Mirae Asset Knowledge Academy

Profit from Knowledge

Benefit from Multi-cap investing

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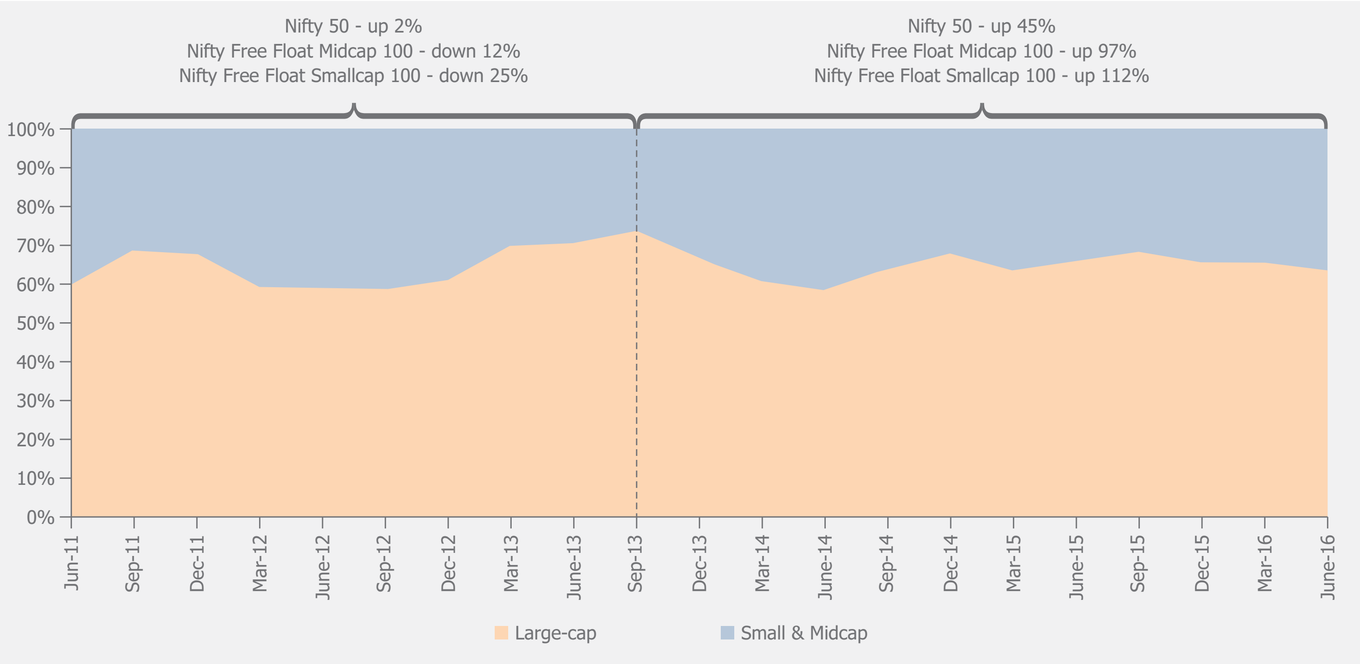
Asset allocation is one of the greatest shock-proof strategies in the investment universe. It spreads the risk emanating from a riskier asset (such as equity) to a less risky asset (such as debt). The strategy can be applied to an individual asset class too. For instance, in equity one can diversify across sectors and market capitalisation (market cap). Multi-cap funds or diversified equity funds are a great champion of the latter.

Multi-cap funds are not restricted to explicit market cap mandate. For instance, large cap funds invest in large cap stocks only, restricting the opportunity to benefit from small and mid-cap stocks in a bull market. Likewise, small and mid-cap funds cannot take high exposure to large cap stocks even during high volatility periods. This shortcoming can be aptly overcome by multi-cap funds as they diversify across market cap. They have the flexibility to change the exposure as per the market scenario. For instance, an analysis of the past five years (chart 1) shows that in June 2011-September 2013, multi-cap funds increased their large cap exposure from 60% to 74% as the small and mid-cap segment suffered a downtrend. However, after that (September 2013 - June 2016), these funds reduced the large cap exposure and increased exposure to the small and mid-cap segment from 26% to 37% to benefit from a rally in the latter.

