

A BEGINNER'S GUIDE TO MUTUAL FUNDS



It is a difficult task to choose funds from close to 800 open ended mutual fund schemes spread across 15 odd categories and 42 fund houses (as of April 2014). Since the choice is vast, one needs to have basic knowledge about mutual funds and their selection to make an informed investment decision. To trim the choice, one may also refer to mutual fund rankings published regularly by various independent research houses and rating agencies or even approach a professional financial distributor to select funds on your behalf.



About Mutual Fund Rankings – The same are published either as star rankings or linear rankings. Both rankings are available on a 5-point scale with 5-star being the best rank in case of star rankings and Fund Rank 1 being the best in case of linear rankings. Both the rankings are provided in clusters where more than one fund may be ranked in each of the 1-5 point ranking scale. Most rankings are refreshed every quarter.

The ranking methodologies typically short-list the funds to be ranked by age of the scheme and its AUM. The shortlisted schemes are then ranked across different parameters ranging from returns and volatility (risk) to portfolio attributes as well as some qualitative factors. Each parameter has a weight which varies from category to category. The score of each fund at a parameter level is adjusted by the parameter's weight and aggregated to arrive at a composite weighted average score across parameters for each fund. The fund with the highest weighted average score in each category gets the top rank and so on. However rankings may not be the last word on mutual funds but only serve as a guide. One may still need to take subjective calls for selecting the final set of funds to include in one's portfolio. It is also important to regularly monitor the performance of selected funds vis-à-vis their category peers and benchmark indices.

Choosing funds is the first step before creating portfolios suitable for a wide variety of uses ranging from short-term requirements to medium and long term goals like buying a house, children's post-graduation or even for retirement.

SUMMARY

It is a difficult task to choose funds from a multiplicity of mutual fund schemes across categories and fund houses. Hence it is important to have basic knowledge about mutual funds and their selection to make an informed investment decision. One may also refer to mutual fund rankings published by various independent research houses and rating agencies or even approach a professional financial distributor for assistance in selecting funds. However rankings may not be the last word on mutual funds but only serve as a guide.

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