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THE PERFORMANCE OF BANKING FUNDS IN INDIA DURING THE PERIOD 2010 TO 2013

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ABSTRACT

The MF industry has the highest exposure to banking sector from August 2009 both in terms of percentage as well as in absolute terms. Market experts believe that expectation of rate cuts from Reserve Bank of India (RBI) has made equity fund managers raise their exposure in the sector. A steady rise in investment in bank shares in the last quarter of 2012 by mutual funds paved the way for entry of more players and investments in the sector, have given a further boost. Besides banking, the exposure to none of the sectors is in double digits, with software being the second-best with an 8.7% exposure. Hence, the need to evaluate the performance of banking funds. The data is collected from official website of Association of Mutual Funds in India (AMFI), Indian Banks Association (IBA), National Stock Exchange (NSE) and from respective websites of Asset Management Companies (AMCs). 'Descriptive Statistics' is employed. Annualised mean, annualised standard deviation and Systematic risk are calculated. Finally, risk adjusted performance using Sharpe Index is measured and funds are ranked. All the funds selected for the study have given significant returns than the market, with ICICI Prudential Banking and Financial Services fund and Reliance banking fund in the top two positions. The reason could be the fund managers of above mentioned funds have invested in highly performing stocks like SBI, ICICI bank, HDFC bank, PNB and Axis bank.

Keywords: Assets under Management, Banking funds, Portfolio turnover ratio, Standard deviation, Systematic risk.

JEL Classification: G10, G12, G20, G23

INTRODUCTION

The banking sector has been on a roll over the last couple of years, throwing up huge opportunities for wealth creation on the way. With economic liberalization, the banking sector has seen unprecedented growth along with remarkable improvements in its quality of assets as well as efficiency. The economic reforms totally have changed the banking sector. Earlier, the banking industry was dominated by public sector banks, but now the situations have changed. New generation banks with use of technology and professional management has gained a reasonable position in the banking industry. The position of banks have become very important in the course of working of the money market and hence the economy of a nation. Today Indian Banking is at the crossroads of an invisible revolution. The sector has undergone significant developments and investments in the recent past. Most of banks provide various services such as Mobile banking, SMS Banking, Net banking and ATMs to their clients. Table 1 highlights the ATMs, POS and number of outstanding credit and debit cards of various banks. State Bank of India is having the highest number of ATMs both on On-site as well as Off-site. On the other hand, On-line Point of Sales is highest for HDFC Bank Ltd .The table also clearly depicts that all the customers are using either ICICI bank's credit or debit card for payments at retail outlets.

Table 1. ATMs and POS of various banks as on April 2013

Bank Name	**ATMs**		**POS**		**No .of outstanding credit cards**	**No .of outstanding debit cards**
	On-site	**Off-site**	**On-line**	**Off-line**		
State Bank of India	15648	12626	74672	0	2598509	112240629
HDFC Bank Ltd.	4410	6461	241246	0	6532818	16000583
ICICI Bank Ltd.	3333	7263	238410	7008	2875459	18741998
Axis Bank Ltd.	2331	8908	216782	0	1108444	14512108
Punjab National Bank	3096	3282	9263	0	116580	20995371

Source: Indian Banks' Association (www.iba.org.in)

Table 2 portrays the transactions done (both in number as well as amount) by credit and debit cards by various banks. HDFC bank ranks in first position in making credit card transactions (Rs 542.79 million) while SBI ranks in first position in debit card transactions (Rs. 562598.50 million).

Table 2. Transactions done by Credit and Debit Cards by various banks

Bank Name	**Credit Cards**				**Debit Cards**			
	No. of Transactions (Actuals)		**Amount of transactions (Rs Million)**		**No. of Transactions (Actuals)**		**Amount of transactions (Rs Million)**	
	ATM	**POS**	**ATM**	**POS**	**ATM**	**POS**	**ATM**	**POS**
State Bank of India	33560	5039611	160.00	12690.00	193041000	9941000	562598.50	16314.10
HDFC Bank Ltd.	82730	10374501	542.79	35837.44	30450447	7539002	133989.71	11767.89
ICICI Bank Ltd.	8150	5241129	39.40	13941.70	28730671	7394571	131176.40	12962.20
Axis Bank Ltd.	9214	1936645	31.77	5845.47	26654823	4040047	113441.89	6884.85
Punjab National Bank	2245	155564	9.82	337.13	46147706	1913572	75036.57	2020.85

