*International Journal of Social Science & Interdisciplinary Research*_______________________________ ISSN 2277 3630
IJSSIR, Vol. 2 (5), MAY (2013)
Online available at indianresearchjournals.com

PERFORMANCE EVALUATION OF SELECT EQUITY FUNDS IN INDIA

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ABSTRACT

There are around 58 Asset Management Companies (AMC) offering mutual funds in India. All these fund houses have several mutual fund schemes in each segment like equity, debt, gilt and liquid funds. Out of which equity segment is flourished and most of the investors are attracted towards equity mutual fund schemes. Because of availability of wide range of equity MF schemes in each AMC, it would be difficult for the investor to choose the best scheme.

It is appropriate to consider risk and return of each fund to yield better returns before taking investment decision. Hence Present study is an attempt of identifying risk and returns of equity funds and comparing the same with bench mark returns and peers to help mutual fund investors in choosing better funds as investment avenues

OBJECTIVES OF THE STUDY

• To analyse Risk and Returns of select equity funds
• To evaluate equity funds and suggest investors about outperforming funds.

METHODOLOGY

Nature and Collection of Data: The data required for the study relates information pertaining to the Net Asset Values of Select MF Schemes. Secondary data were obtained from published reports and websites like amfiindia and moneycontrol.

Tools of Analysis: Various statistical and evaluation techniques were used for analyzing the data. Some of the tools were Average Growth Rate (AGR), Compounded Annual Growth Rate (CAGR), Standard Deviation, Beta, Sharpe Index model, Treynor model etc.,
Period of the Study: The analysis of Mutual fund schemes was done between Dec, 2007 and Dec, 2012.

OBSERVATIONS & SUGGESTIONS

In short term perspective, stock markets may be volatile but in long term equity markets have huge potential to yield decent returns especially in emerging markets like India. With this view researcher attempted to find out returns of equity funds and index for medium to long term called for last 6 years. There is lot of volatility exist during period of study but mutual fund investors

were able to get decent returns. To find out returns two methods are popular mean value of annual returns and CAGR.
AGR and CAGR of TATA Dividend yield and ING Dividend Yield fund offered better returns to investors. In terms of Annual returns and CAGR all funds yields better returns than their bench mark NIFTY returns. Hence retail investors opting mutual funds are advised to stay in markets for long term periods rather than investing for 6 months or one year.
Sharpe and Treynor ratio of equity funds are far better than bench mark NIFTY. It is found that AGR, CAGR, Sharpe Ratio and Treynor Ratio of TATA Dividend yield and ING Dividend Yield fund are higher than their peers.

Annual Growth Rate, CAGR, Standard Deviation and Sharpe Ratio alone cannot reveal performance of mutual funds but together when these indicators are used to measure performance of mutual funds or portfolio, these indicators give some valuable inputs to investors to take investment decisions in mutual fund investment.

All equity diversified funds yielded better returns when compared to Benchmark returns but out of Ten equity funds TATA Dividend Yield fund and ING Dividend Yield fund yielded consistent superior returns than their peers. Hence investors are suggested to invest in these funds to yield better returns in long term horizon.

CONCLUSION
For small investors who can afford only small amounts of investments in stock markets, undoubtedly Mutual funds are best option but one has to bet in better yielded and outperformed funds rather than investing in low yielded funds and NFOs. Necessary evaluation has to be carried out to choose right fund to yield optimum returns. Indicators in present study may not be appropriate in all cases but are reliable in predicting future expected returns based on past performance of these funds in scientific manner. Mutual fund investors are also advised to stay on investing in funds for long term horizon (more than 5 years) and short term investment may lead to high volatility of returns (High risk) and even negative returns.

KEYWORDS: Performance Evaluation of Equity Funds in India, Performance Indicators of Equity funds, Risk evaluation of Equity funds in India, Risk & Returns of Equity Funds.

INTRODUCTION

Mutual fund is an important segment of the financial system. It is non-fund based special type of institution which acts as an investment conduit. It is a mechanism of pooling together the savings of large number of investor for collective investments with an avowed objective of attractive yields and appreciation in their value. The SEBI (Mutual Fund) Regulations 1996 defines a mutual fund as “a fund establishment in the form of a trust to raise money through the sale of units to the public or a section of the public under one or more schemes for the investing in securities, including money market instrument.”
Some basic types of mutual funds are:

- Liquid Funds
- Short term debt funds.

