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A Case Study on Mutual Funds (With Special Reference to Flexi Cap Fund)

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ABSTRACT

Mutual fund industry is growing with rapid pace globally and domestically; the global mutual fund assets market was valued at approximate USD 55.85 Trillion. And in India Assets under management (AUM) is approximately 71.23 trillion. Purpose of this study is to analyse the most popular scheme of mutual fund that is Flexi cap. And our study is based on two highly preferred flexi-cap fund i.e. HDFC Flexi cap Fund and Parag Parikh flexi cap fund.

***Keywords**: Flexi Cap, Assets Management Company (AMC), AUM, Mutual Funds, GDP.*

Introduction

The mutual fund industry is undergoing rapid transformation, with multiple developments taking place on the regulatory front, all ostensibly with the primary objective of protecting the investor and streamlining trading practices to bring in more efficiency. The market participants are in a watchful mood, waiting to see how the industry adapts to these changes.

Asset management companies are restructuring their business models in order to sustain the growth momentum of the industry, and provide for increased levels of operating efficiency and investor satisfaction. The industry continues to battle with the challenges of increasing investor awareness, low retail participation, high dependence on the corporate sector and increasing cost of operations. Mutual funds need to play an anchor role in directing the household savings into capital markets.

Assets under management as % of GDP are below 5% in India as compared to 70% in the US, 61% in France and 37% in Brazil. To increase penetration levels of mutual funds, the focus on inclusive growth has taken centre-stage, with all efforts by the regulator and fund houses being concerted in this direction.

It is therefore necessary to reach out to people in Tier II and Tier III cities, which are a daunting proposition considering costs of distribution and outreach and hence planned steps, need to be taken to attain some of the long term objectives of financial inclusion. The rising incomes in Tier II and Tier III cities would indicate the latent potential in these cities. It is a matter of channelizing their savings appropriately into mutual fund investments, for which investor education is a necessary first step.

This paper tried to find out the different aspect of mutual fund industry, at one hand it tried to find out whether mutual funds are preferred avenue for investment or not. And on other hand it tried to find out what are the factors responsible for selecting a suitable mutual fund scheme.

Mutual funds are in the form of trust basically known as Asset management committee, that managed the amount received from the investor and these pool of money Collected from Various investors, investing in different Types of mutual fund. Mutual fund is basically a basket of shares in which Fund Manager Invest Investors money.

On the functional basis mutual fund can be divided into open ended schemes, Close ended schemes and Interval schemes.

On the basis of portfolio classification mutual fund can we divide into income funds, growth fund, balance fund and money market funds,

On the basis of geographical classification, it can be classified into domestic funds offshore funds.

And on other parts there are so many other types of mutual funds like sectoral fund. Tax saving schemes Equity linked saving schemes Etc.

Review of Literature

Treynor and Mazuy (1966), Jensen (1968), Kon and Jen (1979), enriksson and Merton (1981), Chang and Lewellen (1984), Henriksson (1984) and Jagannathan and Korajczyk (1986). These studies have generally included that mutual fund management cannot consistently time the market or select under-priced securities. This has led to the conclusion that long-term individual mutual fund performance can best be described as random.

Harry Markowitz (1952)' provides a theory about how investors should select securities for their investment portfolio given beliefs about future performance.

He claims that rational investors consider higher expected return as good and high availability of those returns as bad. From this simple construct, he says that the decision rule should be to diversify among all securities, securities which give the maximum expected returns.

The Wharton (1962)' study investigated mutual fund performance in period t and the net inflow of money, or growth, in period t+ 1. The study found only a weak positive relationship for common stock funds The methodology used was a two-by- two contingency table that compared the lower half of a particular sample in performance with the lower half in growth, and conversely. This particular methodology has been criticized.

Smith (1978) called it "coarse" on the ground that it does not use the data in the most efficient manner and is therefore not a strong test of the performance-growth relationship.

William Sharpe (1964)' and John Lintner (1965 separately extend the work of Markowtiz. They show that the theory implies that the rates of return from efficient combinations of risky assets move together perfectly (will be perfectly correlated). This could result from their common dependence on general economic activity. If this is so, diversification among risky assets enables investors to escape from all risks except the risk resulting from changes in economic activity. Therefore, only the responsiveness of an asset return to changes in economic activity is relevant in assessing its risk. Investor only needs to be concerned with systematic risk [beta], not the total risk proposed by Markowtiz. This gave birth to the "Security Market Line" (SML).

