What is Security Analysis?

Security analysis refers to the fundamental, technical or quantitative techniques applied on various tradable financial instruments (assets with some financial value) in order to determine the fair value of assets and help investors make better investment decisions.

- To value financial instruments like equity, debt, and warrants of a company.
- To use publicly available information. Use of insider information is unethical and illegal.
- Security analysts must act with integrity, competence, and diligence while conducting the investment profession.
- To use various analytical tools this includes fundamental, technical and quantitative approaches.
- Security analysts should place the interest of clients above their personal interest.

#1 – Box IPO Analysis

For Box IPO valuation, I have used the following approaches –

1. Relative Valuation – SAAS Comparable Comps
2. Comparable Acquisition Analysis
3. Valuation using Stock-Based Rewards
4. Valuation cues from Box Private Equity Funding
5. Valuation cues from DropBox Private Equity Funding Valuation
6. Box DCF Valuations

Box Inc Valuations	2015		
	Pessimistic	Base	Optimistic
EV/Revenue Implied	5.0x	7.1x	10.0x
Box Revenue	248,384	248,384	248384
EV	1,241,920	1,762,570	2,483,840
Debt	32,514	32,514	32,514
Cash	277,987	277,987	277,987
Equity Value	996,447	1,517,097	2,238,367
Price Per Share	**11.02**	**16.77**	**24.74**

#2 – Alibaba IPO Analysis

In analyzing the Alibaba IPO, I primarily used the discount Cash Flow technique

You can learn more about how I went about doing a security analysis of Alibaba from this article – Alibaba Valuation Analysis

Below are the Top 3 Types of Security Analysis. The securities can broadly be classified into equity instruments (stocks), debt instruments (bonds), derivatives (options) or some hybrid (convertible bond). Considering the nature of securities, security analysis can broadly be performed using the following three methods:-

Popular Course in this category

#1 – Fundamental Analysis

This type of security analysis is an evaluation procedure of securities where the major goal is to calculate the intrinsic value of a stock. It studies the fundamental factors that effects stock's intrinsic value like profitability statement & position statements of a company, managerial performance and future outlook, present industrial conditions and the overall economy.

#2 – Technical Analysis

This type of security analysis is a price forecasting technique that considers only historical prices, trading volumes and industry trends to predict future performance of the security. It studies stock charts by applying various indicators (like MACD, Bollinger Bands, etc) assuming every fundamental input has been factored into the price.

#3 – Quantitative Analysis

This type of security analysis is a supporting methodology for both fundamental and technical analysis which evaluates the historical performance of the stock through calculations of basic financial ratios e.g. Earnings Per Share (EPS), Return on Investments (ROI) or complex valuations like discounted cash flows (DCF).

The basic target of every individual is to increase its Net Worth by investing its earnings into various financial instruments i.e. creation of money using the money. Security analysis helps people achieve their ultimate goal as discussed below:

#1 – Returns

The primary objective of the investment is to earn returns in the form of capital appreciation as well as yield.

#2 – Capital Gain

Capital Gain or appreciation is the difference between sale price and purchase price.

#3 – Yield

It is the return received in the form of interest or dividend.

Return = Capital Gain + Yield

#4 – Risk

It is the probability of losing the principal capital invested. Security analysis avoids risks and ensures the safety of capital, also creates opportunities to outperform the market.

#5 – Safety of Capital

The capital invested with proper analysis; avoids chances to lose both interest and capital. Invest in less risky debt instruments like bonds.

#6 – Inflation

Inflation kills one's purchasing power. Inflation over time causes you to buy a smaller percentage of good for every dollar you own. Proper investments provide you hedge against inflation. Prefer common stocks or commodities over bonds.

#7 – Risk-Return relationship

The higher the potential return of an investment, the higher will be the risk. But higher risk doesn't guarantee higher returns.

#8 – Diversification

"just don't put all your eggs in one basket" i.e. do not invest your whole capital in a single asset or asset class but allocate your capital in a variety of financial instruments and create a pool of assets called portfolio. The goal is to reduce the risk of volatility in a particular asset.

What is Portfolio Analysis?
A financial term Portfolio Analysis, is primarily the study of certain portfolio regarding its performance, ROI and associated risks. The study or analysis is conducted with two objectives viz minimizing the risks and maximizing the returns. In marketing, the use of portfolio analysis is done for the same two reasons mentioned above.

Importance of Portfolio Analyze

Portfolio Analysis - 1

The analysis is done in large multinationals with multiple product portfolios. A company should be aware of the financial health of the portfolios and their wellbeing. To know the top performers and strategies to maintain them the profit makers is the primary objective of Portfolio analysis.
No company will have all products in profit. There will be few products or product lines which may be loss makers. These are the cash consuming portfolios and the company should be aware of them so that they can either be discontinued or revamped. The idea is to make them less costly and more profit making.
Portfolio analysis helps the company to stay in sync with the vision, mission, and objectives. At times it may happen that a certain portfolio may be loss-making and the company may have been unknowingly being financing the dead weight for a long time. In these cases, the analysis will give a clear picture of the scenarios.

Portfolio Analysis Tools :

There are several tools for portfolio analysis but here are two which are majorly used:

BCG Matrix for Portfolio Analyze

Also known as Product-Portfolio Matrix, Boston Box, Boston Consulting-Group Analysis, Portfolio Diagram. It was crafted in the 70s for the analysis of the business lines or product units. The chart is plotted as Market Share on the X-axis vs the growth on the Y-axis. Before one understands the tool, one must know the terms associated with it such as:
Relative Market Share: The market shares relative to the market leader or the product which is considered as a benchmark is called relative market share.
Market Growth Rate: The rate of growth of the specific product or portfolio is called Market Growth rate. Higher growth rate means higher profits.
The BCG Matrix is a graph which has four quadrants plotted on Market Share vs the Market growth or Relative Market Share vs Relative Market Growth. There are four components of BCG Graph as follows:

Cash Cows

Cash cows are the ones which generate the excess cash necessary for the survival of other portfolios as well along with itself. Cash cows are generally mature with relatively low market growth but higher market share. Cash cows have low market share compared to competitors but yield much higher returns as cash hence the term Cash Cow. A company will always try to push Cash cows to Star in terms of market growth. Cash cows require low investment and are usually do not cost much. The cash returns generated by cash cows are much higher than their expenses.

Stars

Like their names, Star is the portfolio which has a higher market share and highest growth compared to all other product portfolios. They are fast growing products with the highest market share close to monopoly but they also require high funding compared to others since they have to maintain their market share and growth, which can be generated from cash cows. If a star declines in market share, it becomes a Cash Cow and if it declines in growth, it becomes a question mark. Star products are very tricky to maintain their position and company has to invest a lot to keep that position. A company’s brand image and brand recognition is enhanced because of the Star products.

Question Mark:

These are also known as Problem Child or Wildcat. They operate with a lower market share compared to others in a high growth market. They have the potential to become Star as their market share increases and they already have a high growth rate as much as Star. When they increase their market share, they become Star and if they lose their share, they turn into Dog.

Dogs

Dog is a category which has a low market share and low market growth. They take a long time simply to break even and generate a nominal business barely necessary for survival in the market. They have a low return on investments and they are usually sold off or traded or closed down since eventually they become cash eating centers only. In very few cases it may be possible to increase their market share and convert them into cash cows or increase their growth rate and push them to Question Mark which eventually is converted to Star.

An example of Portfolio analysis by BCG Matrix would be of Google. Gmail, YouTube and Google Search Engine is the Cash Cow for the company while AdWords and Google Cloud are Star. The newly launched Google's flagship phones Pixel 3 XL, Pixel 3 and other Pixel series is a Question, Mark, while Google Pay is a Dog. Shareholders use this matrix as one of the tools for Portfolio Analysis of the company to determine the financial stability and predict the future for the company.

Product Life Cycle Analysis for Portfolio Analyze :

It is also known as the Product Life Cycle Analysis, determines the various stages at which the product is and will eventually go through. It imitates the biological life cycle and starts with Introduction, proceeds to growth, maturity and ends with decline.

Introduction: Introduction is the initial inception of the product in the market or the introduction. The market share is low and the growth rate is also low since the product is in its early stages. Here profit is not an objective but promotion is.

Growth: This is the prime phase of the product wherein the growth rate is higher and the market share goes on increasing equally faster. Companies earn maximum profit in this phase of the product and investors invest a lot. The promotion levels are kept down and the product earns an excellent profit for the company.

