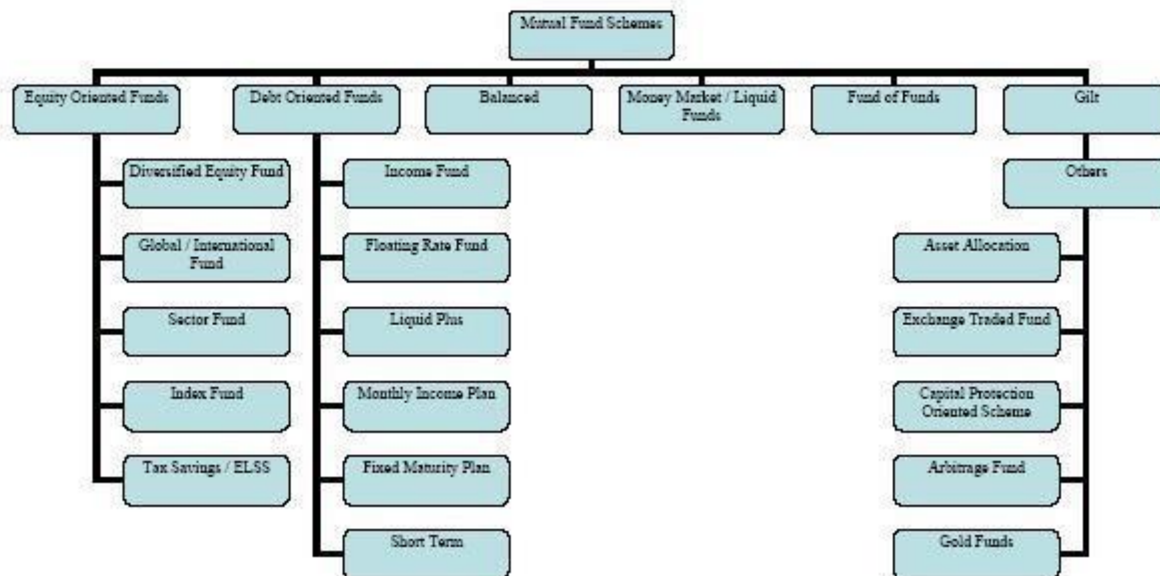
Type of Mutual Funds



Mutual Fund schemes can be classified into different categories and subcategories basedon their investment objectives or their maturity periods.

A) Classification based on maturity period:

Mutual Fund schemes can be classified into three categories based on their maturity periods.

Open-ended schemes

These are mutual fund schemes which offer units for purchase and redemption subscription on a continuous basis. In other words, the units of these schemes can be purchased or redeemed at any point of time at Net Asset Value (NAV) based prices. Also, these schemes do not have a fixed maturity period and an investor can redeem his units anytime.

Close-ended schemes

These are mutual fund schemes which have a defined maturity period e.g. 1 year / 5 years etc. The units of close ended scheme can be bought only during a specified period at the time of initial launch. SEBI stipulates that all close-ended schemes should provide for a liquidity window to its investors. These schemes are either required to be listed ona recognized stock exchange or provide periodic repurchase facility to investors.

Interval schemes

These schemes are a cross between an open-ended and a close-ended structure. These schemes are open for both purchase and redemption during pre-specified intervals (viz. monthly, quarterly, annually etc.) at the prevailing NAV based prices. Interval funds arevery similar to close-ended funds, but differ on the following points.

- They are not required to be listed on the stock exchanges, as they have an in-built redemption window.
- They can make fresh issue of units during the specified interval period, at the prevailing NAV based prices.
- Maturity period is not defined.

Classification based on investment objective

Apart from the above classification, mutual fund schemes can also be classified based on their investment objectives:

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Equity Oriented Schemes

Growth/ Equity oriented schemes are those schemes which predominantly invest in equity and equity related instruments. The objective of such schemes is to provide capital appreciation over the medium to long term. These types of schemes are generally meant for investors with a long-term outlook and with a higher risk appetite.

Debt Oriented schemes

The main objective of debt-oriented funds is to provide regular and steady income to investors. These schemes mainly invest in fixed income securities such as Bonds, Money Market Instruments, Corporate Debentures, Government Securities (Gilts) etc. Debt- oriented schemes are suitable for investors whose main objective is safety of capital along with modest growth. These funds are not affected because of fluctuations in equity markets. However, the NAV of such funds is affected because of change in the interest rate in the country.

Balanced Fund

Balanced Funds provide the best of both worlds i.e. equity and debt. The aim of the balanced funds is to provide both capital appreciation and stability of income in the long run. The proportion of investment made into equities and fixed income securities is pre- defined and mentioned in the offer document of the scheme. This type of scheme is a good alternative for pure equity-oriented products and provides an effective asset allocation tool. These schemes are suitable for investors looking for moderate growth. NAVs of such funds are generally less volatile in nature compared to pure equity funds.

Gilt Funds

These Funds invest exclusively in the dated securities issued by the government. These funds carry a very minimal risk because they are free of any default or credit risk. However, they do carry an interest rate risk as is the case with other debt products.

Money Market/ Liquid Funds
These are predominantly debt-oriented schemes, whose main objective is preservation of capital, easy liquidity and moderate income. To achieve this objective, liquid funds invest predominantly in safer short-term instruments like Commercial Papers, Certificate of Deposits, Treasury Bills, G-Secs etc..

These schemes are used mainly by institutions and individuals to park their surplus funds for short periods of time. These funds are more or less insulated from changes in the interest rate in the economy and capture the current yields prevailing in the market.

