Has the Mutual Fund Industry finally come of age?

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History

The Mutual Fund industry in India started in 1963 and in last 5 decades it has established itself as one of the most vibrant and fast-growing spaces in the financial services industry in India. In 1993, the first Mutual Fund Regulations were setup, marking an important landmark of the Industry's history. The MF Industry under the aegis of SEBI is now known world-wide as a disciplined and well-regulated industry. Looking into the history of this Industry gives us a more balanced view and the right perspective that frames the phenomenal growth across assets, investor participation, distributor participation, financial awareness, and above all the emergence of a sustainable solution for wealth creation of investors.

Key Challenges and context

The MF Industry has come a long way since its inception. In order to get a true picture of its maturity, we need to look at some of the challenges that we still face.

India is still a relatively under penetrated market when it comes to paying for financial advice. Many investors are not comfortable paying a fee when it comes to receiving financial advice and even more so in years where the market sees greater volatility and when there may be potential losses on investments. In the mass affluent segment, paying for advice still remains a relatively nascent concept. However, as SEBI Chairman Mr Sinha has mentioned several times, there needs to be a distinction between an advisor and a distributor.

The smaller locations in India also hold potential for tremendous growth, but also pose challenges that are unique to developing economies. Although financial savings are reasonable, there is less clarity about the advantages of investing. Financial literacy and general awareness of the investment options are lacking. A clearer picture about risks, return, pros and cons of various investment avenues would open up inflows in Mutual Funds. There is also a certain tendency to equate Mutual Funds with Equity, thereby ignoring several other products with comparatively less risk. Although concerns about inflation, retirement, financial health are present in these locations, the lack of financial awareness means that these concerns might not have led to investment decisions. One of the main challenges for fund houses is to distribute their products in smaller cities. Fund houses need infrastructure like branches, adequate number of relationship managers and sales service staff in these locations to be able to increase their sales volume coming from these smaller locations. Although, in the past few decades, the investors have increasingly relied on financial assets to invest their savings; the contribution of MFs in the asset portfolio is still low.

What is required is change in investment culture that embraces all the avenues and tailors a portfolio according to the individual's needs. A stronger advisor community could help the investors with these decisions and improve penetration levels. In addition to these, the potential to achieve long-term wealth has not been clearly communicated to the investors. The pure advisory model is likely to be the future, which would help further improve the Industry and have positive impact across stakeholders.

Coming of age

Despite the challenges, the MF Industry has posted all-round growth and continues to build towards its full potential. MF Industry has posted new highs across several aspects. Investors, distributors, and AMCs alike are enthusiastic about the future, mindful of the key positives in favor of the Industry and India's growth story as a whole. There are several signs that clearly show the growing maturity of the MF Industry such as growing investor base, higher focus on investor education, and continuous improvements in the regulatory environment. Though it has a way to go compared to more developed economies, the Industry is definitely going in the right direction.

MF Industry has shown decisive growth post the dip in Dec'11 – effectively doubling its assets from Rs 6 lakh Cr, in close to 4 years. Mutual Fund assets crossed Rs 13.5 lakh Cr this March which is an all-time high for the Industry. Industry continues to witness inflows in the Equity category. One of the positive trends has been the increased participation in SIPs which points towards more stable inflows and a long-term view of the investors. Industry added roughly 37 lakh new SIPs in FY16, with the total SIP count crossing 73 lakh.

Retail participation continues to be a highlight of the Industry. In FY16, folio count touched 4.7 crore, up from 4.1 crore in Mar'15. We are witnessing a trend where more and more investors are coming back into financial assets – March being the 22nd successive month witnessing steady rise in number of folios. Within the MF Industry, we have seen investors participating in a big way this year, and it is heartening to see that folios have risen significantly. Domestic retail investors have started recognizing the potential for a strong recovery and we are beginning to a witness clear shift in investment preferences from physical assets to financial assets. The same can be substantiated by the record high Retail inflows in Mutual funds over the year, defined by inflows in Equity, ELSS, and Balanced categories. Industry has witnessed Retail inflows of more than Rs 1.9 lakh Cr in FY16. Assets in this category grew from Rs ~30,000 Cr in FY04 to a peak of Rs ~2,15,000 Cr in FY10. As per May 2016, assets have Retail assets have gained a new peak once again at Rs 4,58,000 Cr. Distributor network has grown in tandem, with more than 76,000 ARN holders in the Industry and roughly half of them in locations other than the Top 15.

The Industry has grown on the back of a strong regulatory environment and constructive changes have continually helped boost growth and strengthen its potential. This is now one of the most well-regulated Asset Management industries in the world. There are several regulatory changes which have helped address concerns and ensure continued trust in the Industry. For expansion in smaller locations beyond the Top 15, SEBI has allowed an additional 30 bps to boost AMC participation and renewed vigor in acquiring new investors in these regions. In order to balance this with long-term and sustainable growth, it is necessary to boost investor awareness such that the keys tenets of financial planning and investment lead to long term wealth creation for the investors. All MFs are required to set aside 2 bps of their assets for Investor Education and Awareness initiatives. Investors have also been given new avenues of investment under the Direct plans where cost to the investor is further reduced. To round it off, SEBI has always promoted a highly transparent and disciplined approach. Brokerage data, monthly AUM, dependence on associate distributors, and a host of other data are to be disclosed to ensure complete transparency in Industry. Additionally, all AMCs are mandated to disclose complaints count in their Annual Report.

Looking ahead

Industry participants along with SEBI and AMFI have been focusing on geographical and retail penetration for awhile. Initiatives like 'District Adoption' will go a long way to improve overall financial literacy and strengthen presence of the Industry across the country. The green-shoots of these efforts are already showing up. The AUM from B-15 towns in retail segment increased by 26% from Rs ~108,200 Cr to Rs 135,800 Cr in FY16. Despite this growth, there is tremendous opportunity to expand in smaller locations. Drivers like lack of financial education and awareness, limited distribution network, cultural bias towards physical assets are some of the key impediments to growth in B-15 cities as of now.

The biggest opportunity of the Mutual Fund Industry is a strong and focused Investor Awareness Campaign. Overall, the Industry conducted ~10,800 Investor Awareness Programs across more than 250 cities, with about 4,73,000 participants. What is need is the conviction of the AMCs to further increase the scale and scope of these programs with the long-term goal of achieving a powerful pull effect for the MF Industry.

Technology has begun to show its power in the Industry, initially through mobile applications. The meteoric growth of mobile phones in India coupled with advancing mobile banking service provides an opportunity to cover rural markets and bring a larger number of investors to the Industry. Technology can not only improve the investing and advising experience, it will turn out to be a big cost saver. With indication towards using e-commerce sites for MF transactions, the impact of e-commerce websites and its role on the financial services space is also something to keep an eye on for the future.

Conclusion

It is inarguable that this is pivotal phase for the Industry. The platform has been set for wealth creation for investors and overall growth of all stakeholders in the MF Industry. Over the years, the Industry has not only strengthened its processes, but also shown that it can change with the times and adopt innovations in technology. Due to the strong and progressive regulatory environment and continued focus on long term wealth creation for investors, I am sure that the Industry will easily surpass this growth trend and achieve new heights in the future.