Maturity: In this phase, the market growth rate stops and the share continues to remain the same or increases marginally. The promotion levels have no effect on the growth or share. This is where the competition enters the picture and price wars start. The margins over the product are severely affected and this causes a lot of resellers to leave the market.

Decline: Here there is a decline in market share and the consumer's change or divert from the product making the producers divest in the product by introducing new variants of the same product. Many products may be discontinued from the market in this phase since there is little or no profit. The company, in order to increase the profit levels, may undergo cost cutting or cut down on the marketing budget.

Advantages of Portfolio Analyze :

Portfolio Analysis - 2

Determines the financial stability of the company along with product performance

Acts as trend analysis for the product to predict they are possible future in the market

Guide for investors and shareholders for financial assessment of the portfolios

The tool in decision making for the company to take product-related decisions whether to continue, change or discontinue products.

Disadvantages of Portfolio Analyze :

Doesn't consider market influencers and political factors in the analysis which may cause sudden changes in the nature of the portfolio

It is difficult to perform Portfolio Analysis for a startup company or small-scale industries with limited product lines

Any of the major portfolio analysis tools do not consider internal factors of the company like a sudden change in management which may affect sales of the product.

Bond Analysis and Management

A bond is a debt investment in which an investor loans money to an entity (typically corporate or governmental) which borrows the funds for a defined period of time at a variable or fixed interest rate. Bond Analysis is used by companies, municipalities, states and sovereign governments to raise money and finance a variety of projects and activities. Owners of bonds are debt-holders, or creditors, of the issuer.

On this page, we will talk about the basic fundamentals of bonds. Then, we get into the analysis and valuation of these 'Rodney Dangerfield' of assets. Finally we discuss how to manage them in portfolios.

Basic Fundamentals

The bond market is large and diverse, larger than the stock market. Thus, it represents an important investment opportunity.

In this section, we present some of their features and types. Then, talk markets around the world. Finally, we get into the entities who issue the.

Bond Features

Public bonds are long-term, fixed payout debt assets. They are packaged in useful, easy to manage sizes for sale to you and big firms.

The issuer agrees to pay a fixed amount of cash over time to the holder of record. Also, they agree to pay a fixed amount of par at the date of when they end.

Public Debt Segments Based on Term

- **Short-term** issues with terms of one year or less known as near cash or money market
- **Intermediate-term** issues have terms from one to ten years known as notes
- **Long-term** issues with terms over a year are bonds

Intrinsic Features

The *coupon* of a bond states the income a bond investor receives over the life of the bond. Also, the *term to maturity* gives the date or the number of years before a bond ends.

Most bonds are term bond with a single end date. However, a *serial bond* has multiple end dates. They are small issues with different coupons and end dates.

The principal or *par value* of an issue is the original value of the debt. However, par value is not the same as the bond's value.

Issue Types

Unlike common stock, bonds can have many issues outstanding at the time. In addition, they have different types of collateral and be either *senior*, *unsecured or subordinated*. Muni are divided into *general obligation* or *revenue bonds*. Also, *refunding issues* provide funds to end another issue early.

The type of issue only has a little effect on yields.The credit worthiness signals bond quality. Whether an issuer pledged collateral or not is not key unless the issue gets near default.

Factors Affecting Maturity

Call options affect the life and value of bonds. *Callable bond*s have a *call premium* which is the amount above par value the issuer must pay the holders for ending the bond early.

Call options

- **Freely callable** allows issuer to recall the bond at any time with a common grace time frame of 30 to 60 days
- **Non-callable** means issuer cannot retire the bond prior to maturity
- **Deferred call** means the issue cannot be called for a certain time after issue. Then, they are called freely

A *non-refunding* feature stops a call and early recall of an issue from the proceeds of a lower-coupon refunding bond.

A *sinking fund*feature says a bond must be paid off over its life.

Market Structure

The market for fixed-income debt is much larger than the listed stock market because firms tend to issue more bonds than common stock.

Many single buyers and big firms with diverse goals trade in the bond market. Big firms account for 90 to 95 percent of trading although the mix varies among the segments.

Bond ratings are a major part of the bond market because most corp and muni bonds are rated by one or more of the rating firms .Bond ratings provide the basic review for thousands of issues.

The main question is whether the issuer can service its debt in a timely manner over the life of a given issue.

The rating firms have done a decent job except in the last cycle. They have a habit of overestimating the rate of default.

Issuers

Global Bond Markets
The US fixed income market is loaded with US Treasury debt.The US government issues their bonds backed by the full faith and credit of the US government. The interest income is subject to fed income tax but exempt from state and local taxes. These bonds are popular because of their high credit rating, highly liquid trait and non-call feature.
The second largest bond market in the world is Japan. It is controlled by the Japanese government and the Bank of Japan. These bonds are an attractive asset because their rating is equal to the US.
The third largest bond market in the world is the German market, although the government segment is somewhat small. The German market is led by banks because firms mainly finance through bank loans.

Government Agency Issues
The federal government in each country can issue agencies which can issue their own bonds.They are a large and growing segment in the US, a much smaller segment in Japan and Germany and don't exist in the UK.
They are not direct Treasury but carry an implied full faith and credit backing of the federal government. The most popular in the US is GNMA, issued by Dept of Housing and Human Services.

Muni Issues
Muni bonds are issued by states, counties, cities, and other political subdivisions. Interestingly, they represent about 10% of the bond market in most countries and do not exist in the UK.
GO bonds are mainly backed by the full faith and credit of the issuer and its entire taxing power. Also, revenue bonds are serviced by the income thrown off from single revenue-producing projects of the muni.
The key feature of munis is the income is exempt from fed income tax as well as from local and state taxes.

Corporate Bonds
- **Mortgage Bonds**– has lien on real estate
- **Equipment Trust Certificates**– issued by railroads and airlines to buy rolling stock and planes
- **Collateralized Trust Bonds**– secured by financial assets
- **Collateralized Mortgage Obligations (CMOs)**– backed by pools of home loans
- **Asset-Backed Securities (ABS)** secured by cars or credit cards
- **High-Yield Bonds-** junk bonds of less than stellar credit firms

Bond Analysis and Valuation
The value of bonds can be described in terms of dollar values or the rates of return they promise under a set of factors. The value of the bond equals the present value of expected cash flows. The cash flows from the bond are the periodic interest payments and the repayment of par. However, the only factor which affects its value is the market discount rate- its required rate of return.

Relationship of Market Yield and Price
- The bond is priced at *premium* if the yield is below coupon rate
- The bond is priced at *discount* if the yield is above the coupon rate
- Also, a link between yield and price is convex- as yields decline the price goes up at an increasing rate, same in declining case

In this section, we start by talking about the various bond yield measures. Then we talk about theories of bond prices. Finally, we get into the reasons and measure of volatility.

Bond Yields
Bond Yield Measures
- **Nominal yield-** coupon rate
- **Current yield-** current income rate
- **Yield to maturity**– expected rate of return held to end
- **Yield to call-** expected return for bond held to first call date
- **Realized yield-** expected rate for likely bond sold before end considering reinvestment rates

Future Bond Prices
Dollar bond prices are worked up when dealing with realized yield and when issues are quoted on a promised yield basis, such as munis. Therefore the right market price is based on the current market YTM.

Term Structure Theories
- **Expectations Hypothesis**– shape of yield curve results for the interest expectations of market traders
- **Liquidity Preference**– long-term assets should provide a higher return than short-term ones because you are willing to give up some yield to invest in short-term to avoid long-term ups and downs
- **Segmented Market** – big firms have different maturity needs which leaves them to confine their bond picks to certain market segments

You can look at yield expectations by simply observing the shape of the yield curve. Thus, if the curve is declining sharply, it suggests rates will be decline.

Yield Spread Differences
- Segments, i.e. Treasuries vs corps
- Sectors of same segments, i.e. industrials vs. utilities

- Coupons or seasonings
- End dates within a given segment or sector

The strength of the direction of a spread can change over time.

Bond Volatility

There is an inverse link between changes in yields and the price of bonds. Importantly, interest rate sensitivity is one factor which affects the amount of price change for a yield change.

Bond Market Price Factors

- Par value
- Coupon
- Number of years to end
- Current market rates

Link between Yield and Price Change

- Prices move inversely to yields
- For a given change in yield, longer-term bonds post larger price changes
- Price volatility increases at a smaller rate as term increases
- Price movements from equal absolute increases in yield are not square
- Also, higher coupon issues lose smaller percent price changes

Interest rate changes trigger different strategies. Thus, bond prices increase during a major decline in rates. Therefore, you want you bonds to have the max rate sensitivity.

