Various Investment options offered by Mutual Funds

An Investor Education & Awareness Initiative By Franklin Templeton Mutual Fund

Typical classification of mutual funds

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Basis	Type of funds/schemes					
	1	2	3	4	5	6
A. Tenor	Open Ended	Close Ended	-	-	-	-
B. Asset Class	Equity	Debt/ Income	Hybrid	Real Assets	-	-
C. Investment Philosophy	Diversified Equity	Sector	Index Funds	Exchange Traded Funds (ETFs)	Fund of Funds (FOF)	Fixed Maturity Plans (FMPs)
D. Geographic Regions	Country/ Regions	Offshore	-	-	-	-

A. Mutual Fund schemes by Tenor

Mutual funds can be classified on the basis of time as under:

Open-ended funds:

- These funds are available for fresh subscription and redemption all throughout the year
- Investors have the flexibility to buy or sell any part of their investment at any time, at the prevailing price (i.e. NAV)
- These funds do not have a fixed tenor
- The unit capital of an open-ended mutual fund scheme keeps varying
- An open-ended mutual fund scheme is not obliged to keep on selling new units at all times
- An open-ended mutual fund scheme can repurchase the units at all times
- Such funds are susceptible to the worry of regular and sudden redemptions

A. Mutual Fund schemes by Tenor

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Close-ended funds:

- They are available for subscription during a specified period
- Buying a close-ended mutual fund scheme after its NFO period is not possible
- They have a time period until which investors' money is locked-in
- New investors cannot enter, nor can existing investors exit through a repurchase till the term of the scheme ends or an exit window is offered
- Close-ended mutual fund schemes are listed on stock exchange(s)
- The unit capital first issued does not change as a result of trading on the stock exchange
- The units of a close-ended mutual fund scheme may trade at a premium or discount to the NAV
- Close-ended funds are not prone to regular and sudden redemptions

B. Mutual Fund Schemes by Asset Classes:

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Equity Funds:

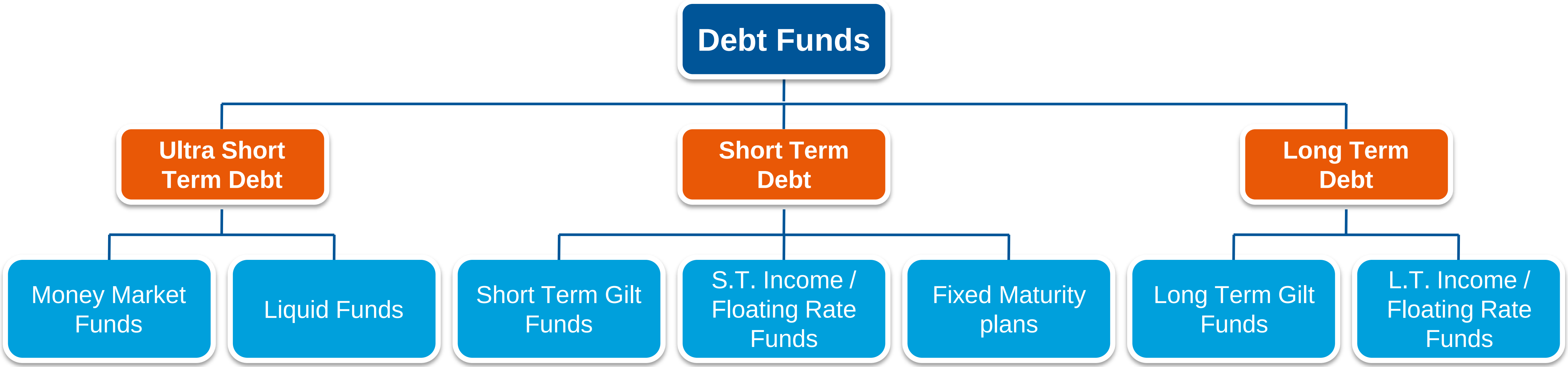
- Invest in equity as an asset class, in shares / stocks, rights, warrants, and other equity related instruments
- Invest in the respective market capitalisation segments such as large cap, mid cap or small cap
- Invest in growth stocks, value stocks or dividend-yielding stocks depending on the investment objective
- Equity Funds may follow a growth style, value style or a combination of both – called as blend style of investing

Suitability ❯ Equity funds are suitable for investors with an appetite and tolerance for high risk and want to earn better real rate of return (i.e. inflation-adjusted returns) in the long run and who invest with an objective of meeting their long-term financial goals.

