TYPES OF MUTUAL FUND IN INDIA

Chapter 10

Mutual funds are popular investments because of their ease, flexibility and diversification benefits. The best part of mutual funds is that they provide investment opportunities for all kinds of investors. Currently, there are over 44 registered mutual funds in India, offering different schemes to satisfy the dynamic needs of diverse investors.
The different types of mutual funds available can be classified broadly based on structure, asset class, and investment goals. Going a step further, funds can also be categorized based on risk.

1. Structure of Mutual Funds

Based on the ease of investment, mutual funds can be:

• Open-ended funds:

These funds do not limit when or how many units can be purchased. Investors can enter or exit throughout the year at the current net asset value. Open-ended funds are ideal for investors seeking liquidity.

• Close-ended funds:

Close-ended funds have a pre-decided unit capital amount and also allow purchase only during a specified period. Here, redemption is bound by the maturity date. However, to facilitate liquidity, schemes trade on stock exchanges.

• Interval funds:

A cross between open-ended and close-ended funds, interval mutual funds permit transactions at specific periods. Investors can choose to purchase or redeem their units when the trading window opens up.

2. Mutual Fund Asset Class

Depending on the assets they invest in, mutual funds are categorized under:

• Equity funds:

Equity funds invest money in company shares, and their returns depend on how the stock market performs. Though these funds can give high returns, they are also considered risky. They can be categorized further based on their features, like Large-

Cap Funds, Mid-Cap Funds, Small-Cap Funds, Focused Funds, or ELSS, among others. Invest in equity funds if you have a long-term horizon and a high-risk appetite.

• Debt funds:

Debt funds invest money into fixed-income securities such as corporate bonds, government securities, and treasury bills. Debt funds can offer stability and a regular income with relatively minimum risk. These schemes can be split further into categories based on duration, like low-duration funds, liquid funds, overnight funds, credit risk funds, gilt funds, among others.

• Hybrid funds:

Hybrid funds invest in both debt and equity instruments so as to balance out debt and equity. The ratio of investment can be fixed or varied, depending on the fund house. The broad types of hybrid funds are balanced or aggressive funds. There are multi asset allocation funds which invest in at least 3 asset classes.

• Solution-oriented funds:

These mutual fund schemes are for specific goals like building funds for children's education or marriage, or for your own retirement. They come with a lock-in period of at least five years.

• Other funds:

Index funds invest based on certain stock indices and fund of funds are categorized under this head.

3. Mutual Funds based on Investment Goals

You can also choose a fund based on your financial objective:

• Growth funds:

Funds that invest primarily in high-performing stocks with the aim of capital appreciation are considered growth funds. These funds can be an attractive option for investors seeking high returns over a long period.

• Tax-saving Funds (ELSS):

Equity-linked saving schemes are mutual funds that invest mostly in company securities. However, they qualify for tax deductions under Section 80C of the Income Tax Act. They have a minimum investment horizon of three years.

• Liquidity-based funds:

Some funds can be categorized based on how liquid the investments are. Ultra-short-term and liquid funds, are ideal for short-term goals, while schemes like retirement funds have longer lock-in periods.

• Capital protection funds:

These funds invest partially in fixed income instruments and the rest into equities. This could ensure capital protection, i.e., minimal loss, if any. However, returns are taxable.

• Fixed-maturity funds (FMF):

These funds route money into debt market instruments, which have either the same or a similar maturity period as the fund itself. For instance, a three-year FMF will invest in securities with a maturity of three years or lower.

• Pension Funds:

Pension funds invest with the idea of providing regular returns after a long period of investment. They are usually hybrid funds that give low but have potential to provide steady returns in future.

4. Risk appetite

Investors may also choose to invest in mutual funds depending on their individual risk appetite. Very-low-risk and low-risk funds are usually short-term investments (liquid or ultra-liquid funds) that attempt to hedge market risk. However, the returns they generate are also low.
Medium-risk funds, like hybrid funds, invest a portion in debt instruments to balance risk while high-risk funds have large equity exposure. Usually, the higher the risk, more the possibility of high returns.

Every mutual fund must disclose its risk exposure via a risk-o-meter that investors can check to decide if it lines up with their risk capacity.

Takeaway
Understanding different mutual fund categories can make it simpler for you to align with individual financial goals. As an investor, you can compare your needs with the fund objective and invest accordingly to make the most of your money.

Use the SIP calculator online to calculate your returns and your monthly investments for mutual fund investment options.
NEXT TO COME: HOW TO SELECT MUTUAL FUNDS: MUTUAL FUND SELECTION GUIDE