The most common measure of rate sensitivity is its duration. As such, it is a composite measure of the timing of a bond's cash flows traits taking into account its coupon and term to maturity.

Duration Types

- **Macaulay**– oldest measure, the time flow of cash from a bond
- **Modified-** makes small change to Macaulay
- **Effective**– direct measure where price changes are figured with a value model
- **Empirical**– measures the real price changes for real changes in rates

Bond Management

Prior to 1960, bonds were managed by simply buying and holding bonds in a group. At the time, purchases were made based on rate guesses and value models.

The early 1970s were hit by record-breaking inflation and rates. The intro of new finance types were in response to increased return risk. As a result, techniques such as matching funds or contingent portfolio were offered to meet the changing needs of big clients.

In this section, we describe passive ways to manage bonds. Then, we talk about a more active approach where we wring out more return and control risk.There are matching Funds techniques and contingent procedures. Finally, we talk about theoretical implications.

Passive Strategies

The simplest strategy is to buy and hold. Thus, these clients do not use active trading to get better returns. Also, a modified version starts with the purchase but still actively looks for ways to trade for stronger holdings.

Some traders opted to build their holdings to match the track record of a major bond index.Therefore, the manager is judged not on risk and return factors but how close the portfolio tracks the index.

Active Strategies

- **Interest Rate Anticipation**– probably the riskiest strategy involves relying on unclear forecasts of future rates
- **Valuation Analysis**– manager attempts to select bonds based on their intrinsic value
- **Credit Analysis**– involves detailed analysis of the bond issuer to determine expected changes in its default risk
- **Yield Spread Analysis**– looks for abnormal spreads within a normal sector spreads and makes swap
- **Bond Swaps**– involves liquidating a current position and simultaneously buying a different issue in ts place with similar attributes

Matched Funds Techniques

- **Dedicated Portfolio, exact match-** used to service a prescribed set of liabilities by lining up maturities to liabilities
- **Dedicated Portfolio, optimal cash match and reinvestment**– matches liability cash flows with interest payments and maturities
- **Immunization Strategies**– attempts to derive a specified rate of return during a given investment horizon regardless of what happens to market interest rates
- **Horizon Matching-** is a combination of cash-matching dedications and immunization

Contingent Procedures

- **Contingent Immunization-** allows managers to pursue the highest returns available through active strategies while relying on classical bond immunization to ensures a given floor return over the time horizon
- **Other Immunization Procedures**– includes requires an investor to accept a cushion spread and then engaging in various portfolio strategies to increase the ending-wealth value

Theoretical Implications

The performance of bonds offers total diversification benefits. In an efficient market, neither stocks nor bonds should dominate a portfolio but some combo should provide a superior risk-adjusted return.
Bond returns are linked directly to risk of default and interest rate risk. Although interest rate risk for investment-quality bond is non-diversifiable, some evidence exists default risk is also largely non-diversifiable because default experience is closely related to the business cycle.
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1. What are derivatives?

Derivatives are financial contracts whose value is dependent on an underlying asset or group of assets. The commonly used assets are stocks, bonds, currencies, commodities and market indices. The value of the underlying assets keeps changing according to market conditions. The basic principle behind entering into derivative contracts is to earn profits by speculating on the value of the underlying asset in future. Imagine that the market price of an equity share may go up or down. You may suffer a loss owing to a fall in the stock value. In this situation, you may enter a derivative contract either to make gains by placing accurate bet. Or simply cushion yourself from the losses in the spot market where the stock is being traded.

2. Why do investors enter derivative contracts?

Apart from making profits, there are various other reasons behind the use of derivative contracts. Some of them are as follows:

Arbitrage advantage

Arbitrage trading involves buying a commodity or security at a low price in one market and selling it at a high price in the other market. In this way, you are benefited by the differences in prices of the commodity in the two different markets.

Protection against market volatility

A price fluctuation of asset may increase your probability of losses. You can look for products in the derivative market which will help you to shield against a reduction in the price of stocks that you own. Additionally, you may buy products to safeguard against a price rise in case of stocks that you are planning to buy.

Park surplus funds

Some individuals use derivatives as a means of transferring risk. However, others use it for speculation and making profits. Here, you can take advantage of the price fluctuations without actually selling the underlying shares.

3. Who participates in derivatives market?

Each type of individual will have an objective to participate in the derivative market. You can divide them into following categories based on their trading motives:

Hedgers

These are risk-averse traders in stock markets. They aim at derivative markets to secure their investment portfolio against the market risk and price movements. They do this by assuming an opposite position in the derivatives market. In this manner, they transfer the risk of loss to those others who are ready to take it. In return for the hedging available, they need to pay a premium to the risk taker.

Imagine that you hold 100 shares of XYZ company which are currently priced at Rs. 120. Your aim is to sell these shares after three months. However, you don't want to make losses due to a fall in market price. At the same time, you don't want to lose opportunity to earn profits by selling them at a higher price in future. In this situation, you can buy a put option by paying a nominal premium that will take care of both the above requirements.

Speculators
These are risk-takers of the derivative market. They want to embrace risk in order to earn profits. They have a completely opposite point of view as compared to the hedgers. This difference of opinion helps them to make huge profits if the bets turn correct. In the above example, you bought a put option to secure yourself from a fall in the stock prices. Your counterparty i.e. the speculator will bet that the stock price won't fall. If the stock prices don't fall, then you won't exercise your put option. Hence, the speculator keeps the premium and makes a profit.

Margin traders
A margin refers to the minimum amount that you need to deposit with the broker to participate in the derivative market. It is used to reflect your losses and gains on a daily basis as per market movements. It enables to get a leverage in derivative trades and maintain a large outstanding position. Imagine that with a sum of Rs. 2 lakh you buy 200 shares of ABC Ltd. of Rs 1000 each in the stock market. However, in the derivative market you can own a three times bigger position i.e. Rs 6 lakh with the same amount. A slight price change will lead to bigger gains/losses in the derivative market as compared to stock market.

Arbitrageurs
These utilize the low-risk market imperfections to make profits. They simultaneously buy low-priced securities in one market and sell them at higher price in another market. This can happen only when the same security is quoted at different prices in different markets. Suppose an equity share is quoted at Rs 1000 in stock market and at Rs 105 in the futures market. An arbitrageur would buy the stock at Rs 1000 in the stock market and sell it at Rs 1050 in the futures market. In this process he/she earns a low-risk profit of Rs 50.

4. What Are The Different Types Of Derivative Contracts?
The four major types of derivative contracts are options, forwards, futures and swaps.

Options
Options are derivative contracts which gives the buyer a right to buy/sell the underlying asset at the specified price during a certain period of time. The buyer is not under any obligation to exercise the option. The option seller is known as the option writer. The specified price is known as strike price. You can exercise American options at any time before the expiry of the option period. European options, however, can be exercised only on the date of expiration date.

Futures
Futures are standardised contracts which allow the holder to buy/sell the asset at an agreed price at the specified date. The parties to the future contract are under an obligation to perform the contract. These contracts are traded on the stock exchange. The value of future contracts are marked-to-market everyday. It means that the contract value is adjusted according to market movements till the expiration date.

Forwards
Forwards are like futures contracts wherein the holder is under an obligation to perform the contract. But forwards are unstandardised and not traded on stock exchanges. These are available over-the-counter and are not marked-to-market. These can be customised to suit the requirements of the parties to the contract.

Swaps
Swaps are derivative contracts wherein two parties exchange their financial obligations. The cash flows are based on a notional principal amount agreed between both the parties without exchange of principal. The amount of cash flows is based on a rate of interest. One cash flow is generally fixed and the other changes on the basis of a benchmark interest rate. Interest rate swaps are the most commonly used category. Swaps are not traded on stock exchanges and are over-the-counter contracts between businesses or financial institutions.

5. How To Trade In Derivatives Market?
You need to understand the functioning of derivative markets before trading. The strategies applicable in derivatives are completely different from that of the stock market.

Derivative market requires you to deposit margin amount before starting trading. The margin amount cannot be withdrawn until the trade is settled. Moreover, you need to replenish the amount when it falls below the minimum level.
You should have an active trading account which permits derivative trading. If you are using services of a broker, then you can place orders online or on the phone.
For selection of stocks, you have to consider factors like cash in hand, the margin requirements, the price of the contract and that of the underlying shares. Make sure that everything is as per your budget.
You can choose to stay invested till the expiry to settle the trade. In this scenario, either pay the entire outstanding amount or enter into an opposing trade.

MUTUAL FUND

What is a mutual fund ?