B. Mutual Fund Schemes by Asset Classes:

Debt Funds or Income Funds:

- Invest in debt and instruments such as Certificate of deposits, corporate bonds, debentures, fixed deposits of banks, commercial papers, Treasury Bills, inter-bank term money and money market instruments amongst others.
- Debt funds are divided into two sub-categories i.e. short-term and long-term on the basis of the maturity profile of the papers they hold
- Debt Funds are of various types



B. Mutual Fund Schemes by Asset Classes:

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Type of Fund	Invests in…
Liquid Funds	Mainly invest in very short term money market instruments with maturity upto 91 days. Also invest in call money
Ultra Short Term Debt Funds	Portfolio comprises a mix of certificate of deposits, commercial paper, call money and other money market instruments with slightly higher maturity than the instruments held in liquid funds
Floating Rate Funds	Typically invest in short-term instruments offering flexible interest rates i.e. whose interest rate reflects the prevailing interest rate in the country
Short-term Income Funds	Have exposure to short-term bonds, deposits and NCDs. May also invest in T-bills and Government securities with maturity of less than 3 years
Fixed Maturity Plans	Provide exposure to bonds, NCDs and money market instruments that have maturity profile in line with the horizon of the scheme the Fixed Maturity Plan (FMP).
Dynamic Bond / Flexi-Debt Funds	Such funds invest in short-term as well as long-term bonds and NCDs. May also invest in Government securities with maturity of upto 5 years
Long-term Income Funds	Invest in bonds and debentures with maturity of more than 5 years. Can also invest in Government securities with maturity profile of 5 to 10 years.
Gilt Funds or G-sec Funds	Invest only in securities issued by the Central and/or State Government.

Suitability Debt funds are suitable for investors who are rather risk averse and do not mind compromising on real rate of returns (i.e. inflation-adjusted returns) they would earn in the long run, and generally have near or short-term financial goals. But while doing that care should be taken to select from various categories of debt mutual fund schemes.

B. Mutual Fund Schemes by Asset Classes:

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Hybrid Funds:

- Invest in multiple asset classes which could hold equity instruments, debt instruments and even gold.
- They are mandated to allocate ascertain portion of their AUM in the respective asset classes
- Depending upon their dominant exposure to equity or debt they are classified as equity-oriented hybrid funds and debt-oriented hybrid funds
- Balanced Fund is an example of equity-oriented hybrid fund, while Monthly Income Plans (MIPs) and capital protection funds are examples of debt-oriented hybrid funds

Suitability Hybrid funds can be suitable for investors who want to tactically allocate their assets; but the selection therein should be done as per their risk appetite and tolerance in order to hold an appropriate fund in the portfolio.

B. Mutual Fund Schemes by Asset Classes:

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Real Asset Funds:

- Invest in physical assets such as gold and real estate
- Gold, Exchange Traded Funds (ETFs) and Real Estate Investment Trusts (REITs) fall within the category of real asset funds

Suitability ❯ Those who wish to invest in other asset classes and diversify their portfolio by assuming high risk thereto, can invest in Real Asset Funds.

C. Mutual Fund Schemes by Investment Philosophy:

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Diversified Equity Funds:

- Are primarily equity funds investing across various sectors and market capitalisation
- They invest in equity & equity-related instruments following the basic tenet of investing, i.e. diversification

Value style: Value investing refers to buying stocks whose market value is severely deviated from their fair intrinsic value.

Value investing also revolves around asset of investment principles which are:

- Companies should have sound management
- Earning capacity of the companies
- Consistency in returns
- Prudent approach to debt financing
- Buying at the right price
- Long-term investment approach

Suitability ❯ Value style funds are suitable for those who give due weight age to the tenets of value investing that we just learn of.

C. Mutual Fund Schemes by Investment Philosophy:

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Growth style:

Growth style of investing focuses on the following factors for stock picking:

- Companies that deliver above-average earnings
- Companies that have higher PE (Price-to-Earning) multiple
- Companies with lower dividend yields

Suitability

Growth style funds are suitable for those who are willing to assume high risk in their endeavour to create wealth at an accelerated pace.

C. Mutual Fund Schemes by Investment Philosophy:

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Blend style:

Blend style of investing follows a combination of value and growth style of investing while picking stocks for the portfolio. Hence it depicts the traits of both, but to what extent the fund manager follows each of them, remains his prerogative.

Suitability ❯ Blend style funds are suitable for those who wish to follow the tenets of value investing, but at the same time would like to assume a little more risk and accelerate the pace of wealth creation.