- Gilt funds
- Debt funds
- Balanced funds
- Index funds
- Diversified Equity funds
- Sectoral funds

There are around 58 Asset Management Companies (AMC) offering mutual funds in India. All these fund houses have several mutual fund schemes in each segment like equity, debt, gilt and liquid funds. Out of which equity segment is flourished and most of the investors are attracted towards equity mutual fund schemes. Because of availability of wide range of equity MF schemes in each AMC, it would be difficult for the investor to choose the best scheme. Present study focuses on identification of risk and returns of equity funds by applying performance evaluation techniques and suggests the investors about outperforming funds before making their investment decisions.

REVIEW OF LITERATURE: HISTORY OF INDIAN MUTUAL FUNDS

In 1963 the concept of Mutual Funds was introduced in India with the formation of Unit Trust of India. Till 1987, UTI continued to be the sole Mutual Fund, and then later some public sector banks and Life Insurance Corporation of India and General Insurance Corporation of India set up Mutual Funds. Only in 1993 the private players were allowed to open shops in the country. The history of Mutual Fund Industry in India can be better understood after dividing it into the following phases:

- **Phase I – Establishment and Growth of the Unit Trust of India – 1964 – 1987**: The Unit Trust of India enjoyed a complete monopoly when it was established in the year 1963 by an act of the parliament. UTI was set up by the Reserve Bank of India, and it continued to operate under the regulatory control of the RBI until the two were delinked in 1978, and the entire control was transferred to the Industrial Development Bank of India (IDBI). UTI launched its first scheme in 1964, named as Unit Scheme 1964 (US – 64), which attracted largest number of investor in any single investment scheme over the years. UTI launched more innovative schemes in 1970s and 80s to suit the needs of different investors. It launched ULIP in 1971, six more schemes between 1981 – 84, Children's Gift Growth Fund and India Fund (India's first offshore fund) in 1986, Master Share (India's first equity diversified scheme) in 1987, another Monthly Income Scheme (offering assured returns) during the 1990s.
- **Phase II – Entry of The Public Sector Funds – 1987 – 1993:** The Indian Mutual Fund industry witnessed a number of Public Sector players entering the market in the year 1987. In November 1987, SBI Mutual Fund from the State Bank of India became the first non – UTI Mutual Fund in India. SBI Mutual Fund was latter followed by Can Bank Mutual Fund, LIC Mutual Fund, Indian Bank Mutual Fund, Bank of India Mutual Fund, GIC Mutual Fund and PNB Mutual Fund.
- **Phase III – Emergence of the Private Sector Funds – 1993 – 1996:** Permission was given to the Private Sector funds including foreign fund management companies (most of them entering through joint ventures with Indian promoters) to enter the mutual fund industry in 1993. The entry of private players provided a wide range of choice to investors and brought more competition in the Industry. Private funds introduced innovative products, investment

techniques and investor – servicing technology. By 1994 – 95, about 11 private sector funds had launched their schemes.

- ❖ **Phase IV – Growth and SEBI Regulation 1996 – 2004:** The Mutual Fund Industry witnessed robust growth and strict regulation from the SEBI after the year 1996. The mobilization of funds and number of players operating within the industry reached new heights as investors started showing more interest in Mutual Funds. Investors' interests were safeguarded by SEBI and the Government offered tax benefits to the investors in order to encourage them. SEBI (Mutual Funds) Regulations, 1996 were introduced by SEBI that set uniform standards for all Mutual Funds in India. The Union Budget in 1999 exempted all dividend incomes in the hands of investors from Income Tax. Various Investor Awareness Programs were launched during this phase, both by SEBI and AMFI, with an objective to educate investors and make them informed about the Mutual Fund industry. In February 2003, the UTI Act was repealed and UTI was stripped of its special legal status as a trust formed by an Act of Parliament. The primary object behind this step was to bring all Mutual Fund players on the same level.
- ❖ **Phase V- Growth and Consolidation – 2004 onwards:** The industry has also witnessed several mergers and acquisitions recently, examples of which are acquisition of schemes of Alliance Mutual Fund by Birla Sun Life, Sun F & C Mutual fund and PNB Mutual Fund by Principal Mutual Fund. Simultaneously, more international mutual fund players entered India like Fidelity, Franklin Templeton Mutual Fund, etc. There were 56 funds at the end of December, 2012. This is a continuing phase of growth of the industry through consolidation and entry of new international and private sector players.

PERFORMANCE EVALUATION OF MUTUAL FUNDS

Literature on Mutual Funds' performance evaluation is enormous. A few research studies that have influenced the preparation of this paper substantially are discussed in this section.

