

# SPIVA<sup>®</sup> INDIA SCORECARD

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## 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.
- Over a five-year period, the percentage of Indian large-cap equity funds and Indian government bond funds outperformed by their respective benchmarks was relatively high compared to the other categories.
- Over the same five-year period, the average survivorship rate for equities was 85%, and the survivorship rate for bonds was 91%.
- **Indian Large-Cap Equities:** The majority of the active funds in this category continued to underperform the S&P BSE 100 over one-, three- and five-year periods. Almost 78% of the funds underperformed in the one-year period. Over the three- and five- year periods, 66% and 69% of the funds underperformed the benchmark, respectively.
- **Indian Equity-Linked Saving Schemes (ELSS):** In 2013, almost two-thirds of the active funds in this category outperformed the S&P BSE 200. Over the three- and five-year periods, more than half of the funds in this category outperformed the benchmark.
- **Indian Mid-/Small-Cap Equities:** In the past year, 22% of the active funds in this category underperformed the S&P BSE Mid Cap. The percentage of funds underperforming the benchmark was higher in longer time periods, with 35% and 42% of the funds underperforming the benchmark over three- and five-year periods, respectively.
- **Indian Government Bonds:** The percentage of funds underperforming the S&P India Government Bond Index increased as the time period increased. The percentage of funds underperforming the benchmark in one-, three- and five-year time periods was 47%, 50% and 74%, respectively.
- **Indian Composite Bonds:** Almost 79% of the active funds in this category beat the S&P India Bond Index over the one-year period. The figure increased to 85% in the three-year time period, but reduced to 59% in the five-year time period.

- **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 and Indian composite bond funds maintained a survivorship rate of over 95% for the three- and five-year periods. The survivorship rate for the other fund categories was less than 90% in the three- and five-year periods.
- **Equal-Weighted Average Funds Return:** Indian composite bond funds and Indian mid-/small-cap equity funds consistently delivered higher equal-weighted average returns than the benchmark across one-, three- and five-year periods. Indian large-cap equity funds, on the other hand, recorded lower equal-weighted average returns than the benchmark across all observed periods.

## 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: Active Funds Underperform

Indian large-cap equity active funds continued to underperform the S&P BSE 100 over one-, three- and five-year periods. As shown in Report 1, more than 78% of the active funds underperformed the benchmark in the one-year period. In the three- and five-year periods, the picture is a little better, with 66% and 69% of the active funds underperforming the benchmark, respectively. The survivorship rate was 95% in the one-year period and 84% in the five-year period (see Report 2). The benchmark return was more than twice the equal-weighted asset return in the one-year period, and was much higher than the equal-weighted asset return in the three-year period (see Report 3). The benchmark return was consistently higher than the equal-weighted asset return in all the periods studied.

The actively managed funds in this peer group invested in the large-cap stocks of the Indian market that were 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: Active Funds Outperform With a Nuance**

More than 66% 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, more than 50% of the funds outperformed the benchmark with a survivorship rate of more than 95% (see Reports 1 and 2). The equal-weighted asset return was greater than the benchmark return in the one- and three-year periods, but it was less than the benchmark return in the five-year period.

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 schemes have a lower investment threshold for the 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 it 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 Slightly**

Less than 25% of the funds in this peer group underperformed the S&P BSE MID CAP over the one-year period. Over the three- and five-year periods 35% and 42% of the active funds underperformed the benchmark respectively (see Report 1). The survivorship rate in the one-year period was close to 98%, but it was only 80% for the three- and five-year time periods (see Report 2). The equal-weighted asset returns were approximately 6% and 4% more than the benchmark return over one- and three-year periods. For five-year period, the equal-weighted asset returns were close to the benchmark return, as shown in Report 3.

The funds in this peer group invested mostly 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: Survival of the Fittest?**

As the time period increased, the percentage of actively managed funds in this peer group outperformed by the S&P India Government Bond Index increased. In the one-year period, 47% of the funds were outperformed by the benchmark, whereas in the five-year period, almost 74% of the funds were outperformed by the benchmark (see Report 1). The survivorship rate in the one-year period was 100%, and it was 88% and 84% in the three- and five-year periods, respectively (see Report 2). As shown in Report 3, the equal-weighted fund return was greater than the benchmark return only in the one-year period.

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: Above-Average Active Performance**

Despite the huge net outflow of foreign institutional investors from the debt market, the majority of the active funds in this peer group continued to outperform the S&P India Bond Index with a survivorship rate of 100% in the past year. As shown in Report 1, the percentage of funds underperforming the benchmark was lower in the three-year period compared with the one-year period, but it increased in the five-year period. As shown in Report 2, the survivorship rate in the three- and five-year periods remained above 95%. The equally weighted average returns for funds in this peer group were consistently higher in all the 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 that meet 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	78.53	66.67	69.23
Indian ELSS	S&P BSE 200	33.33	47.22	48.48
Indian Equity Mid/Small Cap	S&P BSE MID CAP	21.74	35.37	42.11
Indian Government Bond	S&P India Government Bond Index	46.94	50.00	74.00
Indian Composite Bond	S&P India Bond Index	21.30	14.89	40.85

Source: S&P Dow Jones Indices LLC, Morningstar. Data as of Dec. 31, 2013. 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 (%)
<b>One-Year</b>		
Indian Equity Large Cap	163	95.09
Indian ELSS	36	100.00
Indian Equity Mid/Small Cap	69	98.55
Indian Government Bond	49	100.00
Indian Composite Bond	108	100.00
<b>Three-Year</b>		
Indian Equity Large Cap	165	86.67
Indian ELSS	36	97.22
Indian Equity Mid/Small Cap	82	80.49
Indian Government Bond	50	88.00
Indian Composite Bond	94	98.94
<b>Five-Year</b>		
Indian Equity Large Cap	143	84.62
Indian ELSS	33	96.97
Indian Equity Mid/Small Cap	76	80.26
Indian Government Bond	50	84.00
Indian Composite Bond	76	96.05

Source: S&P Dow Jones Indices LLC, Morningstar. Data as of Dec. 31, 2013. 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	7.56	2.28	18.62
Indian Equity Large Cap	3.31	0.35	16.02
S&P BSE 200	6.06	1.51	18.65
Indian ELSS	6.47	2.07	18.11
S&P BSE MID CAP	-4.03	-3.41	17.46
Indian Equity Mid/Small Cap	1.83	1.05	18.23
S&P India Government Bond Index	3.68	6.92	5.07
Indian Government Bond	4.69	6.68	3.99
S&P India Bond Index	4.12	7.06	5.52
Indian Composite Bond	6.18	8.15	6.30

Source: S&P Dow Jones Indices LLC, Morningstar. Data as of Dec. 31, 2013. 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.

<b>Exhibit 1: SPIVA and Morningstar Categories</b>	
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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