What is exit load in mutual funds and how to calculate it?

When you apply for a loan, you are told about a foreclosure charge. It is a charge or penalty that you may have to pay to the lender if you wish to close your loan account before the end of its actual tenure. This is levied to discourage you from closing your loan account prematurely.

Similarly, when you invest in mutual funds, certain Asset Management Companies (AMCs) sometimes disallow redeeming your investments before a specific period. That is why there is an exit load in mutual funds. Let's understand what this exit load is and how it is calculated.

Is the exit load in mutual funds something worth knowing? Yes!

It is a well-known fact that a long-term investment in mutual funds helps create wealth. But the liquidity of certain mutual funds gives investors enough flexibility to withdraw their money whenever they need. So, to discourage them from pulling out their mutual fund investments at early stages, fund houses levy a fee known as the exit load. This usually ranges from 0.25% to 3% and varies across AMCs.

You must know that not all schemes of an AMC levy an exit load. Even if they do, the conditions may differ. Thus, an exit load is not uniform across schemes.

Usually, AMCs charge an exit load if you redeem your mutual fund investments within a year. Hence, to know what and how you will be charged, you must read the offer documents carefully before investing.

Math time! Here's how the exit load in mutual funds is calculated

The exit load is expressed as a percentage of the Net Asset Value (NAV) of a mutual fund scheme. The NAV is simply the value of each mutual fund unit. At the time of your mutual fund redemption, the AMC deducts the exit load from the NAV on that date and then credits the amount to your bank account accordingly.

Say, you have invested in a mutual fund scheme with a 1% exit load if redeemed within a year. However, you faced a financial emergency after two months and decided to redeem your mutual fund investment in the short term. Now, as per agreed terms and conditions, the AMC would charge the exit load.

So, if the NAV of your mutual fund at the time of redemption is Rs. 50, the exit load charged would be 1% of Rs. 50, i.e., Re. 0.5. The

AMC will deduct this amount from the NAV of your mutual fund before crediting the redeemed amount to your bank account.

The table below depicts the calculation of the exit load:

Amount invested in a mutual fund scheme	Rs. 50,000
NAV at the time of investment	Rs. 40
Units purchased	50000/40 = 1250
NAV at the time of redemption	Rs. 38
Exit load	1%
NAV after deducting the exit load	Rs. 37.62
Final redemption amount	Rs. 37.62 x 1250 = Rs. 47,025

Good news! It is possible to avoid the exit load in mutual funds

As you can see, an exit load can bring down your returns from your mutual fund investments. That is why it is advisable to not redeem your mutual funds until you achieve your long-term investment objective. Apart from avoiding the exit load, there is another reason to have a long-term investment perspective. It has been historically observed that equity mutual funds can provide inflation-beating returns over time.

Certain mutual funds are also suited for emergency, short-term and medium-term needs and can help you avoid the exit load. For instance, if you want to invest in mutual funds for building your emergency fund, you can opt for overnight funds. There is no exit load on overnight funds which means that you can redeem them the very next day of your investment without incurring any additional charge.

The final word

The exit load is a vital factor that you should keep in your mind while investing in mutual funds. By investing in the right mutual fund scheme and staying invested in it for a long period, you can avoid incurring an exit load on your redemption.