Opportunities style:

Opportunities style funds invest in stocks of companies across market cap segments (large cap, mid cap, small cap) and across sectors. They hold a flexible investment mandate due to which these funds stand a better chance to benefit from attractive investment opportunities in various market segments. However in practice, this depends mainly on the fund manager's expertise in identifying and tapping promising investment opportunities well before others.

Suitability ❯ These funds are suitable for those who wish to take advantage of opportunities across sectors and market capitalisation optimally, but by assuming a little higher risk as against a typical diversified equity fund.

C. Mutual Fund Schemes by Investment Philosophy:

Large cap mutual fund schemes:

These funds are usually mandated to invest a predominant portion of their assets in large cap companies which stand at the uppermost layer of the market capitalisation pyramid. Some traits about large caps are:

- Companies with well-established businesses and stable revenues
- They have a high market share
- Usually are well-researched
- Their performance is more predictable
- They have the ability to weather the unfavourable economic conditions better
- These companies generally command a premium over the mid and small cap companies

Suitability ❯ Large cap funds are an indispensable part of the equity portfolio, irrespective of the risk appetite of the equity investor. So even if you have a large appetite for risk, you must include in your portfolio some petite composition of large cap funds

C. Mutual Fund Schemes by Investment Philosophy:

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Mid cap mutual fund schemes:

These funds are usually mandated to invest a predominant portion into mid cap companies which fall below the large caps but above the smaller companies in the market capitalisation pyramid. Some traits about mid cap companies are:

- They are well-established but have the potential to grow as they are yet in the growth stage of their life cycle
- They are leaner in size but have the ability to accelerate returns on investments
- They are often less researched
- They are more volatile as they tend to show fluctuations in profits and at times struggle to sustain when the going gets tough

Suitability

Mid cap funds are suitable for those who are willing to assume high risk in their endeavour to clock alluring returns. This is because, while mid caps show a tendency to do well during the upside of the market, they also tend to plunge during the downside of equity markets. Hence although one could invest as permitted by risk appetite, it is imperative to stay invested for the long-term to strike a better risk-return trade-off.

C. Mutual Fund Schemes by Investment Philosophy:

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Small cap mutual fund schemes:

These funds – also known as micro cap funds - are usually mandated to invest a predominant portion into small cap companies which fall below the market capitalisation of mid cap companies. So they are at the bottom of the market capitalisation pyramid. Some traits about small cap companies are:

- These companies are often under-owned
- They are leaner in size as compared to mid caps
- The volume of transactions and liquidity in small caps is low
- Thus investing in small cap carries very high risk
- They have the potential to generate super-normal returns

Suitability

Small cap funds are suitable for those who are willing to assume very high risk in their endeavour to clock super-normal returns. Small caps, as learnt, often have fewer transactions on the exchange and low liquidity, and thus that instils volatility in them when sudden buying and selling occurs. Hence, although one could invest as permitted by risk appetite, it is imperative to stay invested for the long-term to strike a better risk-return trade-off.

C. Mutual Fund Schemes by Investment Philosophy:

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Multi cap mutual fund schemes:

These funds are facilitated by their mandate to invest across market capitalisation, i.e. large caps, mid caps and small caps. Thus by doing so they spread their risk across market capitalisation and even capture investment opportunities across segments. Moreover, they are not confined to one particular style of investing; which allows them to follow a value, growth or blend style of investing.

Suitability ❯ Multi cap funds are appropriate if you are willing and / or want to take exposure across market capitalisation to tap opportunities, and at the same time want to diversify risk.

Flexi cap mutual fund schemes:

These funds, as enabled by their mandate, aim to optimise exposure to every market capitalisation segment depending on its attractiveness. In other words, a flexi cap fund can work as a large cap fund if the fund manager expects a better performance from large caps, and it may serve as a mid & small cap fund if the fund manager turns bullish on mid-sized companies. Moreover, some funds go one step ahead and switch between asset classes such as debt and equity with the flexibility to go 100% on either sides.

Suitability ❯ Flexi cap funds work as all-weather funds for the portfolio and are appropriate for those who wish to optimally capitalise on the opportunities available within market capitalisation and even asset classes vide a flexible investment mandate.

C. Mutual Fund Schemes by Investment Philosophy:

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Sector / Thematic Funds:

- Focus to invest in a particular sector
- A dominant portion of the fund's assets is invested in the respective sectors
- Thematic funds are a variation to sector funds and have a slightly broader mandate for investing by following a theme
- Thematic funds could invest in themes such as infrastructure, consumption, etc.

Suitability ❯ Investors who are willing to take very high risk and are adequately diversified but yet wish to follow their conviction of investing in sectors / themes may consider such funds.