Sharpe (1996) suggested a measure for the evaluation of portfolio performance. Drawing on results obtained in the field of portfolio analysis, economist Jack L. Treynor suggested a new predictor of Mutual Fund performer, one that differs from virtually all those used previously by incorporating the volatility of a fund's return in a simple yet meaningful manner. Jensen (1967) derived a risk-adjusted measure of portfolio performance (Jensen's alpha) that estimated how much a managers forecasting ability contributes to a fund's returns. As indicated by Stateman (2000), the e-SDAR of a fund's portfolio is the excess return of the portfolio over the return of the Benchmark Index, where the portfolio is leveraged to have the benchmark index's Standard Deviation. Rao et-al. conducted an empirical study on conditional performance of Indian Mutual Funds. the results suggested that the use of conditioning lagged information variables improves the performance of mutual fund schemes, causing alpha's to shift towards right and reduced the number of negative timing coefficient. Mishra et al. (2002) measured the mutual fund performance using lower partial movement. In their paper, measures of evaluating portfolio performance based on lower partial movement were developed. Risk from the lower partial movement is measured by taking into account only those states in which return is below a pre-specified "target rate" like risk-free rate. Fernandez (2003) evaluated index fund implementation in India. In her paper, tracking error of index funds in India was measured. The consistency and level of tracking errors obtained by some well-run index fund suggested that it is possible to attain low levels of tracking errors under Indian conditions.

Latest developments in Mutual Fund Industry:

- The Indian mutual funds retail market, growing at a CAGR of about 30%, is forecasted to reach US$ 300 Billion by 2015.
- Income and growth schemes made up for majority of Assets under Management (AUM) in the country. At about 84% (as on March 31, 2008), private sector Asset Management Companies account for majority of mutual fund sales in India.
- Individual investors make up for 96.86% of the total number of investor accounts and contribute 36.9% of the net assets under management.
- The Rs.7.2 trillion Indian Mutual Fund Industry is revisiting its business model to be in sync with the new norms put in place by the capital market regulator, the Securities and Exchange Board of India, or SEBI.
- India has 58 asset management companies (AMCs) and at least some of them are planning to start their own distribution business instead of selling funds through third-party distributors. Among other things, they plan to cut distributors' commission by 25-30 basis points (bps) and shift their focus from frequent churning of funds to managing money for the longer term. One basis point is one-hundredth of a percentage point.
- Out of the 32 crore employed Indians, only 2.5% are investors. Many investors, particularly youth mostly having the dispensable income opt for mutual funds to enter into the securities market indirectly.

Hence, potential investors in mutual funds need evaluation not only by financial institutions but also by academicians and retail investors so that they can make a right choice in their investment decisions.

NEED FOR THE STUDY

It is appropriate to consider risk and return of each fund to yield better returns before taking investment decision. Hence Present study is an attempt of identifying risk and returns of equity funds and comparing the same with bench mark returns and peers to help mutual fund investors in choosing better funds as investment avenues.

SCOPE OF THE STUDY

Present study focuses on equity segment and best rated mutual funds (10 funds of various fund houses) by CRISIL Ratings were chosen for the study. The study focuses on comparison of risk and return of each equity scheme with its peers (9 funds) and benchmark index to identify outperforming and underperforming mutual fund schemes.

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Period of the Study: The analysis of Mutual fund schemes was done between Dec, 2007 and Dec, 2012.

LIMITATIONS OF THE STUDY

- ✓ Present study is only confined to select equity funds. Results of the study cannot be generalized to all categories of mutual fund schemes.
- ✓ Present returns may not be guaranteed in future and investors have to consider other aspects before investing in equity mutual funds.

ANALYSIS AND INTERPRETATION

Annual returns of Equity funds are correlated with market returns. In 2008 NIFTY recorded negative returns as a result of Global Economic Crises, all funds followed the same trend. Net Asset Values (NAV) of all funds were plunged and shown negative returns.