Let's explain this term in a very simple way. Let's assume that you as an investor have no idea of shares and stocks. You need professional help and expertise. All you have to do is invest in a mutual fund scheme. A mutual fund scheme collects money from investors and buys and sell stocks collectively.

Say, there is a Mutual Fund Scheme called Super Returns Mutual Fund, launched by Super Returns Asset Management Company. What this fund does it comes out with a new offer of a scheme called Super Return Mid Cap Scheme. When it gathers say Rs 100 crores, it invests the money gathered from several investors into the stock markets. If the scheme is an equity scheme it would invest most of its money in shares, while if it was a debt scheme it would invest the same in debt like government securities, bonds etc Now, the fund will offer you units at Rs 10 initially. You buy one unit at Rs 10. Say, you buy 1000 units at Rs 10 and you pay a sum of Rs 10,000. One year down the line the stocks invested by the Super Return Mid Cap Fund rise and net asset value climbs to Rs 12 You can now sell the units back to the mutual fund at Rs 12 and you would get Rs 12,000 for your 1000 units.

Mutual Funds In India

- ICICI Prudential Mutual Fund
- Reliance Mutual Fund
- HDFC Mutual Fund
- Sundaram Mutual Fund
- Tata Mutual Fund
- L&T mutual fund
- Kotak Mutual Fund
- Quantum Mutual Fund
- IDBI Mutual Fund
- Canara Robeco Mutual Fund
- Baroda Pioneer Mutual Fund
- Motilal Oswal Mutual Fund
- Escorts Mutual Fund
- Birla Mutual Fund
- Axis Mutual Fund
- SBI Mutual Fund
- IDFC Mutual Fund
- UTI Mutual Fund
- Franklin Templeton Mutual Fund
- Principal Mutual Fund
- DSP Blackrock Mutual Fund
- BNP Paribas Mutual Fund
- HSBC Mutual Fund
- Taurus Mutual Fund
- BOI AXA Mutual Fund

What happens for a new buyer who is interested to buy the units?

For a new buyer who is interested to buy the units he would have to buy the units at Rs 12, since the net asset value has climbed. This means he has to pay Rs 12. In the example below we have tried to make it as simple as possible, assuming that the Super Return Mid Cap Fund is an open ended fund. We have avoided writing on things like entry and exit load, so as to avoid confusing the reader.

Types of mutual funds in India

Again, we are trying to make it as simple as possible in explaining to you the different types of mutual funds.

1. Equity funds invest most of the money that they gather from investors into equity shares. These are high risk schemes and investors can also make losses, since most of the money is parked into shares. These types of schemes are suitable for investors with an appetite for risk. Read more articles on Equity Funds.

2. **Debt Funds** Debt funds invest most of their money into debt schemes including corporate debt, debt issued by banks, gilts and government securities. These types of funds are suitable for investors who are not willing to take risks. Returns are almost assured in these types of schemes. Read more articles about Debt funds

3. **Balanced funds** Balanced funds invest their money in equity as well as debt. They generally tend to skew the money more into equity then debt. The objective in the end is again to earn superior returns. Of course, they might alter their investment pattern based on market conditions. Read More articles on Balanced funds.

4. **Money Market Mutual Funds** Money market mutual funds are also called Liquid funds. They invest a bulk of their money in safer short-term instruments like Certificates of Deposit, Treasury and Commercial Paper. Most of the investment is for a smaller duration.

5 Gilt Funds Gilt Funds are perhaps the most secure instruments that are around. They invest bulk of their money in government securities. Since they have backing of the government they are considered the safest mutual fund units around. Check More Article on Gilt Funds.

How to Apply for Mutual Funds?

If you are an investor who is looking at the much talked about mutual fund SIPs, there are many ways to apply to them. Many brokers accept mutual fund applications. Apart from this you can also apply directly through the website. Many mutual funds will give you login and password after you register. Remember, you need to comply with Know Your Customer Requirements before you apply. This is also known as KYC Requirement of Mutual Funds. You can also call the various toll free numbers of mutual funds, which can provide you all guidance on how to invest.

Understanding the Mutual Fund Schemes Remember, you need to understand the MF schemes before you invest. In the above para, we have made aware of how the various schemes operate. What is most important is that investors pick and choose carefully. If you are a person who has retired, it would be dangerous to choose the equity option. You would do well to consider debt mutual funds. Similarly, if you are young and have a steady income flow, opt for SIPs through equity mutual funds.

How does a Mutual Fund work?

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How does a Mutual Fund work?

Mutual Fund meaning refers to an investment programme which is funded by shareholders which trade in diversified holdings and is professionally managed. A mutual fund generally gathers money from the investor community and the same will be parked into those investments which an investor wants. These funds are generally managed by professional money managers who allocate the funds assets across various investment portfolios and endeavour to produce income or capital gains for the fund's investors. The mutual funds are more popular because they allow the investor to pick one fund which contains different stocks which are spread out based on the risk-taking capacity of the investor and hence one need not worry about putting too many eggs in one single basket. It also reduces the monitoring of prospectuses or keeping a tab on industry news. The mutual funds are managed by a fund manager, who picks up all the investments in the portfolio. It is often a big selling point for the beginners who do not have experience and would rather rely on an expert in the mutual fund for investing. For Example: If an HDFC mutual fund initially comes up with an open-ended equity scheme, then whatever the money it gathers from the investor group from this scheme will be invested in the equity shares. Say if the units were issued at Rs 20, will start inching up if the share prices surge. The Net Asset Value of these units which initially started at Rs 20, will increase gradually. So, it goes up from Rs 20 to Rs 22. Those investors who initially bought these shares at Rs 20 can sell it back to the mutual fund at Rs 22 and reap a profit of Re 2 per share. As it is an open-ended equity scheme, the mutual fund can sell its units constantly at the net asset value. So now, a new investor who did not buy the original initial issue at Rs 20 per share can now buy it at Rs 22 per unit.

List of required things to begin investing in Mutual Funds

The first and the foremost thing required to invest in a mutual fund is to be "KYC compliant", here KYC stands for Know Your Consumer. This includes submission of photographs, address proof, date of birth proof and a copy of PAN (Permanent Account Number) card. One can either directly approach brokers for making investments in mutual funds or can approach the mutual fund house. One can either opt for considering an equity mutual fund or can go for a debt mutual fund. It is important to update the KYC each and every time when you change your address as it is crucial to stay updated.

Keynote on Mutual Funds

There is a long way to go for mutual fund sector. While its development may seem substantial for a comparatively fresh sector in 2016. It is extremely small at 8.4 per cent as a share of GDP. The way individuals invest, which is a nice indication has been visibly changing. This is due to the growing sector consciousness.

KEY TRENDS AND OPPORTUNITIES

The Indian mutual fund industry's AUM is anticipated to reach 20 lakh crore earlier than anticipated with reduced bank interest rates and demonetization. Over the next 2-3 years, the mutual fund industry will see solid development powered by possibilities in the below-given field.

Digitalization and Digitization

- Improved delivery efficiencies have increased scope throughout the nation as retailers can now provide clients on the ground with the prepared assessment.
  Seamless client service has been allowed by a range of portable and web applications for monitoring and transacting end-to-end platforms.
- The mutual fund utility has enabled shareholders to position numerous AMC commands and transfer money seamlessly, all thorough a single door.
- E-KYC using Aadhar has proven to be an online investment game changer technology tool and Aadhar will be utilized for multiple public systems in the future.
- Redemption of mutual funds using a debit card offered by two famous Robo advisory systems as well as big investments in houses rendered the payment method more comfortable.
  Government initiatives and regulations-
- The completion of mutual fund commissions will help prevent mis-selling, it also promotes customer acquisition innovation and enables cost-effectiveness.
- Special mutual fund distribution commissions in less than 15 cities will increase penetration.
- SEBI proposed that leading e-commerce sites should allow the sale of mutual funds.

Greater Flexibility In Choices

Mutual funds provide a more flexible mix of customer choices and schemes, investment choices and higher tax efficiency. For long term loan, gold and real estate have become unattractive failing to produce decent yields in the last 2-3 years. Instead of shareholders take benefit of SIPs, a rigorous manner to construct long term capital and handle the intrinsic volatility of equity markets, with enhanced knowledge of the mutual fund sector.

Mutual Funds – How to Invest?

Beginners to invest in mutual funds may find it a little complicated initially. Investment in Mutual Funds can be done in two ways either directly or through an independent financial advisor or mutual fund distributor or broker based on the medium of investment either via online or offline mode. One should note that having a PAN Card (Permanent Account Number) and complying with the KYC (know your customer) requirements are must to invest in mutual funds in India.