C. Mutual Fund Schemes by Investment Philosophy:

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Index Funds:

- Are aligned to the respective benchmark indices
- The portfolio of such funds replicates the composition in terms of allocation or weight age of the chosen index
- These funds nearly mirror the performance of the designated benchmark index
- Index funds are passively managed
- They carry with them low expense ratio, relatively low portfolio turnover ratio and thus a low risk

Suitability

Index funds can be considered by those who are naïve to mutual fund investing as they generally command low risk amongst the equity funds. So, if you are relatively risk averse but yet want to take exposure to equities and mirror the performance of the benchmark index, then you may invest in such funds.

C. Mutual Fund Schemes by Investment Philosophy:

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Exchange Traded Funds (ETFs):

- Are traded on the exchange
- They can be bought or sold on the stock exchange on a real time basis
- The AMC may not offer sale and re-purchase of units
- ETFs are traded on the respective stock exchanges and are bench marked to the irrespective indices
- ETFs are available for pre-specified equity indices and also those which mirror the price of gold
- Most ETFs are passively managed

Suitability ETFs are suitable again for naïve investors looking for lower cost, convenience of investing and who are relatively risk averse, but yet want to take exposure to equities and mirror the performance of the benchmark index.

C. Mutual Fund Schemes by Investment Philosophy:

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Fund of Funds (FoFs):

- FoFs invest their money in other funds of the same mutual fund house or other mutual fund houses
- FoFs could have a mandate to invest in funds focusing on investing in various asset classes and markets / regions
- Provide an opportunity to create a diversified portfolio of various mutual fund schemes; whereby one can avail of the benefit of: diversification by fund manager and investment style
- FoFs may help in diversification across types and investment style
- Relieves you from the process of selecting the right mutual fund schemes
- Reduces hassles such as multiplicity of transactions, filling forms, maintaining multiple account statements and tracking multiple mutual schemes
- FoFs may have a high expense ratio

Suitability

FoFs are suitable for small and new investors willing to build a portfolio of mutual funds but lack resources and skills to research and select the right funds. Also for those who want to eliminate the hassle of maintaining and tracking their investment in multiple schemes, but are ready to bear high expense ratio.

C. Mutual Fund Schemes by Investment Philosophy:

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Fixed Maturity Plans (FMPs):

- FMPs are close-ended schemes with fixed tenure that cease to exist thereafter
- FMPs are listed on the stock exchange
- They invest in debt & money market instruments of similar maturity as the stated maturity of the plan
- The maturity amount in case of FMPs is not fixed
- There is no default guarantee or insurance
- FMPs do not provide investors with an option to exit
- Exiting prematurely is permissible through a sell transaction on the stock exchange

Suitability

FMPs are suitable to those who wish to clock better post-tax returns as against bank or corporate FDs; but who are willing to take slightly high risk since the maturity proceeds are not guaranteed.

D. Mutual Fund Schemes by Geographic Regions:

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Country or Region Specific Funds:

- Invest in securities (equities and / or debt) of a specific country or region or economic groupings, viz. developing & emerging economies and developed economies
- The underlying belief is that the chosen country or region is expected to deliver superior performance
- Such funds have an exposure to currency risk, interest rate risk, macroeconomic risk, regulatory risk and geopolitical risk
- They can facilitate geographical diversification

Suitability

Country or region specific funds can be suitable if one is adequately diversified within the domestic portfolio, and is looking for further diversification across countries or regions; but is willing to bear high risk emanating from such an investment. Moreover, care should be taken while selecting such funds.

D. Mutual Fund Schemes by Geographic Regions:

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Offshore Funds:

- Are domiciled outside the home country where the mutual fund house is registered
- They are usually established in countries which provide a significant tax advantage for foreign investors
- They ought to comply with the regulations of the country where they are registered
- Offshore funds mobilise money from investors for the purpose of investment outside their home country
- Offshore funds invest in listed equities and debt securities
- They facilitate geographical diversification
- Investors in offshore funds are exposed to regulatory risk, geopolitical risk, macroeconomic risk and currency risk

Suitability

Before investing in offshore funds, one should have a fair diversification within the domestic portfolio, and then if risk appetite permits, may invest in offshore funds for geographical diversification. But utmost care should be taken while selecting offshore funds, and one should avoid those which have a mandate to take an acute country-specific exposure.

Options available for investing in mutual funds

Dividend Option:

This option facilitates investors to book profits in the form of dividend and provides further sub-options:

- **Dividend Payout:** This option proposes to timely pay distributable surplus / profits to investors in the form of dividends either through cheques or ECS credits, thereby facilitating them to book profits.