Source: Indian Banks' Association (www.iba.org.in)

Table 3. Deposits, Total income and Net Profit of various banks

Bank Name	Deposits			Total income			Net profit		
	2010	**2011**	**2012**	**2010**	**2011**	**2012**	**2010**	**2011**	**2012**
State Bank of India	804116	933933	1043647	85962	97219	120873	9166	8265	11707
HDFC Bank Ltd.	167404	208586	246706	20156	24263	32530	2949	3926	5167
ICICI Bank Ltd.	202017	225602	255500	33185	32622	41045	4025	5151	6465
Axis Bank Ltd.	141300	189238	220104	15584	19787	27415	2515	3388	4242
Punjab National Bank	249330	312899	379588	25032	30599	40631	3905	4433	4884

Source: Indian Banks' Association (www.iba.org.in)

From table 3, it is clearly evident that all the banks are showing significant growth in deposits, total income and net profit. Axis Bank stands in the first position with highest growth rate of deposits and total income 55.77% and 75.92% respectively. Punjab National Bank ranks in the second position while HDFC Bank in the third. If net profits are taken into consideration, HDFC ranks in top position with 75.22% followed by Axis bank and ICICI bank.

The banking sector forming a portion of the financial sector primarily works as a financial intermediary generating money supply. Banking system and the Financial Institutions play very significant role in the economy. It is central to a nation's economy as it caters to the needs of credit for all the sections of the society. An efficient banking system caters to the needs of high end investors by making available high amounts of capital for big projects in the industrial, infrastructure and service sectors. On the other hand, the banks and the financial institutions also cater to another important need of the society i.e. mopping up small savings at reasonable rates with several options like savings accounts, recurring deposits and time deposits. Another option is to invest in the stocks or mutual funds. Mutual Fund houses often come out with different schemes. One among them is Sectoral Funds.

As the name implies, Sectoral funds are those mutual funds which invest in a particular sector or industry of the market, e.g. infrastructure, banking, pharma, information technology etc. Sector funds are riskier than equity diversified funds since they invest in shares belonging to a particular sector which gives them fewer diversification opportunities. Sector funds could be either leaders or laggards of the season which means, at times they do better than the broader market and at others, and they lag way behind. If one anticipates higher returns and are willing to take risk, sector funds could be best option. Returns from these tend to be cyclical, and can even be timed. For instance, with interest rates likely to head down, sectors like automobile or banking tend to do well. Hence, it's easier for investors to time their entry into these sectors. Most sector funds tend to attract investors when stocks have peaked. For instance, infrastructure funds collected money when infra stocks were at their peak. Similarly, timing the exit is equally important. For sector funds, it is advisable to look at profits and not the holding period. So, set a profit target and exit once the target is reached. Sector funds can also go out of favour, depending on the market circumstances. That is why a sector fund requires far more active monitoring than equity-oriented balanced funds or large-cap funds. When sectors are not doing well, and it is hard to find any reliable sector, investing in banking sector could be the best option.

Unlike infrastructure funds, where the investment universe is quite large and diversified and these funds invest in stocks of companies related to the infrastructure space and ancillary industries like banking and financial services, energy utilities, media and consumer goods, the banking sector funds are sector oriented and these funds invest in stocks which are concentrated to banking stocks. According to the records of Capital market regulator SEBI, mutual fund industry's investment in banking stocks stood at Rs 43,659 crore at the end of December 2012, which was 21.15 % of the industry's total equity assets under management (AUM) of Rs 2.06 lakh crore. The Mutual Fund Industry has the highest exposure to banking sector from August 2009 both in terms of absolute value as well as percentage. In the year 2012, banking funds was the only sector which recorded double digit exposure. The year 2012 has seen a consistent growth in investment in banking stocks by the industry's equity fund managers. During the year, their exposure has risen from 17.23 % of total AUM to 21.15%. In absolute terms, the investment in banking stocks has grown from Rs 32,380 crores to Rs 43,659 crores. For those investors who want exposure to a sector but not the risk of under-performance due to the fund manager, investing in passive sector funds like banking sector funds could be the best option.

