

## Mutual Fund Update

March 19, 2024

### Stress Test Analysis of Mid cap And Small Cap Schemes

The Securities and Exchange Board of India (SEBI) has asked asset management companies (AMCs) to be cautious and consider moderating inflows and rebalancing portfolios of mid-cap and small-cap schemes. Accordingly, the Association of Mutual Funds in India (AMFI) has also asked AMCs to disclose stress test results every 15 days to comply with the recent SEBI mandate. Mid-cap and small-cap categories schemes have seen huge inflows recently and the purpose of the stress test is to ascertain how soon the scheme can liquidate their portfolio, if investor were to rush for redemption in adverse market conditions.

### What is a Stress Test?

Mid-cap and small-cap category schemes saw huge inflows following stellar performance in 2023. As a result, the SEBI directed fund houses to run a liquidity analysis based on a specific methodology to evaluate how many days it will take for any scheme to liquidate 25% and 50% of its portfolio after removing the bottom 20% of the portfolio based on liquidity. This test will indicate how quickly the schemes can sell their holding if the market is in an adverse condition and investors want to exit their investment.

### Stress test Methodology

- **Liquidation of 50% and 25% of portfolio:** A scheme's liquidity is being tested under scenarios, where 50% and 25% of a portfolio is taken for redemption and the number of days it will take to liquidate these holdings to honour those redemptions.
- **Removing bottom 20% of portfolio based on scrip liquidity:** The stress test is conducted after removing bottom 20% of portfolio based on liquidity. This allows fund manager to hold these stocks for the long term and would not want to sell when there is a redemption pressure.
- **Average trade volume:** The methodology considered scenarios with only 10% market participation for the schemes assuming an average trading volume of three months would triple during stress periods.

The stress test is a very good measure to increase the transparency in the system. Another important thing in the stress test result, is the top 10 investor categories. If the fund has a high percentage of top 10 investors, there would be redemption pressure if they decided to exit and could affect a scheme performance.

## Stress test results of Mid-cap schemes

Mid Cap Funds										
Scheme Name	AUM (Rs. Cr)	Stress Test		Concentration					Volatility	
				Liability side	Asset side (AUM held in)				Portfolio Annualised Standard Deviation (%)	Benchmark Annualised Standard Deviation (%)
		50% portfolio	25% portfolio	Top 10 investor (%)	Large Cap (%)	Mid Cap (%)	Small Cap (%)	Cash (%)		
		(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)
Kotak Emerging Equity Fund	39,732	34	17	4.9	12.83	69	15.5	2.67	11.84	14.67
SBI MAGNUM MIDCAP FUND	16,467	24	12	1.66	7.75	65	18.48	8.69	11.55	14.67
HDFC Mid-Cap Opportunities	60,194	23	12	1.41	12.97	65.7	14.54	6.8	13	14.67
DSP Midcap Fund	16,302	17	9	1.82	7.67	67.8	20.82	3.68	14.03	14.67
Axis Midcap Fund	25,248	12	6	1.34	21.87	68.4	4.65	5.07	11.63	17.89
Motilal Oswal Midcap Fund	8,491	10	5	23.03	17.95	65.4	1.94	14.69	13.2	14.5
Mirae Asset Midcap Fund	14,543	8	4	2.05	8.9	67	21.63	2.52	13.95	14.67
HSBC Mid Cap Fund	9,722	7	3.5	1.56	14.77	68	16.68	0.58	12.36	14.67
Nippon India Growth Fund	24,494	7	4	1.54	18.4	66.7	13.53	1.36	4.03	4.24
Quant Mid Cap Fund	5,443	6	3	2.99	27.36	69.6	0	3.07	16.59	14.67
UTI - Mid Cap Fund	10,046	4.22	2.11	2.08	9.97	66	19.83	4.24	13.03	14.67
Aditya Birla Sun Life Midcap Fund	4,982	4	2	4.14	13.01	65.3	19.35	2.33	13.56	14.67
Franklin India Prima Fund	10,179	4	2	3.74	16.89	67.5	12.64	2.96	13.61	14.69
PGIM India Midcap Opportunities Fund	9,971	4	2	1.43	17.31	67.2	12.83	2.7	18.13	18.67
Sundaram Mid Cap Fund	10,157	4	2	1.83	19.27	65.4	10.95	4.4	13.4	14.7
Tata Mid Cap Growth Fund	3,295	3	2	5.18	8.09	67.4	23.12	1.44	12.78	14.67
Edelweiss Mid Cap Fund	5,070	2	1	0.02	0.17	0.67	0.14	0.03	0.14	0.12
ICICI Prudential MidCap Fund	5,486	2	1	5	13	68	11	8	15	15
Invesco India Midcap Fund	4,238	2	1	3.02	17.06	65.2	16.77	1	13.58	14.15
Canara Robeco Mid Cap Fund	2,041	1.6	0.8	4.98	19.08	68.1	10.22	2.64	-	-
Baroda BNP Paribas Mid Cap Fund	1,791	1	1	3.77	10.86	71.8	13.84	3.53	12.31	14.67
WhiteOak Capital Mid Cap Fund	1,627	0.68	0.34	5.85	7.82	67	22.54	1.4	-	-
JM Midcap Fund	813	0.6	0.3	15	4.48	67.2	26.74	1.54	-	-
Mahindra Manulife Mid Cap	2,154	0.57	0.29	2.06	14.26	65.1	13.41	7.25	14.77	14.67
BANDHAN MIDCAP FUND	1,073	0.45	0.22	3.38	13.2	67.7	15.5	3.69	0	0
Union Midcap Fund	1,049	0.32	0.16	2.91	13.79	72.3	10.29	3.59	13.93	14.15
ITI Mid Cap Fund	714	0.18	0.09	3.42	17.3	66.5	11.86	4.34	-	14.67
Taurus Mid Cap Fund	117	0.1	0.1	4.77	2.28	69.8	25.08	2.83	16.19	15.6
LIC MF Mid Cap Fund	243	0.09	0.05	4.77	24.3	65.5	7.77	2.48	14.49	14.67