Chart 1: Multi-cap funds exposure across market cap



Past performance may or may not be sustained future. Includes ranked diversified equity funds as per CRISIL MF Ranking for June 2016
Stocks having market cap lower than the Nifty 50 stocks are considered small and mid-cap, otherwise largecap

An analysis of market cap allocation of various categories (Table 1) shows that in the past five years, diversified equity funds have a more varied allocation across market cap, while allocation of large cap, small and mid-cap funds has been restricted to their respective mandate.

Table 1: Market cap allocation of the past five years

	Large cap exposure			Small and mid-cap exposure		
	Average	Maximum	Minimum	Average	Maximum	Minimum
Multi cap funds	65%	74%	59%	35%	41%	26%
Large cap funds	86%	92%	80%	14%	20%	8%
Small and mid-cap funds	22%	30%	12%	78%	88%	70%

Past performance may or may not be sustained future. Includes ranked diversified equity, large cap, and small and mid-cap funds as per CRISIL MF Ranking for June 2016.
Stocks having market cap lower than the Nifty 50 stocks are considered small and mid-cap, otherwise largecap.

The flexibility to invest across market cap helps them get stability from the large-cap segment and opportunity to earn higher returns from the small and mid-cap segment. Market cycle analysis in Table 2 highlights multi-cap funds' balancing approach.

Table 2: Market cycle analysis

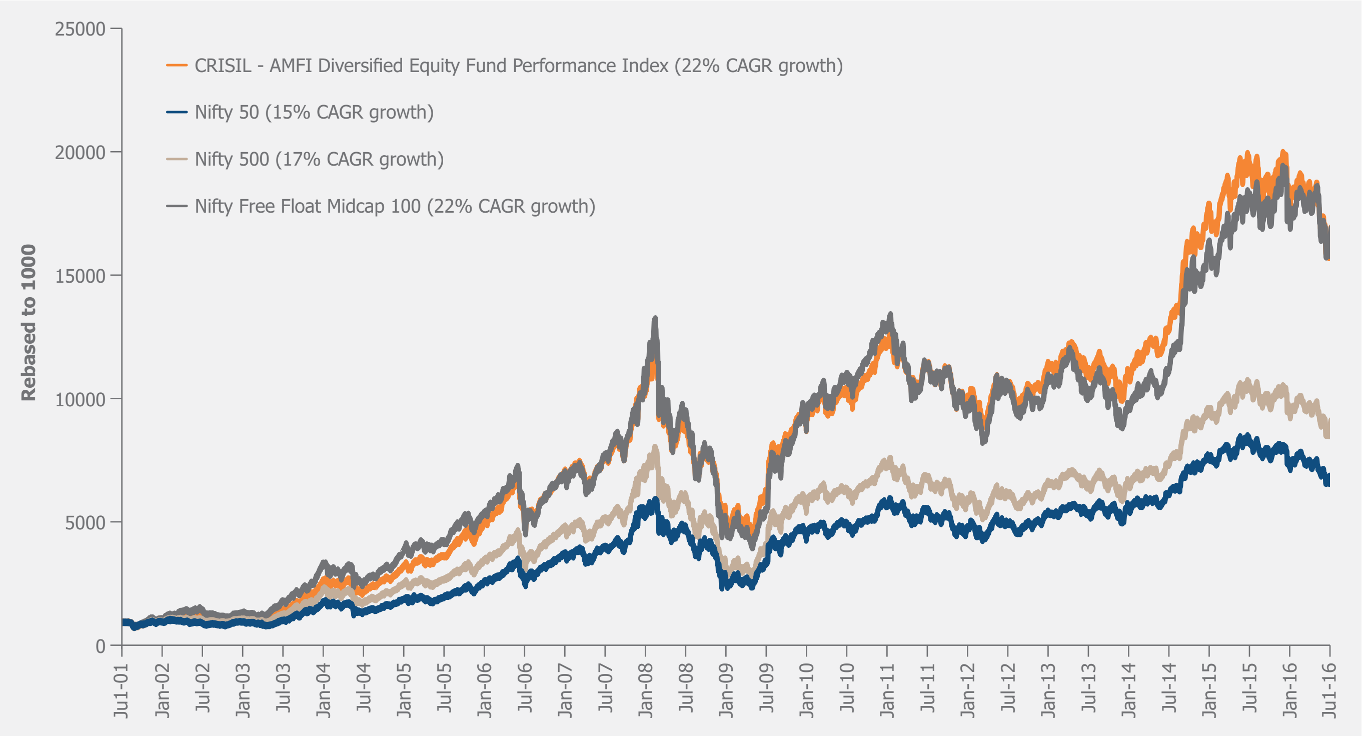
Period	From Date	To Date	CRISIL- AMFI Diversified Fund Performance Index	Nifty 50	Nifty Free Float Midcap 100	Nifty 500
Bull phase of 2003-07	1-Apr-03	30-Dec-07	63.47	46.97	-	53.14
Subprime crisis	1-Jan-08	31-Mar-09	-47.33	-43.42	-55.67	-49.55
Sharp bounce-back post subprime crisis	1-Apr-09	31-Dec-10	58.57	48.77	71.87	53.83
European crisis	1-Jan-11	28-Jun-13	-3.32	-1.94	-7.25	-3.59
Post European crisis	1-Jul-13	28-Feb-15	40.56	28.27	47.65	32.52
Chinese slowdown	1-Mar-15	30-Jun-16	-1.07	-4.75	3.98	-2.39