Table1: Annual Growth Rate of Equity Funds and NIFTY

NAME OF THE FUND	Annual Growth Rate (AGR) of Select Equity Funds and Bench Mark Index					
	2007	2008	2009	2010	2011	2012
Birla Sunlife Gennext Growth	58.21	(48.00)	58.40	28.56	(15.76)	48.55
Franklin Indian Prima Plus	54.76	(46.54)	71.01	19.41	(17.20)	31.86
HDFC Growth Fund	67.90	(47.88)	73.93	26.98	(21.35)	28.75
ING Dividend Yield	70.63	(49.40)	101.24	27.24	(17.45)	26.57
Kotak Opportunities Fund	92.49	(56.16)	77.63	18.11	(23.45)	32.03
Principal Dividend Yield	65.04	(55.15)	77.47	23.73	(27.27)	43.57
Quantum Long-Term Equity	46.11	(46.24)	100.75	28.71	(20.72)	32.70
Reliance Equity Opportunities	47.70	(54.91)	104.71	30.68	(21.98)	48.61
TATA Dividend Yield Fund	76.44	(52.70)	87.91	31.88	(17.86)	34.73
UTI MNC Fund	32.65	(42.28)	81.72	26.47	(7.51)	31.99
NIFTY	54.72	(51.71)	75.51	18.78	(24.88)	27.96

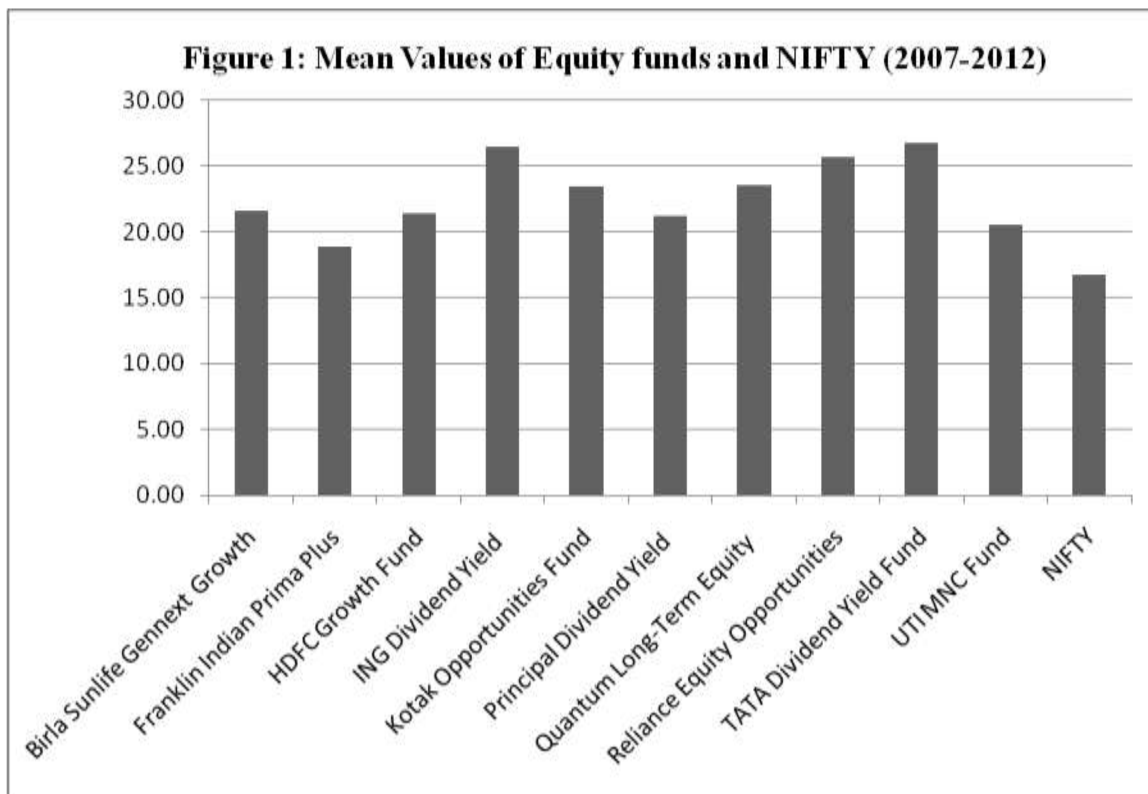
*values in brackets indicate negative returns

$$\text{Annual Growth Rate of MF} = \frac{\text{Current Year NAV} - \text{Previous Year NAV}}{\text{Previous year NAV}} \times 100 \quad (1)$$

In 2011 NIFTY recorded negative returns and all equity funds followed the same trend and yielded negative returns. In 2007 Kotak opportunities fund yielded 92.49 percent returns followed by TATA and HDFC funds with 76.44% and 67.90% respectively. In 2008 all funds and NIFTY yielded negative returns due to Global economic downturn. In 2011, ten out of ten

equity funds including NIFTY witnessed negative trend in returns. In 2009 and 2012 Reliance equity opportunities fund outperformed its peers. TATA dividend yield fund offered superior returns to investors in the year 2010.

