Cover Story

FOCUS IS BACK ON PERFORMANCE

Our Mutual Fund Roundtable in Mumbai last fortnight was attended by an expert panel comprising Nitin Rakesh, MD & CEO, Motilal Oswal MF; V.M. Sachdeva, CEO, Edelweiss MF; Nimesh Shah, MD & CEO, ICICI Prudential AMC; Waqar Naqvi, chief executive, Taurus MF; and Nikhil Johri, MD, BNP Paribas MF. It was moderated by *OLM*'s Kundan Kishore

KUNDAN KISHORE Has the new transaction charge helped the mutual fund industry regain its momentum? Is this a game changer?

WAQUAR NAQVI It is not a game changer, but it is a positive change. It covers a small part of the expenditure that a distributor incurs. It has not really done wonders for the industry, though it conveyed more of a psychological feeling to the distributors that they are not exactly being sidelined or being overlooked. However, the imposition of transaction charge came in when the market environment was not conducive. But it's a fair step.

NIMESH SHAH It's a step in the right direction. In the first year, the investor was charged 2.25 per cent up front, plus almost 2 per cent as yearly management fee, totaling 4.25 per cent for the first year. Now the charges are only 2 per cent, which makes it one of the best products. The

biggest change that has happened in the last three years is that, there is no business if you are not doing a good job for the final investor. In the last 10 months, an overwhelming amount of money has come in the top 10 performing schemes. Now, there is only one way to remain in business, my schemes have to perform for the final investor.

NITIN RAKESH It is not something that is going to revolutionise sales, or get distributors charged up to bring clients in; but sentimentally a step that says we know you have to be compensated. We have to also keep in mind that all these changes are happening at a time when the environment for equity has been the lowest. Post-2007, it has never really recovered. So, whether this will have an impetus or not remains to be seen.

NIKHIL JOHRI There was a lot of speculation before the announcement that there may be a substitute for entry load and, therefore, the immediate reaction from a lot of distributors was that it is probably not enough. But, as everyone has said, it is a directional change that the regulator has shown and the fact that the regulator is willing to recognise the interest of all constituents of the market.

KUNDAN KISHORE Why is mutual fund penetration concentrated in only a few large cities?

NIMESH SHAH It is not the presence that matters. Most asset management companies (AMC) would be present in over 100-plus cities. But are there enough distributors in a small city who want to sell mutual funds? The market decides everything and, incidentally, it has selected the top 10 performing funds to invest more money. It is not that availability is an issue, we are not shrinking our distribution, but the inflows are only from the top cities. High net worth individuals (HNI) are coming into the mutual fund industry, because below a certain ticket size, the business might not be viable for distributors. In smaller cities, perhaps, the distributors are not making a living out of selling mutual funds.

NIMESH SHAH
Managing Director & CEO, ICICI Prudential AMC

We need to bring in alignment of all the stakeholders—the manufacturers, the distributor and the final investor. Today, ...the manufacturer and the investors make money

NIKHIL JOHRI One of the big factors is that the levels of financial literacy are better in the bigger cities than in the smaller cities. Therefore, as an industry, we need to spread financial literacy to smaller cities. Hence, the industry is putting a lot of effort in investor awareness programmes.

More people are putting money in capital protection schemes and debts

NITIN RAKESH Concentration of wealth is in some of the bigger cities. It is going to take some time till that same quality of intermediation and advisory is available in smaller cities. But, clearly we are seeing a broader penetration—five years ago contributions from large cities was 80 per cent, but today it is down to 70 per cent. All said and done, only one in five Indians has a bank account. Unless you have a bank account, you can't really buy a financial product. PAN card is another limiting factor and so is know your customer (KYC).

VIKAAS M. SACHDEVA If you analyse the data that is available, in terms of penetration, you will find that a lot more people are putting money in capital protection schemes and debt because that is what they understand. Equity inherently is a systematic investment plan (SIP), and SIP ticket sizes are far too nominal.

