

SPIVA[®] INDIA SCORECARD

MID-YEAR 2014

CONTRIBUTOR

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SUMMARY

- The index vs. active debate has been a contentious subject for decades, and there are strong opinions on both sides. The SPIVA India Scorecard is the de facto scorekeeper of this debate as it pertains to India.
- The SPIVA India Scorecard reports on the performance of actively managed Indian mutual funds vs. that of their benchmarks, showing equal-weighted peer averages.
- After the Lok Sabha election, Indian equities provided phenomenal performance through mid-year 2014 when S&P BSE 100, S&P BSE 200 and S&P BSE Mid Cap gained 35.37%, 36.43% and 59.93% respectively. While there was positive performance across all the segments of the market, Indian mid-/small-cap equities and Indian ELSS funds moderately outperformed the benchmark, whereas Indian large-cap equities did not over a five-year period.
- The bond market results were mixed. While Indian composite bond funds outperformed their benchmark, Indian government bond funds underperformed their benchmark over the one-year time period. Over the past five years, both peer groups underperformed the benchmark.
- Over the five-year period, the average survivorship rate was 83% and 86% for equity funds and bond funds, respectively.
- **Indian Large-Cap Equities:** Almost two-thirds of the active funds in this category outperformed the S&P BSE 100 over a one-year period. But over three- and five- year periods, 60% and 54% of the active funds underperformed the benchmark, respectively.
- **Indian Equity-Linked Saving Schemes (ELSS):** The majority of the active funds in this category outperformed the S&P BSE 200 in all the periods observed. The percentage of active funds that outperformed the benchmark over one-, three-and five-year periods, was 78%, 69% and 66% respectively.
- **Indian Mid-/Small-Cap Equities:** The percentage of active funds in this category that outperformed the S&P BSE Mid Cap over a one-year time period was 55%. Over three- and five-year periods, the percentage of funds outperforming the benchmark was 68% and 61%, respectively. The five-year survivorship rate was only 77%.
- **Indian Government Bonds:** Almost 60% of the active funds in this category underperformed the S&P India Government Bond Index over the one-year period. The percentage of funds underperforming the benchmark increased as the time period increased, with 64% and 78% of the active funds underperforming over three and five years, respectively.
- **Indian Composite Bonds:** More than 70% of the active funds in this category beat the S&P India Bond Index over the one-year period. Over three- and five-year periods, the percentage of funds outperforming the benchmark was 62% and 47%, respectively.

- **Fund Survivorship:** Over 95% of active funds in each of the peer groups observed in this report survived more than one year. However, only Indian ELSS funds maintained a survivorship rate of over 95% for the three- and five-year periods. The survivorship rate for the Indian mid-/small-cap equity funds and Indian government bond funds was less than 80% over the five-year period. The survivorship rate of Indian large-cap equity funds and Indian composite bond funds was 83% and 93% respectively over five years.
- **Equal-Weighted Average Funds Return:** Indian ELSS funds, Indian mid-/small-cap funds and Indian composite bond funds consistently delivered higher equal-weighted average returns than the benchmark across one-, three- and five-year periods. Indian government bond funds, on the other hand, recorded lower equal-weighted average returns than the benchmark across all observed periods. Indian large-cap equity funds recorded higher equal-weighted average returns than the benchmark over the one-year period only.

A Unique Scorecard for the Active vs. Passive Debate

The SPIVA India Scorecard provides a semiannual update on the active vs. index debate in India. The SPIVA India Scorecard shows the performance of actively managed Indian mutual funds compared with S&P Dow Jones Indices in their respective categories. Although many such reports are available, the SPIVA Scorecards are unique in offering:

- **Apples-to-apples comparison:** Fund returns are often compared to popular benchmarks, regardless of size or style classification. SPIVA Scorecards avoid this pitfall by measuring a fund's returns against the returns of a benchmark appropriate for that particular investment category.
- **Survivorship bias correction:** Many funds might be liquidated or merged during a period of study. However, for someone making an investment decision at the beginning of the period, these funds are part of the opportunity set. Unlike other commonly available comparison reports, SPIVA Scorecards account for the entire opportunity set—not just the survivors—thereby eliminating survivorship bias.
- **Data cleaning:** The SPIVA India Scorecard avoids double counting by removing multiple share classes of the same fund. It includes the share class with the longest available history.
- **Equal-weighted returns:** The SPIVA India Scorecard shows equal-weighted averages. Equal-weighted returns are a measure of average fund performance.

