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## Focused funds: Volatile but fund manager can mitigate portfolio risk

By doing rigorous research on her limited holdings, the fund manager can mitigate portfolio risk

Sanjay Kumar Singh  
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The number of stocks in these funds usually ranges from 20-30, much less than the typical 60 or more found in diversified peers

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The Securities and Exchange Board of India's (Sebi's) September 11 circular stipulating that multi-cap funds must invest 25 per cent each in large-, mid- and small-cap stocks has sparked a search for alternatives. One category that many financial advisers are suggesting is focused funds.

Like multi-cap funds in their earlier avatar, focused funds are also free to invest across market caps without any restriction. However, Sebi has capped the number of stocks they can hold at 30. "The idea is that the fund manager should only include his highest-conviction stocks in this fund," says Taher Badshah,

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chief investment officer-equity, Invesco Mutual Fund. The fund house's ongoing new fund offer (NFO) for Invesco India Focused 20 Equity Fund closes on September 23.

The number of stocks in these funds usually ranges from 20-30, much less than the typical 60 or more found in diversified peers. "Concentrated position is a key feature of these funds. The weight of each stock can begin from 2-3 per cent and go as high as 9-10 per cent," says Mayur Patel, principal, fund manager-listed equity, IIFL Asset Management.

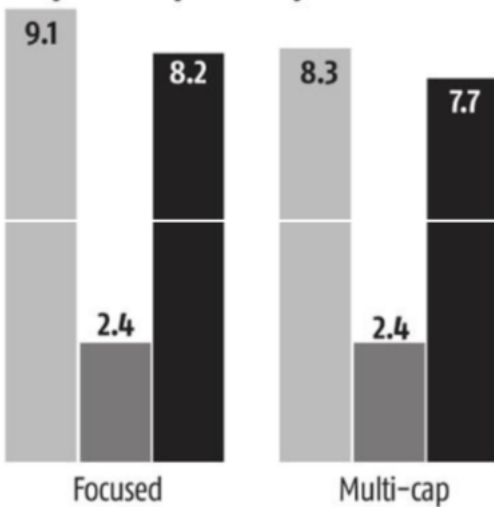
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Focused funds have the potential to deliver alpha. "If the fund manager's select ideas do well, he can materially outperform the benchmark," says Badshah. For the fund manager, these funds are less cumbersome to manage. He needs to focus only on 20-30 companies and try to maximise his understanding of them. It is harder to develop an in-depth understanding of 60 stocks or more. According to Patel, higher conviction about his chosen picks' long-term prospects allows a fund manager to take advantage of market corrections and build positions in such times.

## CATEGORY HAS OUTPERFORMED OVER 5-YEAR HORIZON

Category average return (%)

■ 1-year ■ 3-year ■ 5-year



Source: mutualfundindia.com

On the flip side, these funds can be more volatile than their more diversified peers, at least in the short term. Fund managers, however, say that investors should distinguish between volatility and risk.

Volatility refers to the fluctuation in a fund's net asset value while risk refers to the possibility of actual loss of money. While these funds can be more volatile due to their concentrated positions, they need not necessarily be riskier than their diversified peers, if the fund manager chooses high-quality businesses. Patel, in fact, informs that when he ran the numbers for the bigger (in terms of asset under management) focused funds, he found their one-year standard deviation to be lower than that of multi-cap funds from the same fund house.

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When selecting a fund, look for one that has consistently beaten its category average (a couple has achieved this in four of the past five years). The choice of fund manager is crucial. "Select a fund manager who has displayed an aptitude for running concentrated portfolios and has created a track record," says Sameer Kaul, chief executive officer and managing director, TrustPlutus Wealth Managers (India). Also, the portfolio should be diversified across market caps, segments (secular growth, cyclicals, and defensives), and sectors. Kaul suggests that only aggressive or moderately aggressive investors should invest in them. Finally, take the SIP route and invest for at least seven years in these funds.

**Read our full coverage on Sebi**

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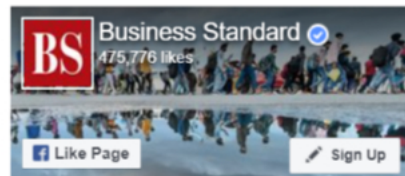


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According to finance ministry sources, the search committee had shortlisted five to six candidates.



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