors; depending upon how many years the investor has stayed with the fund. The longer the investor stays with the fund, lesser the amount of exit load is charged. This is called contingent load.

Long-term Capital Gains Tax

Tax that has to be paid on a capital gain, when the investor has held the investment for a period more than 365 days.

Net Asset Value

Net Asset Value is the market value of the assets of the scheme minus its liabilities. The per unit NAV is the net asset value of the scheme divided by the number of units outstanding on the Valuation Date.

Risk Adjusted Returns

Return alone should not be considered as the basis of measurement of the performance of a mutual fund scheme, it should also include the risk taken by the fund manager because different funds will have different levels of risk attached to them. The most important and widely used measures of risk adjusted performance are: Sharpe Ratio, Sortino Ratio, Treynor Measure, Jensen's Alpha and Fama.

Risk-Free Rate

Return generated on debt instruments having no credit risk. Generally returns on T-bills are used as risk-free rates.

Sharpe Ratio

It is one of the measures of showing risk-adjusted returns. This ratio shows excess returns generated by the fund on the total risk associated with it. If the ratio is 1.2, it means that the fund has undertaken one unit of total risk to generate 1.2 units of return (over and above the risk-free rate). Higher the ratio, the better it is. This ratio uses standard deviation to represent total risk associated with the fund.

Short-Term Capital Gains Tax

Tax that has to be paid on a capital gain, when the investor has held the investment for a period less than 365 days.

Shorting

Shorting involves selling a stock that the seller doesn't own. This strategy is adopted when there is an expectation of the market price going down, one should sell a future stock A.

Sortino Ratio

It is also one of the measures of showing risk-adjusted returns. This is a slightly advanced version of Sharpe Ratio where downside deviation is used to represent risk associated with the fund instead of Standard Deviation (used in Sharpe Ratio). If the ratio is 0.8, it means that the fund has undertaken one unit of downside risk to generate 0.8 units of returns in excess of the risk-free rate. Higher the ratio, the better it is.

Standard Deviation (SD)

SD measures the entire risk of a given fund; it provides good indication of volatility. The higher the SD, the greater the potential for volatility.

Securities Transaction Tax (STT)

Securities transaction tax is a tax which is payable by the investors or dealers for dealing in securities. In the context of mutual funds, STT at the rate of 0.25% is payable only at the time of redemption of an equity fund.

Unamortised Expenses

Generally, initial issue expenses are charged against the fund over a period. As per the latest regulation, SEBI allows closed-ended schemes to written off initial issue expenses over the life of the fund. As on any day, the extent of initial issue expenses which has not been written off is known as unamortized expense. For example, a fund incurs a 3% initial issue expenses. It has to charge 1% against the fund each year. Therefore, at the end of year two, 1% would be the remaining expense which has not been charged against fund. This is known as unamortized expense.

Research Team

Kirti Singh email : kirti.s@karvy.com
Chinmay email : chinmay@karvy.com
Sonika Dheer email : sonika.dheer@karvy.com
Ph : +91 40 23312454 Ext : 304



For more information call us on : 1800 425 82 83

Disclaimer

The information and views presented in this report are prepared by Karvy Stock Broking Limited. The information contained herein is based on our analysis and upon sources that we consider reliable. We, however, do not vouch for the accuracy or the completeness thereof. This material is for personal information and we are not responsible for any loss incurred based upon it. While acting upon any information or analysis mentioned in this report, investors may please note that neither Karvy nor Karvy Stock Broking nor any person connected with any associate companies of Karvy accepts any liability arising from the use of this information and views mentioned in this document.

This report is intended for a restricted audience and we are not soliciting any action based on it.