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Scorecard Results

Indian Large-Cap Equity Funds: Surprise in store

Since the Indian general elections of 2014, large-cap stocks have gained momentum. Almost 66% of Indian large-cap equity active funds outperformed the S&P BSE 100 over a one-year period. This percentage reduces drastically to 40% and 46% in three- and five-year periods, respectively. The survivorship rate was 97% for the one-year period, but only 87% and 83% for the three- and five-year periods (see Report 2). The equal-weighted asset return was 5% more than the benchmark return for the one-year period, but was less than the benchmark return for three- and five-year periods (see Report 3).

The actively managed funds in this peer group invest in the large-cap stocks of the Indian market that are sufficiently liquid. Since the S&P BSE 100 is designed to measure the performance of the top 100 large-cap companies in India based on size and liquidity, it is the most relevant index for benchmarking the large-cap segment of the Indian stock market.

Indian ELSS: Strong Active Performance

Close to 78% of the active funds in this peer group continued to outperform the S&P BSE 200 with a survivorship rate of 100% in the one-year period. Over the three- and five-year periods, 69% and 66% of the funds outperformed the benchmark with a survivorship rate of more than 97% over both periods (see Reports 1 and 2). The equal-weighted asset return was almost 8% more than the benchmark return over a one-year time period. It remained greater than the benchmark return in three- and five-year time periods as well (see Report 3).

The equity-linked saving schemes are eligible for tax benefits under Section 80C of the Income Tax Act in India. They have a lock-in period of three years, which explains the survivorship rate of this peer group. Unlike regular equity schemes, these have a lower investment threshold for investors and, therefore, remain a popular option for managing taxes. The S&P BSE 200 is designed to measure the performance of the top 200 companies based on size and liquidity, and is diversified across sectors. The top 200 companies include the large- and mid-cap companies in which the funds in this peer group invested; therefore, the S&P BSE 200 is the most appropriate benchmark for this peer group.

Indian Equity Mid-/Small-Cap Funds: Active Funds Outperform with a Nuance

Less than 45% of the active funds in this peer group underperformed the S&P BSE Mid Cap over the one-year period, with 32% and 39% underperforming over the three- and five-year periods (see Report 1). The survivorship rate in the one-year period was close to 96%, but it was only 85% and 77% for the three- and five-year periods respectively (see Report 2). The equal-weighted asset return was 3% higher than the benchmark return over a one-year time period and was 4% and 3% higher than the benchmark return over three- and five-year periods, as shown in Report 3.

The funds in this peer group invest primarily in the mid-cap segment of the market. Because the S&P BSE Mid Cap is designed to be a broad representation of the mid-cap segment of Indian market, it is the benchmark chosen for this peer group.

Indian Government Bond Funds: Active Funds Underperform

The percentage of active funds in this peer group outperformed by the S&P India Government Bond Index is very high. Over a one-year period, 60% of the funds underperformed the benchmark, whereas over the three- and five-year periods, almost 64% and 78% of the funds underperformed the benchmark (see Report 1). The survivorship rate for the one-year period was 100%, and was 92% and 76% for the three- and five-year periods, respectively (see Report 2). As shown in Report 3, the equal-weighted fund return was less than the benchmark return in all periods measured.

The Indian bond market is dominated by government bonds, in terms of the number, size and liquidity of the issues. The S&P India Government Bond Index comprises the government bonds that meet size thresholds. This index is designed to provide a broad representation of the government bond market in India, and it aims to serve as an appropriate benchmark for this peer group. All the bonds in the index are market-value weighted.

