

Indian Mutual Fund Industry – The Impending Tectonic Shift



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While we have seen strong growth in the Assets under Management (AUM) over the last few years, the Indian mutual fund industry still remains significantly underpenetrated. In a country of nearly 137 crore people, there are only about 2.39 crore mutual fund investors. The number of mutual fund investors is lower than the number of car owners in India. The Indian MF industry is

still in its adolescence even by global standards. The total AUM of the industry at Rs.33.7 lakh crore works out to just 12% of our GDP, whereas in the US, the MF AUM is over 120% of GDP. In terms of GDP, India ranks as the 7th largest economy in the world, whereas in terms of MF AUM, India's rank is 17.

Several trends are encouraging at this juncture. Concepts like goal planning, asset allocation, systematic investing, compounding, diversification are no longer alien to many domestic individual investors. The growing awareness about smarter ways of investing along with rising income levels is likely to speed up adoption of mutual funds in the coming decade. The formalisation and digitization of our economy is expected to accelerate this trend further and bring about a tectonic shift in the Indian mutual funds industry.

Mutual Fund Awareness in India

SEBI has been at the forefront to spread awareness about mutual funds among Indian masses. In the year 2012, SEBI mandated each mutual fund to earmark 0.02% of its AUM every year for the purpose of creating investor awareness. All AMCs regularly conduct Investor Awareness Programs under this initiative, which has been one of the key factors behind new investors going through their first-time experience with mutual funds.

The AMFI or Association of Mutual Funds in India, an industry body, has also been dedicated to developing the Indian Mutual Fund Industry on professional, healthy and ethical lines. AMFI's "mutual funds sahi hai" campaign started in 2017 has been effective in educating individual investors about various aspects of mutual funds. The educational campaigns not only talk about the return potential of funds, but also help investors learn about risks and long-term orientation. The success of SIPs (Systematic Investment Plan) over the last few years

need to be attributed to a great extent to the increased awareness among the masses.

Smaller MFDs – The Last Mile Warriors

The growth in mutual fund AUM and the number of investors can be attributed in a big way to the smaller MFDs (Mutual Fund distributors, who do not fall under the broad categorization of a bank or a National Distributor), who have been successful in reaching out to individual investors across the country. Of the AUM of over Rs.7 lakh crore managed by these distributors, over Rs. 5 lakh crore are in equity-oriented funds, whereas only about 41% of the overall mutual fund industry assets are equity-oriented. We cannot overemphasize the role played by the smaller distributors in spreading awareness about mutual funds among people who need it the most.

We should not mistake a small distributor for one with archaic ways of servicing. Most small distributors are now digitally equipped having done away with the reliance on physical forms. They widely use the AMC portals, stock exchange platforms and the registrar portals to digitally process mutual fund transaction. Smaller distributors are the true last mile warriors when it comes to mutual fund distribution in this country.

Digitization – The Future of MF Distribution

As far as the issue of under-penetration of mutual funds is concerned, the answer lies in digital transformation of distribution too. The distribution of not just mutual funds, but almost all financial products including loans and insurance is shifting to the digital landscape.

India has been witnessing an exponential growth in smartphone users along with fall in mobile data costs. The availability of technology does not necessarily mean adoption of technology, as it requires a change in behavior among consumers and an ecosystem conducive for financial inclusion. The biggest push towards digital adoption came in the form of demonetization in 2016, as many Indians became familiar with digital payments and basic online banking services. The digital ecosystem received a boost with the Jan Dhan and Aadhar initiatives in the previous decade. While a bank account is a basic need to access various financial products, Aadhar has simplified the KYC process, setting up the stage for a digital explosion within the financial services space. The emergence of Covid pandemic and the resultant lockdowns has led to digital adoption in almost every aspect of our life, and most of these trends are here to stay forever.

Digitization is expected to be a huge game changer for the mutual fund industry resulting in twin benefits of expanding its reach to crores of new investors, while also bringing down the operational costs. For instance, in the pre-covid days a typical NFO launch would entail roadshows with the fund manager travelling across the

country proving to be a costly affair with only a limited reach. Today, as we reach out to people digitally through online medium, the message is spread more efficiently to a much larger audience.