Suitability ❯ This option can be selected by those who are in need of cash flows during the investment horizon and may not have regular flow of income.

- **Dividend Re-investment:** The dividend amount declared by a mutual fund scheme, goes in to buy additional units of the same scheme. So it keeps re-investing the dividend proceeds in the same scheme.

Suitability ❯ This option is suitable for investors who are not in need for cash flows in the form of dividend during the investment horizon; but instead would prefer to add additional units to the same scheme (where they are invested) via the dividend declared for the scheme.

Options available for investing in mutual funds

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Growth Option:

This option facilitates compounded growth in value of your mutual fund scheme, subject to the investment bets taken by the fund manager.

Suitability ❯ This option is suitable for those investors who are not in need for cash flows in the form of dividend during the investment horizon; but would instead prefer to invest their hard earned money for compounding their wealth.

Bonus Option:

Under the bonus option investors are not paid regular dividends. Instead they continue to receive bonus units in accordance to a ratio declared by the fund house.

Suitability ❯ This option is suitable to those who wish to add units to their investments as per the ratio of bonus declared.

Direct Plan vs. Standard Plan

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Direct Plan:

- Facilitates investors to invest directly in the mutual fund scheme offered by the fund house
- Investor can bypass the distributor channels
- Direct plan has a lower expense ratio
- Investors can save a good deal of money and thus may fetch better returns

Suitability ❯ Savvy investors who use the online platform and don't mind investing in mutual funds using e-route may be better off opting for direct plans. Likewise those who take independent advice on mutual funds from a mutual fund research company can also consider investing through direct plans.

Direct Plan vs. Standard Plan

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Standard / Regular Plan:

- Investors go through the distribution channel, whereby the investments are done through mutual fund distributors / agents / relationship manager / advisor
- Servicing issues are taken care of by the mutual fund distributor / agent / relationship manager / advisor
- Standard plan commands a high expense ratio
- Returns fetched under standard plan could be a little lower

Suitability ❯ Investors who may opt for the standard plan are those who are looking for convenience, getting service, not having access to mutual fund research and therefore do not mind paying a higher expense ratio and compromising on the returns a bit

Some Key Takeaway Points!

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- Care should be taken while selecting mutual fund schemes
- Have funds from the respective categories of mutual fund schemes as per your investment objectives
- Equity funds carry high risk
- Equity funds are suitable if you have a long-term investment horizon and wish to clock better real returns
- Debt funds are suitable if you are risk averse and do not mind compromising on real rate of returns
- Tactical allocation can be facilitated by hybrid funds

Some Key Takeaway Points!

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- Sector / thematic funds carry very high risk
- Diversified equity funds expose you to lower risk
- FoFs provide an opportunity to create a diversified portfolio of various mutual funds schemes by investing in a single fund
- Country or region specific funds and Offshore funds facilitate geographical diversification but expose you to regulatory, geopolitical risk, macroeconomic risk and currency risk
- Selection between dividend, growth and bonus option should be done carefully in alignment to your financial plan
- Opting for Direct Plan helps to clock better returns due to relatively low expense ratio charged

We now invite you to test your learning by taking up this simple quiz

(And win exciting prizes!)

Thank You For Participating!

Quick Quiz

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1) Which investment option in a mutual fund scheme is suitable for investors who are not in need of intermediate cash flows, but wish to compound the money invested?

   A. Dividend Payout
   B. Dividend Reinvestment
   C. Growth
   D. Bonus

2) FMPs are open-ended mutual fund schemes.

   A. True
   B. False

3) Investing in which of the following fund or funds carries currency risk?

   A. Country or Region Specific Funds
   B. Offshore Funds
   C. Debt Funds Exchange Traded Funds

Quick Quiz

4) Which of the following is not a style of investing

A. Value
B. Blend
C. Growth
D. Mid cap

5) Which of the following is not a hybrid fund?

A. Multi cap Fund
B. Balanced Funds
C. Monthly Income Plans
D. Capital Protection Funds

Mutual Fund Investments Are Subject To Market Risks, Read All Scheme Related Documents Carefully.

Franklin Templeton Asset Management (India) Pvt. Ltd.
Indiabulls Finance Centre, Tower 2,
12th and 13th floor, Senapati Bapat Marg,
Elphinstone (W)
Mumbai 400013
Tel (91-22) 6751 9100
Fax (91-22) 6639 1281
www.franklintempletonindia.com

Caveat (Arial Narrow 10pt.)