Indian Composite Bond Funds: Average Active Performance

Almost 70% of the active funds in this peer group outperformed the S&P India Bond Index over a one-year time period. The percentage of funds outperforming the benchmark was 62% and 47% over three- and five-year time periods, respectively. As shown in Report 2, the survivorship rate was above 97% for the one- and three-year time periods and 93% for the five-year period. The equally weighted asset returns for funds in this peer group were consistently higher than the benchmark return in all periods (see Report 3).

The actively managed funds in this peer group consist of both government and corporate bonds. The S&P India Bond Index is a composite bond index that comprises government and corporate bonds meeting the size thresholds, making it a prime benchmark choice for comparison. All the bonds in the index are market-value weighted.

Report 1: Percentage of Funds Outperformed by the Index

This report shows the percentage of funds that were outperformed by the benchmark index over the one-, three- and five-year periods. We begin with the funds listed in a category at the beginning of the period and report the percentage of funds that have underperformed the benchmark index. The fund's category at the end of the period is not considered, since the category of interest is the one at the beginning of the holding period. Therefore, fund category changes do not unduly affect the results in this report.

Report 1: Percentage of Funds Outperformed by the Index				
Fund Category	Comparison Index	One-Year (%)	Three-Year (%)	Five-Year (%)
Indian Equity Large Cap	S&P BSE 100	34.18	60.36	54.36
Indian ELSS	S&P BSE 200	22.22	30.56	34.29
Indian Equity Mid/Small Cap	S&P BSE MID CAP	44.93	32.00	38.67
Indian Government Bond	S&P India Government Bond Index	59.62	64.00	78.18
Indian Composite Bond	S&P India Bond Index	29.82	37.62	53.01

Source: S&P Dow Jones Indices LLC, Morningstar. Data as of June 30, 2014. Charts and tables are provided for illustrative purposes. Past performance is no guarantee of future results.

Report 2: Survivorship

This report shows the number of funds that existed in a particular category at the beginning of the period in question, as well as the percentage of funds that survived until the end of the period. Once again, the fund's category at the end of the period is not considered, because the category of interest is the one at the beginning of the holding period.

Report 2: Survivorship		
Fund Category	No. of Funds at Start	Survivorship (%)
One-Year		
Indian Equity Large Cap	158	97.47
Indian ELSS	36	100.00
Indian Equity Mid/Small Cap	69	95.65
Indian Government Bond	52	100.00
Indian Composite Bond	114	98.25
Three-Year		
Indian Equity Large Cap	169	86.39
Indian ELSS	36	97.22
Indian Equity Mid/Small Cap	75	85.33
Indian Government Bond	50	92.00
Indian Composite Bond	101	97.03
Five-Year		
Indian Equity Large Cap	149	82.55
Indian ELSS	35	97.14
Indian Equity Mid/Small Cap	75	77.33
Indian Government Bond	55	76.36
Indian Composite Bond	84	92.86

Source: S&P Dow Jones Indices LLC, Morningstar. Data as of June 30, 2014. Charts and tables are provided for illustrative purposes. Past performance is no guarantee of future results.

Report 3: Equal-Weighted Fund Returns

This report shows the equal-weighted average returns of funds in a particular category for the one-, three- and five-year periods. The eligible population in a given category is determined on a monthly basis.

For every month in the period, we calculated the simple average return of all the existing funds in each category. We then compounded the returns from all the months in the period. These returns are compared to the respective benchmark index returns. It should be noted that the population of funds used in the averaging process one month might differ from that used the next month because some funds could have merged or liquidated, new funds may have been formed and some funds might have switched categories.

Most reports that purport to show an average active fund performance report for funds in a category at the end of the period, and then they take the average of their historical returns. The SPIVA methodology offers a more accurate picture of active fund performance by calculating the average performance of the active funds in existence in a given category each month—not just at the end of the period.