Photos: PRIYAM DHAR

Clockwise (from left): Nitin Rakesh, managing director & CEO, Motilal Oswal Mutual Fund; V.M. Sachdeva, chief executive officer, Edelweiss Mutual Fund; Nimesh Shah, managing director & CEO, ICICI Prudential AMC; Kundan Kishore, special correspondent, OLM; Waqar Naqvi, chief executive, Taurus Mutual Fund; Nikhil Johri, managing director, BNP Paribas Mutual Fund; and Clifford Alvares, deputy editor, OLM; at the OLM Mutual Fund Roundtable

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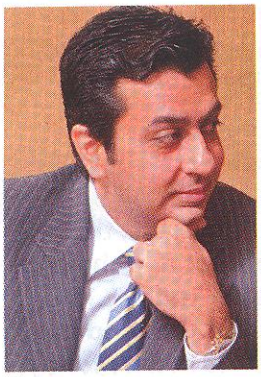


NITIN RAKESH
Managing Director & CEO, Motilal Oswal Mutual Fund

More and more people will realise that this is a stronger business than they had anticipated. Penetration should increase rapidly for various reasons such as tax incentives...

KUNDAN KISHORE What will be the future of the mutual fund industry in terms of players and investors?

NIMESH SHAH We need to bring in alignment of all the stakeholders—the manufacturers, the distributor and the final investor. Today, the structure is such that the manufacturer and the final investors will make money if they stay invested in a mutual fund for a longer period of time.

WAQAR NAQVI One has to understand the conditions of the Indian environment. Performance is important. More education and more literacy is required. Given that, the distribution set-up in India is at a nascent stage. It has to undergo a lot of maturity, which it is, and guys who have been there are leading that change.

NIKHIL JOHRI Globally, it has shown that it takes several decades for the industry to mature. The industry will continue to witness several regulatory changes, some changes in tax laws, etc. Some fiscal incentives are needed to make it attractive for investors in order to build the industry. I am a firm believer in financial literacy. Efforts are being made, but a lot more needs to be done by all of us. Lastly, some fundamental changes in the outlook for long-term savings has to come into the industry, like pension money.

NITIN RAKESH You will see a change because more and more people will realise that this is a stronger business than they had anticipated. Penetration should increase rapidly for various reasons, such as tax incentive or opening up insurance assets to mutual funds.

VIKAAS M. SACHDEVA One of the things which will be a catalyst to future growth would be technology. Five years back, the number of people logging onto Netbanking and doing transactions, vis-a-vis what is happening today, was completely different. In fact, Association of Mutual Funds in India (AMFI) is bringing out an MF utility platform to reach out to customers and distributors. It will be an extremely powerful tool once it is launched, which will make it that much easier for a customer or distributor to transact.

KUNDAN KISHORE Now, we have many schemes. Over a period of time, will there be fewer schemes?

WAQAR NAQVI There are large-, mid- and small-cap funds and a couple of other schemes, but beyond that it is a diversification for the sake of diversification. I don't find

YOU ASKED, THEY REPLIED

Why do mutual funds charge trail commissions for investors who directly go with the AMC?
—ANAND BALAKRISHNAN

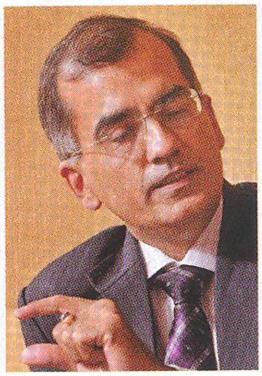
WAQAR NAQVI
Look at the expenditure of a scheme. If I am charging 1.75 per cent and there is a certain amount I keep as management expenses and as scheme accruals. We maintain scheme accounts. For a scheme that has more than 1 million folios, maintaining individual accounts are going to be difficult. There is no way one can segregate the accounts for every investor. The other thing is that this charge is a very minuscule percentage.

NITIN RAKESH
Mutual fund is a co-mingled pool of assets. We can only charge certain expense ratio and that includes all costs.

NIMESH SHAH
He should not worry about what we are charging him. For getting all the expertise of a mutual fund, he is paying 1.75 per cent or 1.8 per cent as management fee, which is the expense ratio. After the expense, he should look at how much he has earned and whether the fund has beaten the benchmark.

If we compare returns in liquid funds for retail and institutional investors, it is always better for institutional investors. Why is it so?
—PRAKASH SWARNAKAR

NIKHIL JOHRI
The difference is the expense ratio. The actual expenses charged by the mutual funds to the institutional plans are lower than the retail plan. The reason for that is the cost of acquisition of a retail customer in the form of distribution costs is much higher.