Note - The above table sorted based on the stress test for 50% of portfolio.

## Stress test analysis (Mid-cap)

- The largest AUM scheme of "HDFC Mid Cap Opp" would require 23 days to liquidate 50% of its holding and 12 days to liquidate 25% of its holding. The "Kotak Emerging Equity Scheme" require maximum days of 34 days and 17 days to liquidate 50% and 25% of its holdings respectively.
- The scheme with higher AUM will have a higher proportion of their holdings in illiquid or low liquidity stock. For schemes upto Rs.15,000 crore of AUM would require on an average 3 days to liquidate 50% of holdings and for the schemes above Rs,15,000 crore of AUM, on an average this would take 20 days.
- The top 50 schemes have lower standard deviation compared to its benchmark.
- The "Motilal Oswal Midcap Fund" has AUM of Rs.8491 crore but still require 10 days to liquidate 50% of its holdings as compared to average of 6 days. The "Nippon India Growth Fund" is in our top picks and has AUM of Rs.24,494 crore and it require only 7 days to liquidate 50% of its holding.

## Stress test results of small-cap schemes

Small Cap Funds										
Scheme Name	AUM (Rs. Cr)	Stress Test		Concentration					Volatility	
				Liability side	Asset side (AUM held in)				Portfolio Annualised Standard Deviation (%)	Benchmark Annualised Standard Deviation (%)
		50% portfolio	25% portfolio	Top 10 investor (%)	Large Cap (%)	Mid Cap (%)	Small Cap (%)	Cash (%)		
		(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)
SBI SMALL CAP FUND	25,534	60.0	30.0	0.6	6.1	6.7	80.7	6.5	11.4	17.2
HDFC Small Cap Fund	28,597	42.0	21.0	3.0	4.7	7.7	77.0	10.6	15.3	17.2
Tata Small Cap Fund	6,274	35.0	18.0	3.0	0.0	1.8	93.8	4.4	13.7	17.6
Kotak Small Cap Fund	14,189	33.0	17.0	1.2	5.5	17.2	72.9	4.5	13.2	17.6
DSP Small Cap Fund	13,703	32.0	16.0	1.6	-	6.9	87.6	5.6	15.3	17.2
Axis Small Cap Fund	19,604	28.0	14.0	1.2	2.3	19.6	67.5	10.7	16.9	19.5
Nippon India Small Cap	46,030	27.0	13.0	0.9	13.5	14.7	67.5	4.4	4.1	5.1
Quant Small Cap Fund	17,233	22.0	11.0	2.1	28.4	0.2	65.9	5.5	19.7	17.6
HSBC Small Cap Fund	13,744	14.5	7.3	0.9	2.8	21.8	73.2	2.2	14.6	17.6
Canara Robeco Small Cap Fund	9,586	13.5	6.7	1.5	11.1	14.9	70.7	3.3	15.2	18.1
Franklin India Smaller Companies	11,825	12.0	6.0	2.1	3.2	13.6	75.8	7.4	13.9	17.6
Aditya Birla Sun Life Small Cap	5,382	10.0	5.0	2.5	1.9	12.8	81.5	3.9	15.0	17.2
ICICI Prudential Smallcap	7,414	10.0	5.0	2.0	7.0	20.0	67.0	6.0	14.0	18.0
Sundaram Small Cap	3,024	5.0	3.0	3.2	11.5	10.4	73.2	4.8	14.2	17.6
UTI Small Cap Fund	3,649	4.3	2.2	1.2	0.0	13.3	82.5	4.1	13.4	17.6
Invesco India Smallcap	3,705	4.0	2.0	3.4	3.9	23.7	69.2	3.2	15.3	17.2
Mahindra Manulife Small Cap	3,533	3.0	1.5	14.3	15.2	5.5	69.7	9.6	-	15.6
Edelweiss Small Cap	3,142	3.0	2.0	0.0	-	0.3	0.7	0.0	0.1	0.1
Motilal Oswal Small Cap	1,492	3.0	2.0	12.5	10.1	9.0	72.1	8.8	-	-
PGIM India Small Cap	1,436	3.0	1.0	3.1	-	16.5	78.6	4.9	-	-
BANDHAN Small Cap	4,385	2.6	1.3	11.1	7.6	9.7	72.4	10.3	16.6	6.0
BANK OF INDIA SMALL CAP FUND	920	2.0	1.0	2.2	5.8	9.2	73.3	11.9	21.8	26.9
Union Small Cap Fund	1,328	1.3	0.7	3.0	0.0	9.6	86.2	4.1	14.5	17.2
ITI Small Cap Fund	1,766	1.2	0.6	22.0	13.7	19.4	66.2	0.7	16.3	17.6
Baroda BNP Paribas Small Cap Fund	1,325	1.0	1.0	2.4	2.8	14.4	79.2	3.6	0.0	0.0
QUANTUM SMALL CAP	39	1.0	1.0	6.8	8.3	2.5	70.6	18.6	-	14.6
LIC MF Small Cap Fund	212	0.5	0.2	4.8	1.5	8.0	87.1	3.6	13.3	17.6