OBJECTIVES OF THE STUDY

- To analyse the performance of banking funds using mean return and variance analysis.
- To find out the systematic risk for the funds under study.
- To evaluate the performance of banking funds using risk adjusted measure as suggested by Sharpe.

DATA

Funds which are in existence for a period of 3 years or more are only considered for the study. All the funds chosen for the sample are of growth option. The data is collected from official website of Association of Mutual Funds in India (AMFI), National Stock Exchange (NSE) and from respective websites of Asset Management Companies (AMCs). Three years data from April 1st 2010 to March 31st 2013 for these selected funds (5 banking funds) is collected. Nifty is considered as Proxy for the market. Risk free rate is taken as 6 %.

METHODOLOGY

The performance of banking funds is evaluated using daily NAVs. Daily returns are computed making use of daily NAVs. Further, 'Descriptive Statistics' is employed to obtain mean and standard deviation. Thereafter annualised mean and annualised standard deviation are calculated.

Systematic risk (beta) for the funds is calculated with respect to Nifty. Finally, risk adjusted performance using Sharpe Index is measured.

The following formulae are used

Return R_t = ln (NAV_t - NAV_{t-1}) * 100

Where Rt = Return for the period t

ln = log normal or natural logarithm

NAV_t = Net Asset Value of fund in period t

NAV_{t-1} = Net Asset Value of fund in period t-1

For computing annualised returns and annualised standard deviation, the following formulae are used.

Annualised returns = (avg daily returns * T)/3

Annualised std. deviation = (std. deviation *sqrt (T))/3

Where T = number of trading days.

Systematic risk is calculated as

$$\beta = (\sum(X - X_i)(Y - Y_i)) / \sum(X - X_i)^2$$

Where β = beta

$(X - X_i)$ = deviation of market return and market mean return

$(Y - Y_i)$ = deviation of fund return and fund mean return

Sharpe Index is computed as

$$S_i = (r_p - r_f) / \sigma_p$$

Where S_i= Sharpe index

r_p = return on portfolio

r_f = risk free rate

σ_p = total risk of portfolio

FINDINGS

Table 4. Annualised return and Annualised Standard Deviation of selected funds

S. no.	Scheme Name	Annualised Return	Annualised Std Dev
1	ICICI Prudential Banking and Financial Services Fund	9.49	12.22
2	Reliance Banking Fund	9.47	12.09
3	UTI Banking Sector Fund	6.41	13.40
4	Sahara Banking and Financial Services Fund	5.59	12.22
5	Sundaram Financial Services Opportunities Fund	3.75	12.57
	CNX Nifty	2.39	10.0

Table 4 gives a glimpse of annualised returns and annualised standard deviation of banking funds and CNX Nifty .From the table; it is clearly evident that all the funds are giving returns above the market. On the other hand, the risk associated with the funds is above the market, with UTI Banking Sector fund having the highest standard deviation of 13.40. Of all the 5 funds considered for the study, ICICI Prudential Banking and Financial Services fund is performing better with highest returns, followed by Reliance Banking fund and UTI Banking Sector fund. Though Sahara Banking and Financial Services fund as well as Sundaram Financial services Opportunities Fund generated higher returns than the market, they had to satisfy in fourth and fifth positions respectively.

Table 5. Systematic risk of banking funds

S. no	Scheme Name	Beta
1	UTI Banking Sector Fund	1.192
2	Sundaram Financial Services Opportunities Fund	1.101
3	ICICI Prudential Banking and Financial Services Fund	1.090
4	Sahara Banking and Financial Services Fund	1.076
5	Reliance Banking Fund	1.047

Table 5 portrays the systematic risk (beta) for banking funds. The highest systematic risk is for UTI Banking Sector fund, followed by Sundaram Financial Services Opportunities fund and ICICI Prudential Banking and Financial Services Fund. Reliance banking fund has got the least systematic risk.