Direct Investment

Individuals can purchase mutual funds directly from the mutual fund houses without the need to pass through any middleman. In this case, one has to do the research part all on their own as they will not be getting any financial advice or assistance from any fund houses. One can buy mutual funds physically by visiting the office of the asset management company or by filling in the application form and mailing it with supporting documents or via online mode.

Financial Advisor

The Financial Advisor is a certified, professional expert who will identify the investor's financial goal and helps an investor to build a financial blueprint based on the goals and recommend the correct investment options to match their objectives. One should understand as to how the advisor is paid and one is convenient with their recommendations. The financial advisor may charge a fee for providing his/her service to their clients.

Mutual Fund Brokers/ Agents/ Distributors

The mutual fund brokers or agents or distributors are the financial entities which usually recommends investors with investment products. One should always make a clear understanding of how they get paid for the investment and one should do their part of the research for meeting their financial and investment needs. Investors can transfer money to them directly or across the counter or by bank transfer. One should maintain an account with them to enable smooth transactions. Most of the brokers offer investment in multiple class assets apart from providing value-added services like risk profiling, financial planning and so on. One need not have to pay any additional fee for the services provided by the distributors as they get commissions directly from the mutual fund companies.

Online Portal

Several third-party portals are available online through which investors can invest. You can visit one of them and invest in a variety of mutual funds after payment of a nominal fee.

Key Takeaways from Mutual Funds

- A mutual fund is a type of investment vehicle which consists of a portfolio of stocks, debt-based bonds and other securities.
- A mutual fund gives small or individual investors access to diversify professionally managed portfolios at a low price.
- They are divided into various categories each representing the kind of securities they invest in, their investment objectives and the types of returns they seek.
- The mutual fund charges an annual fee which is known as expense ratios and in some cases, commissions which can affect their overall returns.
- The majority portion of money in case of employer-sponsored retirement plans go to the mutual funds.

Mutual Funds Calculator

A mutual fund calculator is a tool which helps in generating returns at maturity based on the investment amount, expected returns on investment and the tenure of investment. The users can adjust the variables of the calculators like the amount of investment, frequency of investment, systematic investment plan (SIP), frequency of SIP, lump-sum amount, expected rate of return and so on. The returns are usually varied in nature and are mainly based on the period of investment. The users should fill in the fields accordingly to find out how much would be the principal investment to arrive at the estimated accumulated wealth at the time of maturity. Investors can plan in a better way in advance by using the mutual funds calculator to meet their financial goals.

Mutual Funds Types that an individual can invest in

1.Equity or Growth Funds

The term equity funds clearly state that the investment money will be predominantly parked in equity shares (shares of companies). The primary objective of investing in these funds is wealth creation or capital appreciation. They have the ability to generate the highest return and these are best for long term investments. Examples of Equity Funds include:

- ‘Large-Cap’ funds which mainly invests in companies which run a large established business.
- ‘Mid Cap’ funds which invest in mid-sized firms.
- ‘Small-Cap’ funds which invest in small-sized companies.
- ‘Multi-Cap’ funds which invest in a mix of large, mid and small-sized companies.
- ‘Thematic’ funds which invest in a common theme.

Example – infrastrucutre funds that invest in companies that will benefit from the growth in the infrastructure segment.
- 'Sector' funds which invest in companies that are related to one type of business. Example: Technology funds that invest only in technology companies like Tech Mahindra Ltd, Oracle Financial Services Software Ltd, Infosys Ltd and so on.
- Tax Savings Funds

2. Bonds or Fixed Income Funds
The term bond is a kind of fixed income instrument which represents a loan made by an investor to a borrower (government or corporate). A bond is a kind of agreement between the lender and borrower which includes the details of the loan and payment. It is mainly used by states, companies, sovereign governments to finance projects and operations. The owners of the bonds are referred to as creditors/issuer/debt holders. These bonds include details such as the end date which refers to the principal amount of the loan which is due to be paid to the bond owner and includes all the terms for fixed interest payments or variable payments made by the borrower. They mainly invest in fixed income securities such as commercial papers, debentures, government securities or bonds, bank certificates of deposits and money market instruments like treasury bills and so on. They are a relatively safer form of investments and are suitable for income generation.
Examples of Bonds or Fixed Income Funds include –
- Corporate Debt
- Short Term
- Liquid, Floating Rate
- Dynamic Bond
- Gilt Funds and so on.

3. Hybrid Funds The term hybrid funds refer to an investment that is characterized by diversification amongst two or more asset classes. Here the mutual funds will park your investment in both equities and fixed-income funds, which means the fund typically invests in a mix of stocks and bonds. The aim is to offer the best of both in terms of growth potential and income generation. These funds offers the investor a diversified portfolio and hence it is known as asset allocation funds
Examples of Hybrid Funds includes –
- Child Plans
- Aggressive Balanced Funds
- Pension Plans
- Monthly Income Funds
- Conservative Balanced Funds and so on.

Mutual Funds Types based on Asset Class
The following are the types of Mutual Funds based on an asset class

- Equity Funds
- Debt Funds
- Money Market
- Funds Hybrid Funds

Equity Funds
This includes investing primarily in stocks and hence it is also known as stock funds. Mutual funds usually pool the money from the investors from the diversified background and infuse the same into the shares of different companies. The returns or losses are determined based on the performances of these shares in the stock market. Though investment in equity funds earns quick returns, the risk associated with losing money is relatively higher.
Debt Funds

The debt funds usually invest in the fixed income securities which include bonds, treasury bills, securities, gilt funds, short-term plans, liquid funds, fixed maturity plans, long term bonds and monthly income plans and so on. These debt funds come in with a maturity date and interest rate. If an investor is risk-averse who is looking out for a small but regular income (which includes small but regular income) then they can opt for debt funds.

Money Market Funds

The term money market funds are also known as capital market or cash market. It is usually managed by the banks, government, corporations by issuing money market securities like treasury bills, bonds, certificate of deposits, dated securities and so on. The fund manager will invest the investor's money and disburses a regular dividend to them in return. If an investor opts for a short term plan the associated risk is very less.

Hybrid Funds

As the name suggests hybrid refers to the balanced funds. These funds make an optimum mix of bonds and stocks which in turn helps to bridge the gap between the equity and debt funds. The ratio between the same can be either fixed or variable. It takes the best of two mutual funds by distributing 60% of assets in stocks and the remaining in bonds or vice versa based on the risk-taking ability of the investors. This is the most optimal form of investment for those who prefer to take more risks for debt plus returns benefit rather than holding on to the lower but steady income schemes

Mutual Funds Types based on Structure

The Mutual Funds can also be classified based on different attributes based on the asset class, risk profile and so on. The Structural classification which involves open-ended funds, interval funds and close-ended funds is broad in nature and the difference depends on the flexibility of the purchase and sale of individual mutual fund units.

Open-Ended Funds
Closed-Ended Funds
Interval Fund

Open-Ended Funds

The open-ended funds do not have any constraints with respect to the number of units or time period. An investor can trade funds based on their convenience and can exit from it whenever they want at the net asset value (NAV) at the time of exit. This is the reason why its unit capital changes regularly with new entries and exits. An open-ended fund may also stop including new investors if they do not want to or cannot manage large funds.

Closed-Ended Funds

In the case of the closed-ended funds, the unit capital to invest is fixed beforehand and hence the investors cannot sell more than the pre-agreed number of units. Some funds also come up with a new fund offer (NFO) period, wherein there is a preset deadline to buy the units. These funds have a specific maturity tenure and fund managers are open to funding the size, however large it may be. The regulatory body – SEBI mandates the investors to be given either to list them on stock exchanges or to provide them with repurchase option to exit the scheme.

Interval Funds

This fund has traits of both the open-end as well as closed-ended funds. The interval funds can be purchased or exited only at specific intervals and the same will be decided by the fund house and it remains closed at the rest of the time. There will be no transactions for at least 2 years. This kind of funds is generally suitable for those who want to save a lump sum amount for reaching out an immediate goal usually between 3 – 12 months.

Mutual Funds Types based on Investment Goals

The investment goals of an investor also play a major role while deciding to go with mutual funds. This particular kind of investment platform has something in store for everyone even if you are an aggressive investor or a conservative one who is risk-averse. The mutual fund basket has all forms of investment patterns be it for short or medium or long term. One can use different kinds of mutual funds with different investment objectives to reach their respective investment goals. The following are the types of mutual funds based on investment goals:

Growth Funds

The growth funds invest heavily in shares and growth sectors which are suitable for high net worth individuals (HNIs) investors who have surplus money to be distributed in riskier plans which will also fetch high returns or are positive about the high-risk schemes.