Equity funds and NIFTY mean values have shown positive returns. Average returns of NIFTY and Franklin India prima face fund stood at 16.73 and 18.88 percent. Average returns of three out of ten funds are more than 25 percent. Returns of remaining funds are between 20 and 25 percent.



Standard deviation of NIFTY stood at 47.84, while standard deviation of mutual funds deferred from 41 to 57. Standard Deviation of UTI MNC Fund, Birla Sun Life and Franklin India Prima fund are between 40 to 45. HDFC growth fund returns are deviated to the extent of 48.24 percent during 6 years tenure. Three out of 6 funds returns are deviated from 50 to 55 percent. ING dividend yield, Reliance equity and Kotak Opportunities fund returns are highly deviated during the tenure of 6 years (55 to 60).

Table 2: Risk and Returns of Equity Funds and NIFTY				
NAME OF THE FUND	**AGR (%)**	**CAGR**	**SD**	**BETA**
Birla Sunlife Gennext Growth	21.66	13.13	44.07	1.00
Franklin Indian Prima Plus	18.88	10.74	44.17	1.06
HDFC Growth Fund	21.39	11.84	48.24	0.99
ING Dividend Yield	26.47	14.97	55.18	0.93
Kotak Opportunities Fund	23.44	10.18	57.17	1.16
Principal Dividend Yield	21.23	9.22	52.49	0.88
Quantum Long-Term Equity	23.55	13.48	51.79	0.99
Reliance Equity Opportunities	25.71	12.80	56.50	1.20
TATA Dividend Yield Fund	26.74	13.87	54.04	1.05
UTI MNC Fund	20.51	13.59	41.93	0.77
NIFTY	16.73	6.96	47.84	1.00

Compounded Annual Growth Rate of NIFTY is 6.96 percent. CAGR of 10 mutual funds are far better than bench mark NIFTY but KOTAK opportunities fund out performed in CAGR among 10 funds (14.97 percent), CAGR return of Principal Dividend Yield fund hammered with 9.22 percent.
Standard deviation and Beta indicates total risk of portfolio. Out of 10 equity funds, Standard Deviation and Beta value of Kotak Opportunities Fund and Reliance Equity Opportunities fund are high.

Table 3: Sharpe and Treynor Ratio of Equity Funds and NIFTY		
NAME OF THE FUND	**Sharpe Ratio**	**Treynor Ratio**
Birla Sunlife Gennext Growth	0.29	14.22
Franklin Indian Prima Plus	0.22	10.74
HDFC Growth Fund	0.26	12.39
ING Dividend Yield	0.32	15.32
Kotak Opportunities Fund	0.25	12.45
Principal Dividend Yield	0.23	11.22
Quantum Long-Term Equity	0.28	13.73
Reliance Equity Opportunities	0.30	14.53
TATA Dividend Yield Fund	0.33	15.70
UTI MNC Fund	0.27	13.70
NIFTY	0.16	7.73

*Risk free returns is taken as 9 percent per annum.

Sharpe ratio is an evaluation method which considers Returns of funds and Standard deviation of returns. Sharpe ratio of Tata Dividend yield fund and ING dividend yield fund (0.33 and 0.32) is higher than remaining funds. Sharpe ratio of Market Index NIFTY is 0.16. Sharpe ratio of mutual funds are higher than bench mark ratio. Sharpe ratio of 7 out of 10 mutual funds is above 0.25. Only two funds Sharpe ratio is between 0.20 and 0.25

Treynor ratio of Tata Dividend yield fund (15.70) and ING Dividend yield fund (15.32) is high. Treynor ratio of Bench mark is 7.73 while the ratio is above 10 for all remaining equity funds. Hence the performance of Equity funds is far better than that of NIFTY.

OBSERVATIONS & SUGGESTIONS

There exist correlation between annual returns of Individual fund and NIFTY returns. There was huge crash of equity markets in 2008. As a result of this NIFTY yielded negative returns in 2008 and all equity related funds followed the same pattern. In 2011 also equity fund returns followed NIFTY and have shown negative values of returns.

In short term perspective, stock markets may be volatile but in long term equity markets have huge potential to yield decent returns especially in emerging markets like India. With this view researcher attempted to find out returns of equity funds and index for medium to long term called for last 6 years. There is lot of volatility exist during period of study but mutual fund investors were able to get decent returns. To find out returns two methods are popular mean value of annual returns and CAGR.

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