Addressing Issues in MF Market

What is the issue?

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Equity markets are facing a hard time in attracting the retail customers as they are used to predictable returns.

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What is the status of Indian Equity market?

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- Mutual fund industry discloses monthly portfolios and daily NAVs, follows mark-to-market accounting and promises swift redemption at the latest NAV in its open-end schemes.
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- Many sordid details of the IL&FS group's financials have tumbled into the public domain after the default. Click here to know more
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- As the credit ratings for IL&FS and its group entities fell steeply from investment to junk grade, debt mutual funds that held these bonds took immediate hits to their Net Asset Values (NAVs).
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- A decision by DSP Mutual Fund, which also had exposure to IL&FS paper, to sell its DHFL bonds at a discount set off an irrational panic about the NBFC sector.
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- Now calm appears to be returning to the market after government's offer of liquidity support after superseding the IL&FS Board.
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What are the fundamental issues in equity market?

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- In India there is fallibility of rating agencies in assessing the credit-

worthiness of borrowers.
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- The fact that bond deals happen mostly through the private placements also makes them susceptible to misinformation.
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- In the case of debt mutual funds, AMCs seem to have no well-thought out communication strategy to reach out to their investors in the event of sudden risks.
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- Unlike listed companies, most mutual funds in India do not have an ‘Investor Relations’ section on their home page that immediately directs the user to an important update.
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What measures are needed to address fundamental issues?

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- It is important for the mutual fund industry to introspect the issues in the industry and fix the gaps in its credit appraisal processes before it actively promotes debt products to risk-averse retail investors.
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- The fact that the IL&FS bonds figured in many liquid, ultra-short duration and short-duration funds, which are marketed as alternatives to bank deposits, makes it even more critical for MFs to improve their risk management skills.
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- The fund industry will need to be far more proactive and elaborate with its communication to appeal to retail investors.
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- The lack of uniform valuation norms for corporate bonds and their sporadic liquidity, are issues that need to be taken up on a war footing if the open-end fund structure is to work smoothly for debt funds.
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How mutual funds can be made accessible to retail investors?

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- Retail investors are used to the predictable returns of bank deposits or post office schemes, to understand the strange workings of the Indian debt

market.
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- MF industry can certainly do its bit to make life easier for retail investors by not mixing and matching both retail and institutional investors in the same debt schemes.
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- As smart institutions investors often get wind of trouble early and rush to redeem, it is retail investors who are left holding the baby.
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- The best solution to this problem would be for AMCs to create separate products for first-time retail investors testing out debt schemes.
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- If these schemes can be managed with minimal credit and duration risks, and deliver less volatile returns, common man would choose the mutual funds.
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Source: Business Line

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