Pension Funds
Analysts advise earning individuals to put away a portion of their monthly income in a chosen pension fund to accrue the returns over a long period as this will safeguard the individual as well as their family during financial distress post-retirement from regular employment. This fund helps investors to take care of most of the expenses in the later part of their life be it children's wedding or a medical emergency and so on. Depending only on the savings post-retirement is not a good idea as the saved amount may end up.
Income Funds
These funds come in handy for those investors who are risk-averse. The investor's money will be deposited in a mix of bonds, securities, certificate of deposits which promises a guaranteed return. Income funds belong to the family of Debt Mutual Funds which is helmed by skilled fund managers who keep the portfolio in an organized way that the rate fluctuations will not compromise on the creditworthiness of the portfolio. This type of mutual fund has earned investors better returns than the traditional bank deposits which are best suited for those who are risk-averse.
Capital Protection Funds
This fund is suitable for those who opt to protect their principal and it fetches smaller returns. The fund manager will invest a portion of funds in Certificate of Deposits, bonds and the rest will be parked in equity funds. The investor will not incur any loss. One should lock in their investment for a minimum of three years (closed-ended) to safeguard their investments and the returns are taxable.
Fixed Maturity Funds
Most of the investors opt for fixed mutual funds as the financial year ends to take advantage of triple indexation as this will bring down the tax burden. If investors are not comfortable with the debt market trends then they can go for related risks by choosing fixed maturity funds which invest in securities, bonds, money markets and so on. It is a close-ended plan, it has a preset fixed maturity period which usually ranges between 1 month – 5 months similar to fixed deposits. The respective fund manager will make sure to put the money in those instruments with the same tenure, to reap accrual interest at the time of maturity of fixed maturity funds.
Tax-Saving Funds
The equity-linked savings scheme is gaining popularity amongst the investors' group as it serves the investor by doubling the benefits of saving the tax as well as building wealth. The lock-in period is lowest at 3 years. The investments are mainly parked in equity and its related products. It is well known to earn a non-taxed return ranging between 14% - 16%. It is best suited for salaried and long term investors.
Liquid Funds
The liquid funds fall under the debt fund category as most of the investments are parked in debt instruments and money market for a tenure of up to 91 days. The maximum amount of money allowed to invest stands at Rs 10 lakhs. One of the exclusive features which differentiate it from other debt funds is the calculation of Net Asset Value. The NAV for liquid funds is calculated for 365 days (which also includes Sundays) while for others only business days are included for calculation purpose.
Aggressive Growth Funds
Investment in this type of funds is slightly on the riskier note as is it designed to make steep monetary gains. Though they are susceptible to market volatility, one can opt as per the beta. Beta is also known as the beta coefficient, is a tool to gauge the fund's movement in comparison with the market as a whole. It can be calculated using the regression analysis and it represents the tendency of an investment's return to respond to movements in the market. By definition, the market has a beta of 1.0. A beta of 1.0 indicates that the investment's price will move in the lockstep with the market. A beta of less than 1.0 will indicate that the investment will be less volatile than the market. A beta of more than 1.0 indicate that the investment's price will be more volatile than that of the market.

Mutual Funds Types based on Risks
The risk factor is always present in the mutual funds as the investment is made in a variety of financial instruments including equities, debt, government securities and so on. The prices of securities keep on fluctuating owing to several factors which include interest rates changes, economic factors, supply-demand, inflation and so on.
Very Low-Risk Funds

Liquid Funds and Ultra Short-term Funds which have a tenure of 1 month to 1 year are not risky and the returns from the funds are relatively low (best returns at 6%). Investors who are looking to fulfil the short-term financial goals and prefer to keep their money safe can opt for Very Low-Risk Funds.

Low – Risk Funds

When investors are unsure about investing in riskier securities in case of a fall in rupee value or due to an unexpected national crisis, then most of the fund managers recommend investors to park money in either one or a combination of liquid, arbitrage funds or ultra short-term funds. Returns from these funds range between 6% - 8%, but investors are free to switch when valuations become more balanced.

Medium-Risk Funds

The risk factor in case of medium-risk factor is of medium level as fund managers invest a portion in debt funds and the remaining will be parked in equity funds. The NAV is not buoyant. The average returns from medium-risk funds could range between 9% - 12%.

High-Risk Funds

The high – risk funds are suitable for those investors who prefer riskier funds and aim for huge returns in the form of dividends and interest, high-risk mutual funds. These funds require active fund management. One has to keep a track of regular performance reviews as they are susceptible to market volatility. Investors can expect returns between 15% - 20% though the high-risk funds and the best one can fetch up to 30% returns.

Specialized Mutual Funds Types

The specialized mutual funds invest mainly in those securities which are from a particular sector or geographic region or type of security or industry and so on. Due to the lack of diversification, the risk factor is high but will provide potentially higher rewards to the investors.

Index Funds

The index funds are a type of mutual fund wherein a portfolio is constructed to match or track the components of the financial market index. It is said to provide a broad market exposure, with low operating expenses and low portfolio turnover. These funds follow their benchmark index irrespective of the state of markets.

Emerging Market Funds

The emerging-market fund is a kind of mutual fund which invests the majority of assets in those securities from countries are classified as emerging. These countries are in the phase of growth and offer high potential return with equally higher risks than those mutual funds from the developed market countries.

Sector Funds

As the term sector denotes, the sector funds are a type of mutual funds wherein investment is done solely in one specific sector. As investment is made only in specific sectors with only a few stocks, the associated risk factor is on the higher side. The investor should constantly be aware of the various sector-related trends and in case of a fall, he/ she should exit immediately, without having a second thought. The advantage of investing in this kind of mutual fund is great returns. Some of the examples of sector funds in India include IT, banking, pharma and so on. Most of the sectors have witnessed a huge potential and has proven consistent growth in the recent past and are anticipated to be promising in the future as well

Global Funds

The term global fund is a kind of mutual fund which invests in those companies which are located anywhere in the world and also includes investor’s own country. This kind of fund seeks to identify the best investment from a global universe of securities. It can either be focused on a single asset class or can be allocated to multiple asset classes. Investment in this fund can be quiet risky due to changing policies, currency valuations, market and so on. The positive thing about it yields higher returns on long term investment.

Fund of Funds

The term fund of funds is also known as multi-manager investment. It is a kind of pooled investment fund that invests in other types of funds which contains different underlying portfolios of other funds. These holdings usually replace any kind of investing directly in stocks, bonds and other types of securities. The main strategy of fund of funds is to achieve broad diversification and appropriate asset allocation with investments in a variety of funds which are wrapped in one portfolio. The types of fund of funds include hedge fund, mutual fund or a private equity fund or an investment trust.

Real Estate Funds The outstanding growth of real estate in India has led to the introduction of real estate funds. Despite the boom in the sector, many investors are wary about investing in such projects owing to multiple risks. This fund can be the perfect alternative as investors are affected indirectly as the investment will be parked in real estate companies or trusts and not in the projects managed by them. Investment for a long period will negate the risk factor.

Commodity Focused Stock

Funds This fund is ideal for those who can take sufficient risk appetite and are looking for a diverse portfolio. The commodity-focused stock funds give a chance to multiply and expand trades. The returns from this fund are not periodical and are either based on the performance of the stock company or a particular commodity itself. Gold – the yellow metal is the only commodity in India wherein mutual funds can invest directly. Others will invest either in units or shares of commodity-based businesses.

Suitable Mutual Funds Investment for Investors

If you are an investor then you can invest in mutual fund schemes. If you have just started your career, then one can opt for equity-related mutual funds which mainly park their funds in shares. The risk factor is high and so is the returns. The probability of losing money is high in equity-related mutual funds, but in the long term, they do fetch superior returns when compared with other forms of investment including bank deposits. For individuals who are in their middle age say the 40s to 60s, it is better to opt for debt rated mutual funds. This fund, unlike equity ones, will provide guaranteed returns. In the case of medium risk investors, one can choose hybrid funds which will form a diversified portfolio as the investment will be distributed in both equities and debt.

Advantages of Mutual Funds

1. **Diversification of funds**

The mutual funds have their share of risks as the performance of funds is mainly based on the market movements. Hence the fund manager will invest in more than one asset class to spread out the risk factor. This is known as diversification. If in case, if one of the asset class does not perform, then one can compensate with higher returns from the other one to avoid the loss for investors.