Report 3: Equal-Weighted Fund Returns			
Index/Peer Group	One-Year (%)	Three-Year Annualized (%)	Five-Year Annualized (%)
S&P BSE 100	35.37	12.55	13.67
Indian Equity Large Cap	40.82	12.03	13.50
S&P BSE 200	36.43	12.23	13.74
Indian ELSS	44.31	13.95	15.61
S&P BSE MID CAP	59.93	12.83	14.77
Indian Equity Mid/Small Cap	63.09	17.20	17.91
S&P India Government Bond Index	3.78	8.37	6.93
Indian Government Bond	3.51	7.66	6.07
S&P India Bond Index	4.24	8.56	7.21
Indian Composite Bond	5.97	8.62	7.29

Source: S&P Dow Jones Indices LLC, Morningstar. Data as of June 30, 2014. All returns in INR. Charts and tables are provided for illustrative purposes. Past performance is no guarantee of future results.

Appendix: SPIVA Methodology

Data

We obtain a feed of monthly fund data from Morningstar® India for all managed funds for which data are available for a given month-end date during the performance period. The data feed includes the most comprehensive data on active, closed and finalized (merged or liquidated) funds in India over the chosen period. S&P Dow Jones Indices applies the following filters to ensure that an equitable comparative analysis is made.

- Only open-end unlisted retail unit trusts are selected.
- We retain only one version, or share class, of a fund by selecting the oldest share class.

The following identifiers are available on a monthly basis.

- Fund name
- Fund identifier
- Month and year
- Fund returns for the month, including distributions
- Fund categorization in that month

- Management type, i.e., whether the fund is indexed or actively managed

We then limit our subset using the following filters.

- We choose funds that are actively managed, excluding index and leveraged funds.
- While calculating the percentage of funds outperformed by the index, we remove funds that lack information on one-year returns from one-year periods, three-year returns from three-year periods and five-year returns from five year periods.

Fund Categories

We choose funds that have, at any point in the previous 60 months, been classified in at least one of the following five categories.

- Indian Equity Large Cap
- Indian ELSS
- Indian Equity Mid/Small Cap
- Indian Government Bond
- Indian Composite Bond

These categories, we believe, represent the primary categories of interest for Indian fund investors and were derived from the Morningstar Indian fund classification policy. The Morningstar classification system produces narrow, style-based classifications for funds, particularly in relation to Indian equities. S&P Dow Jones Indices has consolidated the style-based categories in order to generate a larger sample size and develop a broad-market comparison to market-based benchmarks. A narrow, style-based comparison would yield a limited sample size given that distinct value and growth style segments have not been consistently discernible over the past five years.

Morningstar categories have been mapped to SPIVA peer groups in the following manner.

Exhibit 1: SPIVA and Morningstar Categories	
SPIVA Category	Morningstar Category
Indian Equity Large Cap	India OE Large Cap
Indian ELSS	India OE ELSS (Tax Saving)
Indian Equity Mid/Small Cap	India OE Small/Mid Cap
Indian Government Bond	India OE Long Term Government Bond
	India OE Intermediate Government Bond
	India OE Short Term Government Bond
Indian Composite Bond	India OE Intermediate Bond
	India OE Short Term Bond

It is unlikely that funds will change from one category to another due to the broad nature of the groups that have been selected, which allows the SPIVA Scorecards to provide consistent comparisons over time.

Benchmarks

The chosen benchmarks are shown in Exhibit 2. All index returns are total returns (i.e., include dividend reinvestment) measured in Indian Rupees. There has been no deduction from index returns to account for fund investment expenses. It is important to note that active fund returns are shown after expenses, but they do not include loads and entry fees.

Exhibit 2: SPIVA Categories and Their Benchmarks

SPIVA Category	Benchmark Index
Indian Equity Large Cap	S&P BSE 100
Indian ELSS	S&P BSE 200
Indian Equity Mid/Small Cap	S&P BSE MID CAP
Indian Government Bond	S&P India Government Bond Index
Indian Composite Bond	S&P India Bond Index

The benchmarks chosen are the most commonly adopted benchmarks for funds that fall into the respective fund peer groups. In some instances, a fund may not adopt the benchmarks stipulated above. However, a vast majority do set their performance hurdle based on the assigned benchmarks in this report, ensuring that the study is robust and fair.

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