Table 6. Sharpe Index of banking funds

Sno	Scheme Name	Sharpe Index
1	Reliance Banking Fund	0.778
2	ICICI Prudential Banking and Financial Services Fund	0.772
3	UTI Banking Sector Fund	0.474
4	Sahara Banking and Financial Services Fund	0.453
5	Sundaram Financial Services Opportunities Fund	0.293

Table 6 gives a brief look about the Sharpe Index of banking funds selected for the study. It is observed that Reliance Banking fund ranks in first position with highest Sharpe Index followed by ICICI Prudential Banking and Financial Services Fund and UTI Banking Sector fund. Sundaram Financial Services Opportunities Fund ranks in fifth position with least Sharpe Index.

DISCUSSION

Table 7. Assets under Management of selected funds (in crores)

Fund Name	As on 30April 2010	As on 30April 2011	As on 30April 2012
ICICI Prudential Banking and Financial Services Fund	112.51	N.A	140.76
Reliance Banking Fund	1126.98	1661	1731
UTI Banking Sector Fund	N.A	305.31	352.58
Sahara Banking and Financial Services Fund	11.96	24.56	20.80
Sundaram Financial Services Opportunities Fund	179	261	197

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Table 8. Portfolio Turnover ratios of selected funds (in times)

Fund Name	As on April 30 2010	As on April 30 2011	As on April 30 2012
ICICI Prudential Banking and Financial Services Fund	1.38	N.A	0.76
Reliance Banking Fund	0.27	0.44	0.47
UTI Banking Sector Fund	N.A	2.71	3.22
Sahara Banking and Financial Services Fund	2.24	2.28	2.82
Sundaram Financial Services Opportunities Fund	N.A	N.A	N.A

Table 9. Standard Deviation of banking funds

Fund Name	As on April 30 2010	As on April 30 2011	As on April 30 2012
ICICI Prudential Banking and Financial Services Fund	38.89	N.A	30.76
Reliance Banking Fund	5.27	4.95	4.03
UTI Banking Sector Fund	N.A	22	27.3
Sahara Banking and Financial Services Fund	N.A	N.A	N.A
Sundaram Financial Services Opportunities Fund	39.07	35.09	34.68

Assets under management are generally looked at as a measure of success against the competition. Table 7 gives a glimpse about assets under management of selected funds. It is observed that except Sahara Banking and Financial Services Fund and Sundaram Financial Services Opportunities Fund, all the funds AUM has augmented over the period. The reasons for the decline in AUM could be with the increase in the Net Asset Values of banking funds; many unit holders may have redeemed their units.

Turnover ratio denotes the percentage of the holdings of the fund that changes each time. Higher turnover ratio implies higher the volume of trading performed by the fund. In the year 2012, for most of the funds, portfolio turnover ratio is high compared to previous years. UTI Banking Sector fund has got the highest turnover ratio of all funds considered under study which indicates that fund manager has been very aggressive in holding the stocks of a portfolio. Besides, the systematic risk of UTI Banking Sector fund is also high which signifies that possibility of losses associated with this fund could be more.

Standard deviation is the most appropriate measure for measuring the risk of a fund. The fund with higher standard deviation implies greater volatility. Table 9 portrays the information about standard deviation of all sample funds. High standard deviation of Sundaram Financial Services opportunities fund implies that the stocks of this particular fund have been more volatile .The fund manager has been very aggressive in holding the stocks of portfolio and failed to identify the high performance stocks in the banking industry.

CONCLUSION

Most sector funds tend to attract investors when stocks have peaked. Returns from these funds tend to be cyclical. When the interest rates are likely to fall down, banking sector funds tend to perform well. Moreover, when sectors are not performing well, and it is hard to rely on any sector, investing in banking space could be a better option. At the same time, timing of entry and exit into these sectors is equally important. The fund managers of

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Reliance banking fund and ICICI prudential Banking and Financial Services fund have invested in stocks like SBI, ICICI bank, HDFC bank, Axis bank and Punjab National Bank. As the performance of the above said banks is outstanding, this could be the reason for better performance of Reliance banking fund as well as ICICI prudential Banking and Financial Services fund.

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