2. Liquidity

Only if investors choose to invest in close-ended mutual funds, it is easy for them to purchase and exit a scheme. One can sell their units at any point. Always not to keep an eye on surprises like exit load or pre-exit penalty. Mutual fund transactions can happen only once in a day after the release of the day's net asset value (NAV) by the fund house.

3. Professional Management

Investment in mutual funds is one of the favoured forms of investment as it is run by a fund manager who takes care of it and makes decisions based on the investors risk adverseness. The professional money manager will decide on how to invest your money based on a good deal of research and works out an overall strategy for making money. The fund manager will decide to either invest in debt or equities. They also decide on whether to hold them or not and also on the tenure of holding them.

4. Cost Efficiency

The investors have an option to pick up zero-load mutual funds which have fewer expense ratios. The expense ratio refers to the fee meant for maintaining the fund and it is a useful tool to assess the mutual fund's performance. An individual investor can check the expense ration of different mutual fund and choose the one which fits his/her budget and financial goals.

5. Tax Efficiency

Investment in mutual funds helps individual investors to claim tax deductions. Investment of up to Rs 1.50 lakh per financial year in tax saving mutual funds which are mentioned in Section 80C of the Income Tax Act is eligible for tax deductions. The best example of this is the ELSS. One should keep in mind that a 10% Long Term Capital Gains (LTCG) is applicable if the returns are more than Rs 1 lakh after one year. Investment in mutual fund fetches more returns when compared to other tax-saving instruments like FD in recent years.

6.Automated Payments

The mutual funds provide automated payments options to investors with this forgetting or delay in payment of SIPs or prompt lump sum investment can be avoided. One can opt for paperless automation by giving in standing instructions to the agent or fund house to make automated payments. The timely SMS and email notifications will help to counter negligence.

7. Meet Financial Goals The mutual funds in India are designed in such a way that every individual can make their part of the investment to reach their respective financial goals. Irrespective of the income level of the individuals, one should always set aside a part of their earnings towards savings. It is simple to find a mutual fund which matches the income pattern, investment goal, risk appetite, expenditure, growth pattern and so on.
8. Quick and Hassle-free Process Individual investors can initially start with one mutual fund and can diversify slowly at a later stage. It has become easier to identify and handpick the most suitable fund which suits an individual's financial goals. With the help of fund manager, the task of regulating and maintaining the funds becomes easier and their team will decide as to when, where and how to invest in mutual funds. The job of a fund manager is to consistently beat the benchmark and to deliver maximum returns on the investor's investment
9. 9. Systematic or One – Time Investment Individuals can now plan their mutual fund investment as per their convenience and budget. One can initially start with either a monthly or quarterly based SIP investment which best suits them with less amount and can expand gradually as per their convenience.

Disadvantages of Mutual Funds

Investment in mutual funds also has its share of disadvantages. The following are the disadvantages of investing money in mutual funds
1. Lock-in Periods Some of the mutual funds have a lock-in period which ranges between 5 years to 8 years, investing in such mutual funds is quite a risky affair as exiting such funds before maturity will be pretty expensive. Usually, the mutual funds will keep a certain portion of the fund in cash to pay the investors if they prefer to exit and this will not fetch any kind of interest to the investors. The Equity Linked Savings Scheme or ELSS have 3 years lock-in period.
2. Managing Costs of Mutual Funds The salary paid by fund houses to their fund managers and market analysts usually comes from investors. An individual investor should consider the total fund management charge as it acts as one of the main parameters while choosing a mutual fund. The higher management fee will not guarantee the investor with better returns. Usually, mutual funds pay its investment advisor a fee ranging between 0.5% to 1% of the fund's asset value. Most of the mutual fund houses in India charge different types of fee which includes sales charge or commission, expense ratio, short-term trading fee, redemption fee and 12(b)1 fee or distribution fee, service fees.
3. Dip in Profits Investors in mutual funds will diversify their investment to minimize risk factor, but this can even lead to falling in the profits and hence one should not invest in more than 7 – 9 mutual funds at a time. Investors are therefore advised that they should carefully pick the investment options after doing clear research and analysis.

Type of returns that you can get from Mutual Funds

There are mainly two types of returns which an investor can get from a mutual fund. One is the capital appreciation and the other one is the dividends. One has to choose either for a growth plan or for a dividend plan at the time of investment. In case of a growth plan, the money is not distributed like dividends, but it is added back to the scheme and the plan grows. For example: If you start investing in a mutual fund at a price of Rs 10. If you opt for dividend, then your net asset value will hardly move because the mutual fund has distributed the profit. In the case of a growth plan, the dividend amount is added back to the scheme and the plan grows. If your initial investment is Rs 10, you may witness the net asset value of Rs 17 in some years down the lane. This means you can sell the units at a higher price of Rs 17 and encash the profit.

How are returns from mutual funds taxed in India?

The beginners in the mutual funds should understand and know as to how to save tax. One can either opt for growth or dividend distribution. In case of a dividend distribution plan, the dividends earned by the investor is tax-free in the hands of the investor. This is the same even for the equity shares as well wherein dividends are tax-free in nature up to a maximum of Rs 10 lakhs. On the other hand, if you opt for a growth plan, there are capital gains that apply to the units that are sold at a profit. It is advised to go for dividend distribution. There is no tax liability in case of equity mutual funds if it is sold off before a period of one year. If one sells it before a year, then a tax of 15 per cent will be levied on the seller. It is very important to understand the tax liability before investing in a particular mutual fund.

List of Mutual Funds India

The initial investors in mutual funds should know the various popular mutual funds in India. Most of the equity mutual funds will give good returns when the markets are rallying. Currently, there are many mutual funds in India. The best mutual funds are primarily categorized based on their past performance, fund managers track record, financial ratios, and AUM of the scheme. Some of the best performing mutual funds in India includes Axis Mutual Fund, SBI Mutual Fund, ICICI Prudential, DSP Black Rock Mutual Fund, HDFC Mutual Fund, Kotak Mutual Fund, Birla Sunlife, Franklyn India, Reliance Mutual Fund and so on. The top mutual funds in India include - ICICI Prudential Equity and Debt Fund, Axis Bluechip Fund, Mirae Asset Hybrid Equity Fund, L&T Midcap Fund, HDFC Mid-Cap Opportunities Fund, Motilal Oswal Multicap 35 Fund and so on. The type of scheme than an investor chooses usually varies based on age and risk-taking ability.

Important Terms to know in case of Mutual Funds

As a beginner, one should know some of the prominent terms used in case of mutual funds and should know the basic meaning of the same. Some of these include SIP, NAV, AMC, Load Fund, Portfolio, AUM and so on.

SIP: The term SIP stands for Systematic Investment Plan and it refers to periodic investment in a mutual fund over a period of time. The investment can be either made on a monthly basis or every three months. The investor will have to commit to investing a fixed amount of money and the same will be used to purchase units. It mainly works on the principle of regular and periodic purchase of shares or units of securities. The payments for SIP can be either made by hand or one can even opt for funding it automatically once in a month, once in a quarter or whatever time frame the investor chooses.

NAV: The term NAV refers to the Net Asset Value. It is the prices of a unit of a fund. It represents the net value of an entity and is calculated as the total value of the entity's assets minus the total value of its liabilities. The NAV mainly represents the per share or unit price of the fund on a specific time or date. It constitutes the price at which the shares or units of the funds get registered with the regulatory body – Securities and Exchange Commission (SEC) and are traded.

AMC: The term AMC refers to the Asset Management Company (AMC). AMC is a firm that invests funds from clients by putting the capital to work through different investments including equities, bonds, master limited partnerships, real estate and so on. They mainly manage hedge funds, pension plans, create a pooled structure such as index funds and so on. They are also referred to as money managers or money management firms. Some of the AMU's which offer public mutual funds or exchange-traded funds (ETFs) are also known as Mutual Fund Companies or investment companies.

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AUM: The terms AUM refers to the Assets Under Management. It is the total market value of the investments that a person or entity manages on behalf of its clients. Usually, the definitions and formulas of AUM differ from one company to another. In some calculations, the AUM of some financial entities includes mutual funds, banks, deposits, cash whereas others limit it to funds under discretionary management, wherein the investor assigns authority to the company to trade on his/her behalf. AUM also helps in evaluating an investment or a company in general. Usually, higher AUM and high investment inflows for a firm are considered as a positive indicator of quality and management experience.