V.M. SACHDEVA
Chief Executive Officer, Edelweiss Mutual Fund

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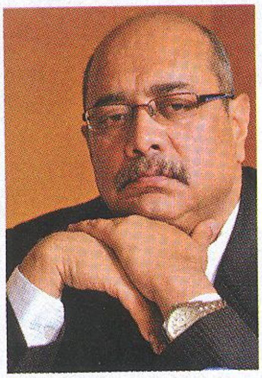
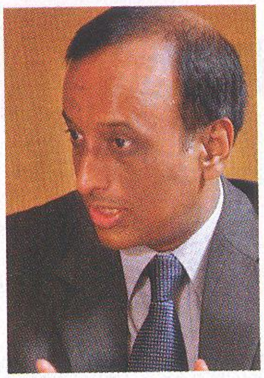


WAQAR NAQVI
Chief Executive, Taurus Mutual Fund

Performance is important. More education and more literacy is required. The distribution set up in India is at a nascent stage and has to undergo a lot of maturity



NIKHIL JOHRI
Managing Director, BNP Paribas Mutual Fund

Globally, it has been seen that it takes several decades for the industry to mature...You need some fiscal incentives to make it attractive for the investors to look at this

space for the existence of such schemes, barring a few.

NIKHIL JOHRI A lot of global funds will come in, however there needs to be a consolidation for similar schemes and that has already started happening.

KUNDAN KISHORE Do you see the distribution base shrinking, going ahead?

NITIN RAKESH The serious, dedicated and committed professionals have stuck on and they will continue to toil away because that is their primary business. So, survival of the fittest is at play here and, eventually, the market will determine who wants to stay in the business.

NIKHIL JOHRI As regulatory expectations increase over how distributors are functioning, they will need to be conscious of compliance; that comes with a cost. All the steps are moving in the direction of making this a profession that is more respectable and, some players who thought it was very easy to recommend and earn some money are going to face tough times ahead.

KUNDAN KISHORE Mutual funds are the sixth most preferred investment vehicle. What will prompt the Indian investor to migrate to mutual funds?

NIMESH SHAH If you see the last 6-9 months, it has already happened. Equity as a sector is not doing very well, but AMCs are trying to educate the people on what is a debt mutual fund, an accrual product or duration product. A lot needs to be done and it is happening.

VIKAAS M. SACHDEVA If you want to open an FD, how long does it take? Five minutes? If you want to invest in MFs, how much time does it take? A lot more. The processes has to be streamlined to be very easy, the product is only the end result. Secondly, you invest because you are comfortable, not because you are convinced. If somebody is comfortable with higher risk-higher return, that's his choice.

WAQAR NAQVI Financial literacy is paramount and, then, you need conviction and comfort to be with MFs. For some, it may happen, for others it might not happen. But this change can happen with youngsters faster.

NITIN RAKESH If you look at households, you first buy real estate and then buy gold, because it is a consumption product. So, people who have had a pleasant experience will be converts, who didn't, would take some more time.

VIKAS SACHDEVA A recent survey said that people invest in real estate and gold more because, implicitly, they believe there is capital appreciation. Similarly, over a period of time, people will realise that if you stay in financial products like MFs, you will get a lot of wealth.

KUNDAN KISHORE What are the emerging trends of ETFs?

> Eventually market will determine who wants to stay in the business

NITIN RAKESH If you have a view on asset allocation and you want to allot a certain amount of money to passive investments, you use an ETF to allocate money. And, the more asset allocation products we can create, the more portfolios we will be able to create by using a line of instruments of beta products. But, it's very early in the game. In most developed markets it has taken 20 years for ETFs to get to where they are. Almost 30 per cent of assets in the US, for example, are in index or ETF. At present, we have 1.5-2 per cent of assets in ETF. So, even if we can go up to 5 per cent or 10 per cent, we will see growth. This is a simple basic premise to see why ETF makes sense from an asset allocation point of view for long-term investors.

NIMESH SHAH When we look at ETF's, we see that in the last 10 years in the US, markets have brought more money. A lot of fund managers, were able to beat benchmarks, but they could not justify the expenses they were charging. You can justify an expense of 2 per cent if you are going to give 12-15 per cent returns. That is not happening in the US and that is why passively-managed funds have done so well in the US. In India, the growth is going to be 6-7 per cent. Therefore, we are talking of a nominal growth of 12-13 per cent in risk assets. If that is the scenario, actively managed funds, after taking care of the expenses, can give positive returns, vis-a-vis the benchmark. Then it would take that much more time. We have to be really bad for ETFs to do really well. ❐