Fund of Funds
Fund of Funds (FoF) as the name suggests are schemes which invest in other mutual fund schemes. The concept is popular in markets where there are number of mutual fund offerings and choosing a suitable scheme according to one's objective is tough. Just as a mutual fund scheme invests in a portfolio of securities such as equity, debt etc, the underlying investments for a FoF is the units of other mutual fund schemes, either from the same fund family or from other fund houses.

New Product categories

Capital Protection Oriented schemes
The term 'capital protection oriented scheme' means a mutual fund scheme which is designated as such and which endeavours to protect the capital invested therein through suitable orientation of its portfolio structure. The orientation towards protection of capital originates from the portfolio structure of the scheme and not from any bank guarantee, insurance cover etc. SEBI stipulations require these type of schemes to be close-ended in nature, listed on the stock exchange and the intended portfolio structure would have to be mandatory rated by a credit rating agency. A typical portfolio structure could be to set aside major portion of the assets for capital safety and could be invested in highly rated debt instruments. The remaining portion would be invested in equity or equity related instruments to provide capital appreciation. Capital Protection Oriented schemes are a recent entrant in the Indian capital markets and should not be confused with 'capital guaranteed' schemes.

Gold Funds
The objective of these funds is to track the performance of Gold. The units represent the value of gold or gold related instruments held in the scheme. Gold Funds which are generally in the form of an Exchange Traded Fund (ETF) are listed on the stock exchange and offers investors an opportunity to participate in the bullion market without having to take physical delivery of gold.

Quantitative Funds
A quantitative fund is an investment fund that selects securities based on quantitative analysis. The managers of such funds build computer based models to determine whether or not an investment is attractive. In a pure "quant shop" the final decision to buy or sell is made by the model. However, there is a middle ground where the fund manager will use human judgment in addition to a quantitative model. The first Quant based Mutual

Fund Scheme in India, Lotus Agile Fund opened for subscription on October 25, 2007.

Funds Investing Abroad

With the opening up of the Indian economy, Mutual Funds have been permitted to invest in foreign securities/ American Depository Receipts (ADRs) / Global Depository Receipts (GDRs). Some of such schemes are dedicated funds for investment abroad while others invest partly in foreign securities and partly in domestic securities. While most such schemes invest in securities across the world there are also schemes which are country specific in their investment approach.

Real Estate Mutual Funds

Real Estate Mutual Funds or realty funds as they are popularly known are the latest addition to the mutual fund offerings in India. SEBI recently paved way for the launch of such products, by making amendments to its existing Regulations. However, real estate mutual funds are yet to be introduced in India by any asset management company. These schemes invest in real estate properties and earn income in the form of rentals, capital appreciation from developed properties. Also some part of the fund corpus is invested in equity shares or debentures of companies engaged in real estate assets or developing real estate development projects. REMFs are required to be close-ended in nature and listed on a stock exchange.

In addition to the above broad classification, mutual fund schemes can be further classified into sub-categories. Each of the sub-categories has a stated objective and caters to specific requirements of investors.

Investment options available to investors Growth Option

Under growth option, dividends are not paid out to the unit holders. Income attributable to the Unit holders continues to remain invested in the Scheme and is reflected in the NAV of units under this option. Investors can realize capital appreciation by way of an increase in NAV of their units by redeeming them.

Dividend Payout Option

Dividends are paid out to the unit holders under this option. However, the NAV of the units falls to the extent of the dividend paid out and applicable statutory levies.

Dividend Re-investment Option

The dividend that accrues on units under option is re-invested back into the scheme at ex-dividend NAV. Hence investors receive additional units on their investments in lieu of dividends.

What is Portfolio Revision ?

The art of changing the mix of securities in a portfolio is called as portfolio revision.

The process of addition of more assets in an existing portfolio or changing the ratio of funds invested is called as portfolio revision.

The sale and purchase of assets in an existing portfolio over a certain period of time to maximize returns and minimize risk is called as Portfolio revision.

Need for Portfolio Revision

- An individual at certain point of time **might feel the need to invest more**. The need for portfolio revision arises when an individual has some additional money to invest.
- **Change in investment goal** also gives rise to revision in portfolio. Depending on the cash flow, an individual can modify his financial goal, eventually giving rise to changes in the portfolio i.e. portfolio revision.
- Financial market is subject to risks and uncertainty. An individual might sell off some of his assets owing to fluctuations in the financial market.

Portfolio Revision Strategies

There are two types of Portfolio Revision Strategies.

1. **Active Revision Strategy**

   Active Revision Strategy involves **frequent changes** in an existing portfolio over a certain period of time for maximum returns and minimum risks.

   Active Revision Strategy helps a portfolio manager to sell and purchase securities on a regular basis for portfolio revision.

2. **Passive Revision Strategy**

   Passive Revision Strategy involves rare changes in portfolio only under certain predetermined rules. These predefined rules are known as formula plans.

   According to passive revision strategy a portfolio manager can bring changes in the portfolio as per the formula plans only.

What are Formula Plans?

Formula Plans are certain predefined rules and regulations deciding when and how much assets an individual can purchase or sell for portfolio revision. Securities can be purchased and sold only when there are changes or fluctuations in the financial market.

Why Formula Plans ?

- Formula plans help an investor to make the best possible use of fluctuations in the financial market. One can purchase shares when the prices are less and sell off when market prices are higher.
- With the help of Formula plans an investor can divide his funds into aggressive and defensive portfolio and easily transfer funds from one portfolio to other.

Aggressive Portfolio

Aggressive Portfolio consists of funds that appreciate quickly and guarantee maximum returns to the investor.

Defensive Portfolio

Defensive portfolio consists of securities that do not fluctuate much and remain constant over a period of time.

Formula plans facilitate an investor to transfer funds from aggressive to defensive portfolio and vice a versa.