

Chapter 11: Mutual Fund Scheme Performance

11.1 Benchmarks and Performance

Benchmarks and Performance:

Benchmarks are standard indices or standards used to measure the performance of mutual funds. They provide a reference point for evaluating the returns of a fund. Common benchmarks include indices like the Nifty 50, Sensex, and others. The performance of a mutual fund is often compared against these benchmarks to determine if the fund has outperformed or underperformed the market.

Quiz Questions:

1. What is a benchmark in the context of mutual fund performance?
 - Answer: A benchmark is a standard index used to measure the performance of mutual funds.
2. Why are benchmarks important for mutual fund performance evaluation?
 - Answer: Benchmarks provide a reference point to determine if a mutual fund has outperformed or underperformed the market.

11.2 Price Return Index or Total Return Index

Price Return Index vs. Total Return Index:

- Price Return Index (PRI): Measures the price appreciation of the stocks in the index. It does not account for dividends paid by the companies.
- Total Return Index (TRI): Includes both the price appreciation and dividends paid by the companies in the index. TRI gives a more accurate representation of the total returns from an investment.

Quiz Questions:

1. What does the Price Return Index measure?
 - Answer: The Price Return Index measures the price appreciation of the stocks in the index.
2. How does the Total Return Index differ from the Price Return Index?

- Answer: The Total Return Index includes both price appreciation and dividends, providing a more accurate measure of total returns.

11.3 Basis of Choosing an Appropriate Performance Benchmark

Choosing an Appropriate Performance Benchmark:

The selection of an appropriate benchmark depends on several factors:

1. Investment Objective: The benchmark should align with the fund's investment objective.
2. Asset Class: The benchmark should represent the same asset class as the fund.
3. Geographical Focus: The benchmark should match the geographical focus of the fund.
4. Risk Profile: The benchmark should have a similar risk profile to the fund.

Quiz Questions:

1. What factors should be considered when choosing a performance benchmark for a mutual fund?
 - Answer: Factors include investment objective, asset class, geographical focus, and risk profile.
2. Why is it important to align the benchmark with the fund's investment objective?
 - Answer: Aligning the benchmark with the investment objective ensures a relevant comparison of performance.

11.4 Benchmarks for Equity Schemes

Benchmarks for Equity Schemes:

Equity mutual funds typically use stock market indices as benchmarks. Common benchmarks for equity schemes include:

1. Nifty 50: Represents the performance of 50 large-cap stocks in India.
2. BSE Sensex: Comprises 30 well-established and financially sound companies listed on the Bombay Stock Exchange.

Quiz Questions:

1. Name two common benchmarks used for equity schemes.
 - Answer: Nifty 50 and BSE Sensex.

2. What does the Nifty 50 index represent?
 - Answer: The Nifty 50 index represents the performance of 50 large-cap stocks in India.

11.5 Benchmarks for Debt Schemes

Benchmarks for Debt Schemes:

Debt mutual funds use fixed-income indices as benchmarks. Common benchmarks for debt schemes include:

1. CRISIL Composite Bond Fund Index: Represents the performance of Indian bond markets.
2. ICRA Composite Bond Fund Index: Another popular benchmark for debt funds in India.

Quiz Questions:

1. Name two common benchmarks used for debt schemes.
 - Answer: CRISIL Composite Bond Fund Index and ICRA Composite Bond Fund Index.
2. What does the CRISIL Composite Bond Fund Index represent?
 - Answer: It represents the performance of Indian bond markets.

11.6 Benchmarks for Other Schemes

Benchmarks for Other Schemes:

Other types of mutual fund schemes, such as hybrid funds or sectoral funds, use specific benchmarks that align with their investment strategy. Examples include:

1. Hybrid Funds: May use a combination of equity and debt indices.
2. Sectoral Funds: Use sector-specific indices like the Nifty IT Index for technology sector funds.

Quiz Questions:

1. What type of benchmarks might a hybrid fund use?
 - Answer: A combination of equity and debt indices.
2. Give an example of a benchmark for sectoral funds.

- Answer: The Nifty IT Index for technology sector funds.

11.7 Quantitative Measures of Fund Manager Performance

Quantitative Measures of Fund Manager Performance:

Various metrics are used to evaluate the performance of fund managers, including:

1. Alpha: Measures the fund's excess return over its benchmark.
2. Beta: Measures the fund's sensitivity to market movements.
3. Sharpe Ratio: Measures risk-adjusted returns, indicating the return per unit of risk.
4. Treynor Ratio: Similar to the Sharpe Ratio but uses beta as the risk measure.

Quiz Questions:

1. What does the Sharpe Ratio measure?
 - Answer: The Sharpe Ratio measures risk-adjusted returns, indicating the return per unit of risk.
2. How is alpha used in evaluating fund manager performance?
 - Answer: Alpha measures the fund's excess return over its benchmark, indicating the value added by the fund manager.

11.8 Tracking Error

Tracking Error:

Tracking error measures the deviation of a fund's performance from its benchmark. A lower tracking error indicates that the fund's performance is closely aligned with the benchmark, while a higher tracking error indicates greater deviation.

Quiz Questions:

1. What does tracking error measure?
 - Answer: Tracking error measures the deviation of a fund's performance from its benchmark.
2. What does a low tracking error indicate?
 - Answer: A low tracking error indicates that the fund's performance is closely aligned with the benchmark.

11.9 Scheme Performance Disclosure

Scheme Performance Disclosure:

SEBI mandates mutual funds to disclose their performance regularly to ensure transparency.

Key requirements include:

1. Periodic Reporting: Funds must report performance quarterly and annually.
2. Comparison with Benchmarks: Performance must be compared with relevant benchmarks.
3. Risk Disclosure: Funds must disclose the risk factors associated with their schemes.

Quiz Questions:

1. How often must mutual funds report their performance?
 - Answer: Mutual funds must report their performance quarterly and annually.
2. Why is it important for mutual funds to compare their performance with benchmarks?
 - Answer: Comparing performance with benchmarks helps investors understand how the fund is performing relative to the market.

By understanding these key aspects of mutual fund scheme performance, mutual fund distributors can provide valuable insights and guidance to investors, helping them make informed investment decisions.