Load Fund: The term Load Fund is a mutual fund which comes in with a commission or sales charge. The fund which an investor pays will form the load as it goes to compensate a sales intermediary including investment advisor, broker, a financial planner who actually invests his time and expertise to select an appropriate fund for the investor. The load is either paid upfront at the time of purchase which is known as front end load, whenever the shares are sold it forms the back-end load or as long as the funds are held by the investors it forms level-load.

Portfolio: The term portfolio refers to the grouping of financial assets including shares, bonds, currencies, cash equivalents. Apart from this they also include fund counterparts such as closed funds, mutual funds and exchange-traded funds. It can also include non-publicly tradable securities like private investments, real estate, art and so on. These portfolios can either be held directly by the investors or they can be managed by the money managers and financial professionals. An investor can build his/her investment portfolio as per their risk tolerance and investment purpose. Investors can also have multiple portfolios for various purposes.

Acid Test Ratio: The term acid test ratio is obtained on dividing the current assets of a company by the current liabilities. It generally indicates the company's financial strength. It mainly uses the firm's balance sheet data as an indicator to check if it has sufficient short-term assets to cover its short-term liabilities. The acid test ratio is popularly known as the quick ratio.

Formulae for calculating Acid Test Ratio: Acid Test = Cash + Marketable Securities + Accounts Receivable
Current Liabilities

Back End Load: The term back end load is a fee (either load or sales charge) that an investor pays while selling mutual funds shares and the fee amounts to a percentage of the value of the share being sold. A back end load can be a flat fee or it can gradually diminish over some time usually within 5 – 10 years.

Asset Allocation Fund: The term Asset Allocation Fund refers to a fund that provides investors with a diversified portfolio of investments across various asset classes. It can either be variable or fixed in nature amongst a mix of asset classes, which means that it may be held to a fixed percentage of asset classes or can be allowed to go overweight on some based on market conditions. The popular asset categories for asset allocation funds include equities, bonds, cash equivalents.

Automatic Investment Plan: It is an investment programme which allows the investor to provide funds to an investment account regularly. The investment amount can be deducted directly either from the individual's salary account or from his/her account. The automatic investment plan is one of the best ways to save money. Many mechanisms have been developed to help facilitate automatic investment plans. Investors can contribute through their employer by scheduling automatic deductions from their salary account for investing in employer-sponsored investment schemes. Individuals can also opt for automatic withdrawal from their respective personal account.

Bond: The term bond refers to a fixed income instrument which represents a load made by an investor from a borrower (either corporate or government). A bond can be considered as an I.O.U. (I owe you) between the borrower and lender which includes the details of the loan and its payments. They are mostly issued by the states, companies, municipalities to fund their projects and operations. The owners of bonds are known as debt holders (creditors) of the issuer. The details in the bond will include the end date as to when the principal amount of the loan is due to be paid to the bond owner and it usually includes the terms for fixed and variable interest payments made by the borrower.

What to look out for before investing in Mutual Funds?

If an investor is a beginner and is looking forward to investing in equity funds, then it is better to take some professional advice from experts. For those who have some prior knowledge, it is good to take a look at the exit ratio, NAV, past track record and so on to understand if markets have surged up and you are buying the fund at an extremely high price to earnings ratio. For example: If in case, if the stock markets have rallied up then it may be time to wait for some time before investing a huge amount in equity mutual funds. One should always remember that the returns from equity mutual funds are mainly dependent on the movement of stock markets. So, if prices are high, then you can delay for some time before starting to invest. On the other hand, if the stock markets have crashed then the possibility is there that it may go down further and hence it is better to delay investing in stock markets for some more time.

SIP Route to Invest in Mutual Funds

For beginners, the Systematic Investment Plan or SIP is a better route to invest in mutual funds. Say, if you invest in a lump sum in any of the equity-based mutual funds and if the equity markets plunge, your NAV of the fund will also crash and eventually you will incur heavy capital losses. In case of SIP, one can invest in small amounts directly from their monthly salary which will get deducted from your bank account regularly. In the first month, you can buy little equity-based mutual funds and the index slips, next month, if you are buying some more at a lower cost eventually this will reduce your average cost. If in case, if the market gains, you have already bought some units at lower prices and this benefits you. Similarly, if the investor wishes to withdraw the money then they can opt for a systematic withdrawal plan. So one has an option for depositing and withdrawing via the mutual fund way.

What is SIP in Mutual Funds?

The SIP full form stands for Systematic Investment Plan. It is commonly referred to as SIP. It is an investment form which allows the investor to park his/her funds regularly a fixed sum in their chosen mutual fund schemes. In SIP, a fixed amount is deducted from the savings account every month and the investment will be directed towards the mutual fund which an investor chooses.

Benefits of investing in SIP

The investment amount in SIP is usually small and this will reap big returns over the long term.

- It is a very simple and convenient way to track investments. It brings in financial discipline.
- There is a lot of conveniences associated with an investment in SIP because investors can start investing with as low as Rs 500 per month.
- The SIP helps in rupee cost averaging as more units can be bought when markets are low, thus reducing the overall cost of investment.
- The power of compounding in SIP will yield better benefits if invested over the long term as against the one-time investment.
- SIP will give the investor better returns 2 times more than the investment made in fixed deposits of banks.

Why invest through SIP?

The very concept of SIP focuses on the philosophy of 'Save First, Spend Next'. By investing in SIP, the investor can invest small amounts at fixed intervals of time – weekly, monthly or quarterly basis instead of opting for a one-time investment.

Start with just Rs 500

It is very easy for anyone to start with SIP investment as one can start investing with as low as Rs 500 and still manage a burden-free budget plan. Though one has an option to gradually increase the monthly instalments by a factor of 15%.

Power of Compounding

The principle of Compound Interest implies that a small amount of investment made initially will grow into larger returns over some time as against the one – time investment.

Emergency Fund

The SIP acts as an emergency fund as it provides the investor with an opportunity to withdraw the entire amount for possible contingencies and hence acts as an emergency fund which puts life at ease. There will be no penalty for withdrawing from a SIP fund.

Rupee Cost Averaging

The volatile equity market is unpredictable. An investment in mutual funds through SIP will make you buy many units during plunge and less number of units in a flourishing stage and this will help to reduce the cost per unit and ultimately averaging it.

Become a Disciplined

Investor Investment in SIP will make an investor more disciplined in terms of managing finances. As SIP has automated payments options, one need not have to remember the payment dates every month.

One time investment or SIP – Which one is a better option?

Often investors are confused while choosing between a SIP investment or to go with one-time investment.
One-Time Investment In this case, investors will have to invest a considerable amount of money only once and need not think about it till the maturity date.

Monthly SIP In this case, the SIP will be a fixed amount of money which will be deposited at a regular interval of time in a mutual fund scheme. If the investor has a regular inflow of money in future, then they can go for this kind of investment which will earn better returns in the long term (better than bank's FD schemes). The risk factor in more while investing in SIP's as the returns are linked to market performance.

One-Time Investment	SIP Investment
Investment is made one time (lump-sum)	Periodic investments will be made in a tenure
Earnings are better when the market is high	Earnings are better when the market is low
It can lead to major loss in the event of a crash of markets (fall of Sensex and Nifty)	SIPs protects the investment from potential market crash and hence a safer option

How to select a SIP?

With the increase in the number of mutual fund houses, it gets difficult for the investors to choose the best SIP available in the market. To pick the best SIP available in the market, the investor has to look into these things.

Rs 500 Crore Asset Under Management

While opting for a SIP, go for a Rs 500 crore asset size which is a reasonable benchmark to select a fund. The ones below Rs 500 crore is not advisable though they are not bad.

Fund House

The stature of the SIP fund house is also an important attribute to be considered before choosing the SIP as it tells us how well the fund house was able to handle the ups and downs of the market without allowing the investors to feel the impact.

Duration of the SIP

The tenure of the SIP is also one of the important factors from the viewpoint of returns, risk factor and from the tax point of view. The investor should do an analysis of SIP for a minimum of 5 years as a reference point and check for the performance of funds across the market to get a larger picture before investing in SIP.

How to invest in SIP?

- **Make Investment Goals**

Every mutual fund has a goal and a purpose. The investor will have to first choose the best SIPs which will suit his requirements to reach their goal.

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- **Choose the SIP**

After setting up investment goals you will have to choose the best systematic investment plan which you prefer to invest in after making a groundwork on the performance of the fund over the last 5 years across the market.

- **KYC**

All the investors must submit the KYC documents for investing in mutual funds. So keep all the relevant KYC documents ready with you before filing in the mutual fund's form and duly submit the same to enjoy the fruitful benefits of returns from SIP.