In 1984; Chang and Eric Chieh developed an investment performance evaluation model in the multi-factor arbitrage pricing theory framework and then empirically compared and applied; Three investment performance evaluation methodologies examined are the multi-factor selectivity model, the single-factor selectivity model, and the single-factor selectivity and timing model. Several criteria for comparison are developed and the results are reported. The actual investment performances of a sample of mutual funds are evaluated according to these three methodologies. In general, they have provided evidences to show that both the multi- factor selectivity model and the single-factor selectivity and timing model are superior to the single-factor selectivity model. However, the major conclusion about the non- superiority of mutual funds investment performance drawn from the tests based on the single-factor selectivity model have not been altered when more sophisticated models are applied.

Swaminnthan and Bhaskaran (1994) made on attempt to focus on the implications of individual investor behavior for the pricing of close-ended funds and small firms. Specifically, they developed a two security, noisy rational expectations model of closed-end funds and compare its predictions to that of a model of investor sentiment.

Apar, Narayan R. and Madava, R. (2003) conducted are search on the performance evaluation of Indian mutual funds in a bear market. The period of study was September 1998 to April 2002 (bear period). They started with a sample of 269 open ended schemes (out of total schemes of 433) for computing relative performance index. Then after excluding the funds whose returns are less than risk-free returns, 58 schemes were used for further analysis. Mean monthly logarithmic) return and risk of the sample mutual fund schemes during the period were 0.59% and 7.10%, respectively, compared to similar statistics of 0.14% and 8.57% for market portfolio. The results of performance measures suggest that

most of the mutual fund schemes in the sample of 58were able to satisfy investor's expectations by giving excess returns over expected returns based on both premium for systematic risk and total risk.

Rao, D. N. (2006) classified 419 open-ended equity mutual fund schemes and analyzed the financial performance of selected open-ended equity mutual fund schemes for the period 1st April2005 to 31st March 2006 pertaining to the two dominant investment styles and tested the hypothesis whether the differences in performance was statistically significant or not. The variables chosen for analyzing financial performance were monthly compounded mean return, risk per unit return and Sharpe ratio. A comparison of the financial performance of the 21 Open-ended Equity growth plans and 21 Open-ended Equity dividend plans was made in terms of the chosen variables. The analysis indicated that Growth plans generated higher returns than that of Dividend plans but at a higher risk.

Kum Martin (October 2007) in his article, “Basics about Mutual Funds” discussed about different types of mutual funds. He stated that the equity funds involve just common stock investments. They are extremely risky but can end up earning a lot of money. He concluded that the low risk in investment will not earn a lot of returns. Mutual fund managers have to use various investment styles depending upon investor’s requirement.

Rao D.N. and Rao, S. B. (2009) analyzed the performance of the 47 Balanced and 72 Income Funds in terms of Return, Risk, Return per Risk and Sharpe ratio over the past three years (2006, 2007 and 2008) during which period the Indian Stock Market had witnessed much volatility. Further, the performance of these funds was compared with that of the Market and Benchmark Indices. The Null Hypotheses were rejected leading to the acceptance of Alternate Hypothesis in all the six cases, leading to conclude that Market out performed both the Balanced and Income Funds over Bull run and 3-year periods while both the funds outperformed the Market over Bear run period which confirms the popular belief of the Investors and Fund Managers in India.

Flexi Cap

A flexi cap scheme is an open-ended equity mutual fund that can invest in companies across all market capitalisation in large, mid and a small cap funds in this type of Scheme Fund manager have freedom and flexibility to allocate the investment Received from the investor Based on the market condition Company performance and available opportunities.

In this paper We are trying to throw the light on the investment through mutual funds. For this purpose, we are taking two Flex Cap funds, because now a day these funds are very popular because it gives freedom to the fund manager to invest in Different categories of fund Like large cap funds, Midcap funds and small cap funds.

One of the Restriction of this flexicap scheme is That at least 65% Of the total assets must be invested in the equities and equity related instruments

Beyond this It also gives the freedom to fund manager to invest in any proportion of these three types of funds.

We tried to Analyse these flexi cap funds by taking Two assets Management Company.

- Parag Parikh Assess Management Company
- HDFC Assets Management Company

In this paper we will analyse the returns of Flexi Cup Fund of these Assess Management company for 1 year, 2 Year, 3 Year 5 Year and 10 Year.

Analysis

Analysis is based on return given by these two funds in different years,

And these returns are analysed by the Standard deviation, Beta, Sharpe ratio, Treynor Ratio and Jensen Ratio.

The Treynor Measure

Developed by Jack Treynor, this performance measure evaluates funds on the basis of Treynor's Index. This Index is a ratio of return generated by the fund over and above risk saving rate of return (generally taken to be the return on securities backed by the government, as there is no credit risk associated), during a given period and systematic risk associated with it (beta). Symbolically, it can be represented as:

$$\textbf{Treynor Performance Index } (\textbf{TPI}) = \frac{\overline{R} - Rf}{\beta}$$

$\overline{R}$ = Expected return of the Fund

Rf = Risk free return

β = Systematic risk

All risk-averse investors would like to maximize this value. While a high and positive Treynor's Index shows a superior risk-adjusted performance of a fund, a low and negative Treynor's Index is an indication of unfavorable performance.