Past performance may or may not be sustained future. Returns are annualised

Strong performance over long periods

In addition to performing a balancing act during market phases, multi-cap funds have generated reasonably good returns compared with the market benchmarks. As seen in Chart 2, multi-cap funds (represented by CRISIL – AMFI Diversified Equity Fund Performance Index) have outperformed their benchmark (Nifty 500) and the large cap benchmark (Nifty 50) by a considerable margin and have performed at par with the mid-cap benchmark (Nifty Free Float Midcap 100) over 15 years ended July 29, 2016.

Chart 2: Performance



Past performance may or may not be sustained future. Includes ranked diversified equity funds as per CRISIL MF Ranking for June 2016
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Five-year daily rolling returns analysis shows that CRISIL – AMFI Diversified Equity Fund Performance Index has returned 14%, on average, since January 2004, higher than the benchmarks of all market caps (Table 3).

Table 3: Five-year rolling returns (annualised)

	CRISIL - AMFI Diversified Equity Fund Performance Index	Nifty 50	Nifty 500	Nifty Free Float Midcap 100	Nifty Free Float Smallcap 100
Average	14%	11%	10%	12%	9%
Max	29%	22%	24%	25%	30%
Min	0%	-1%	-3%	-2%	-9%

Past performance may or may not be sustained future. To maintain uniformity base date considered is January 1, 2004, which is inception of Nifty Free Float Smallcap 100.

Apart from diversification across market cap, these funds also distribute assets tactically across sectors. For instance, multi-cap funds benefitted from higher exposure to banking, financial and auto sectors (Table 4) in the past three years, which gained 22-28% CAGR. These funds reduced exposure to software and pharma sectors, which gained 12% and 18% in the same period vis-à-vis 14.6% CAGR returns by market benchmark (Nifty 50).

Table 4: Sectoral allocation

Top 5 sector	Exposure as of July 2016 (%)	Exposure as of July 2013 (%)	3-year average exposure (%)	Sector* performance in past 3-years (% CAGR)	Nifty 50 performance in past 3-years (% CAGR)
Banks	19.52	15.82	18.97	23.71	14.60
Software	8.19	14.40	12.22	11.92	
Pharmaceuticals	7.39	8.58	7.97	18.08	
Auto	7.31	5.33	7.06	28.43	
Finance	6.69	5.29	4.98	22.38	

Past performance may or may not be sustained future. Includes ranked diversified equity funds as per CRISIL MF Ranking for June 2016
*Sectoral performance represented by respective Nifty sectoral indices

Choose wisely

The aforementioned benefits notwithstanding, not all funds are winners in the multi-cap category. In a bid to maintain a diversified base, fund manager's decision to allocate across market caps and sectors plays a pivotal role. These funds are safer than small and mid-cap funds but riskier than large cap funds. Investors should do proper due diligence and invest based on their risk-return profile, after discussion with their financial advisor.

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The source for all the data and graph is CRISIL and the data is as on June 2016.

Mutual Fund investments are subject to market risks, read all scheme related documents carefully

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