Other Emerging Trends

Some of the other emerging trends in the industry include:

● **Surge in interest for direct investing:** Interestingly, there has been a surge in new demat accounts since the beginning of the pandemic last year. Over 2 crore new accounts have been added between March 2020 and June 2021, registering a growth of 53% during this period, outpacing the 15% growth in number of MF investors in the same period. A number of fintech platforms have capitalized on this opportunity by offering easy and convenient processing of transactions, appealing especially to the millennials. It remains to be seen how this trend pans out as investing is a life long journey requiring constant guidance, a part of investment advisory where the human touch may be as critical as technological edge. The AMCs also need to adapt with faster digital adoption, with focus on user experience, while also empowering the investor with enhanced awareness and redesigning the communication strategies.

● **Rise of the Fintechs:** Fintech firms have emerged as the new economy game changers, meaningfully altering the financial services landscape, thanks to the smartphone revolution over the previous decade. While the AUM of fintech firms is a small portion of the overall pie at just over Rs.38,000 cr, they have seen a 5-fold growth in just over 2 years. In a short period, they have managed to build an SIP book of over Rs.500 crs a month, which by no means is an insignificant achievement. Many of these apps by fintech firms are a big draw among younger investors, with their ease of use, simpler solutions and a gamified learning experience.

● **Growth in Passive Funds:** Passively managed funds have gained a foothold in the Indian scenario, though accounting for only 10.3% of the industry AUM. If we go by global statistics, where passives account for over 21% of AUM, we can expect a strong growth in this segment over the next decade. I must hasten to add, Indian fund managers have a long term track record of generating alpha and even active funds have a long run way of growth.

● **ESG (Environmental, Social, and Governance) Investing or sustainable investing:** ESG investing has taken off globally in a big way with over USD 2 trillion of assets being managed under the theme, registering a four-fold increase over the last 3 years. The domestic ESG funds account for an AUM of over Rs.12,000 cr. Though the concept is still at a nascent stage in India, we might see increased investor interest in this space.

● **Solution-orientation:** Globally, solution oriented offerings are highly popular as they help individuals achieve a specific financial goal. In India, solution oriented fund categories including Retirement and Children's Funds currently account for less than 1% of

MF industry AUM, while they deserve to occupy a much larger portion of the overall pie.

● **Growth in Alternatives:** We are also witnessing significant interest in Portfolio Management Services (PMS) and alternative investments. Family offices and High Net Worth Individuals have increased their allocations to equity PMS offerings in the last 5 years as these assets now account for Rs.1.85 lakh crore as on May 2021. The Alternatives space has grown to over Rs.4.5 lakh crore in terms of amounts committed as on March 2021, registering a 2.7x growth over the last 3 years. With our fast rising income levels, we can expect to see continued growth in the PMS and Alternatives space

● **International funds:** The last 3 years have also seen a sharp pick-up in interest for funds investing in international assets, as they not only offer global diversification, but also act as a hedge against domestic currency depreciation. Domestic funds offering global exposure account for an AUM of nearly Rs.25,000 crs and have witnessed a 10-fold growth in less than 3 years.

To Conclude

While it is expected that the number of mutual fund investors should grow in the coming years, the path is not without challenges. It is normal for a beginner to find mutual fund offerings to be complex and the terminologies to be jargonistic, and can avoid investing in them. Most AMC websites / apps provide a lot of learning content to help potential investors understand the basics of investing and mutual funds. The fintech advisors have covered a lot of ground over the last few years in terms of user experience to aid the learning of investors. Traditionally, most Indians have been investors in fixed deposits, who not only expect safety of capital, but a kind of certainty as to what would be the value of investments at the end of investing period. Mutual funds are market-linked and do not offer certain or pre-defined returns. Given this, the crucial role of handholding investors through the market cycles lies in the hands of the mutual fund advisors.

Mutual Funds offer unparalleled convenience and a vast range of offerings to meet most of the investment needs of an individual. Mutual funds offer the simplest way to perform asset allocation, goal planning and targeted wealth creation. The regulator has brought about many changes over the years for enhanced transparency and investor awareness. The sheer size of our country, the growing income levels and the largely untapped market holds huge promises for the mutual fund industry. Indian economy's path from USD 3 trillion to USD 5 trillion and beyond, would involve efficient channelizing of savings into key segments of the economy and mutual funds are expected to play a crucial role in this journey.

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MUTUAL FUND INVESTMENTS ARE SUBJECT TO MARKET RISKS, READ ALL SCHEME RELATED DOCUMENTS CAREFULLY.