The Sharpe Measure

In this model, performance of a fund is evaluated on the basis of Sharpe Ratio, which is a ratio of returns generated by the fund over and above risk saving rate of return and the total risk associated with it.

According to Sharpe, it is the total risk of the fund that the investors are concerned about. So, the model evaluates funds on the basis of reward per unit of total risk. Symbolically, it can be written as:

$$\textbf{Sharpe Performance Index}(\textbf{SI}) = \frac{\overline{R} - Rf}{\sigma}$$

$\overline{R}$ = Expected return of the Fund

Rf = Risk free return

σ = Standard deviation

While a high and positive Sharpe Ratio shows a superior risk-adjusted performance of a fund, a low and negative Sharpe Ratio is an indication of unfavourable performance.

Standard Deviation

$$\sigma = \sqrt{\frac{(R - \overline{R})^2}{n-1}}$$

The most basic of all measures- Standard Deviation allows you to evaluate the volatility of the fund. It allows you to measure the consistency of the returns. Volatility is often a direct indicator of the risks taken by the fund. The standard deviation of a fund measures this risk by measuring the degree to which the fund fluctuates in relation to its mean return, the average return of a fund over a period of time.

A security that is volatile is also considered higher risk because its performance may change quickly in either direction at any moment.

Beta

$$\beta = \frac{(\overline{R} - Rf)}{(Rm - Rf)}$$

$\overline{R}$ = Expected return of the Fund

Rf = Risk free return

β = Systematic risk

Rm = Market Return

Beta indicates the level of volatility associated with the fund as compared to the benchmark. So quite naturally the success of Beta is heavily dependent on the correlation between a fund and its benchmark. Thus, if the fund's portfolio doesn't have a relevant benchmark index, then a beta would be grossly inadequate.

A beta that is greater than 1 means that the fund is more volatile than the benchmark, while a beta of less than 1 means that the fund is less volatile than the index. A fund with a beta very close to 1 means the fund's performance closely matches the index or benchmark.

Investors expecting the market to be bullish may choose funds exhibiting high betas, which increase investors' chances of beating the market. If an investor expects the market to be bearish in the near future, the funds that have betas less than 1 are a good choice because they would be expected to decline less in value than the index.

Jensen Ratio

Jensen ratio is also known as Jensen's Alpha Ratio is a major of mutual funds' performance that evaluates its risk adjusted returns against its expected return based on the capital assets pricing model. With the positive alpha indicating performance and negative alphas suggesting underperformance.

Parag Parikh Flexi Cap Scheme

(Data as on 31st march 2025)

Period Invested For	Annualised Return	Category Return
1 Year	9.56%	5.27%
2 Year	22.91%	20.85%
3 Year	22.47%	18.39%
5 Year	23.79%	21.74 %
10 Year	18.53%	15,23%

HDFC Flexi Cap Scheme

(Data as on 31st march 2025)

Period Invested For	Annualised Return	Category Return
1 Year	11.59%	5.27%
2 Year	27.08%	20.85%
3 Year	23.48%	18.39%
5 Year	30.36%	21.74 %
10 Year	17.34%	15.23%

Comparison of Different Ratio

(Data as on 31st march 2025)

Different Ratio	Category Result	Parag Pareek Flexi Cap	HDFC Flexi Cap
Standard Deviation	11.58	8.73	9.63
Beta	0.94	0.69	0.79
Sharpe Ratio	0.91	1.65	1.65
Treynor's Ratio	0.11	0.23	0.2
Jensen's Ratio	0.84	8.87	7.78

Result & Conclusion

- Parag Parikh Flexi cap Fund gave higher return in all the year category except 10-year category. When we analyse the data, we found that average return by this fund since Inception in approx. 20%.
- HDFC Flexi cap Fund gave higher return in all the year.
- In all the years analysed (except 10 year), HDFC flexi cap produced higher return than Parag Parikh Flexi cap fund.
- Standard deviation of HDFC flexi cap fund is higher, it means it is more volatile than Parag parikh flexi cap fund but less volatile than average category Fund.
- Beta of HDFC flexi cap fund is higher, it means it is more risky than Parag parikh flexi cap fund but less risky than average category Fund.
- Sharpe Ratio of HDFC flexi cap fund and Parag parikh flexi cap fund is same, it means both the funds have same risk adjusted return.
- Treynor Ratio of HDFC flexi cap fund and Parag parikh flexi cap fund is almost same, it means both the funds have same risk Volatility.

Website

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