Note - The above table sorted based on the stress test for 50% of portfolio.

## Stress test analysis (Small Cap schemes)

- It would take on average 14 days for small cap schemes to liquidate 50% of holdings.
- The schemes with a large corpus will have a higher proportion to low liquidity stocks. The small cap schemes with AUM of less than Rs.10,000 crore would require average 6 days to liquidate 50% of holdings compared to average 30 days for schemes with AUM of more than Rs.10,000 crore.
- Within top 10 schemes based on AUM, the "SBI SMALL CAP FUND" require maximum number of days of 60 days to liquidate 50% of their holdings and 30 days to liquidate 25% of their holdings.
- The "Tata Small Cap" scheme has AUM of Rs.6,274 crore only but still require 35 days to liquidate 50% of holdings and 18 days to liquidate 25% of their holdings. This is significantly high as compared to similar-sized peers.

## Sharekhan Top Equity Picks in Mid cap and Small Cap categories

Scheme Name	Category	AUM (Rs. Cr)	Stress Test		Concentration					Volatility	
					Liability side	Asset side (AUM held in)				Portfolio Annualised Standard Deviation (%)	Benchmark Annualised Standard Deviation (%)
			50% portfolio	25% portfolio	Top 10 investor (%)	Large Cap (%)	Mid Cap (%)	Small Cap (%)	Cash (%)		
			(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)
HDFC Small Cap Fund	Small Cap	28,597	42	21	3.0	4.7	7.7	77.0	10.6	15.3	17.2
Tata Small Cap Fund	Small Cap	6,274	35	18	3	0	1.83	93.77	4.4	13.7	17.57
Kotak Emerging Equity Fund	Mid Cap	39,732	34	17	4.9	12.8	69.0	15.5	2.7	11.8	14.7
DSP Small Cap Fund	Small Cap	13,703	32	16	1.6	-	6.9	87.6	5.6	15.3	17.2
Nippon India Small Cap Fund	Small Cap	46,030	27	13	0.9	13.5	14.7	67.5	4.4	4.1	5.1
SBI MAGNUM MIDCAP FUND	Mid Cap	16,467	24	12	1.7	7.8	65.0	18.5	8.7	11.6	14.7
HDFC Mid-Cap Opportunities Fund	Mid Cap	60,194	23	12	1.4	13.0	65.7	14.5	6.8	13.0	14.7
HSBC Small Cap Fund	Small Cap	13,744	14.5	7.25	0.9	2.8	21.8	73.2	2.2	14.6	17.6
ICICI Prudential Smallcap Fund	Small Cap	7,414	10	5	2.0	7.0	20.0	67.0	6.0	14.0	18.0
Mirae Asset Midcap Fund	Mid Cap	14,543	8	4	2.1	8.9	67.0	21.6	2.5	14.0	14.7
Nippon India Growth Fund	Mid Cap	24,494	7	4	1.5	18.4	66.7	13.5	1.4	4.0	4.2
Edelweiss Small Cap Fund	Small Cap	3,142	3	2	0.0	-	0.3	0.7	0.0	0.1	0.1
BANDHAN Small Cap Fund	Small Cap	4,385	2.61	1.31	11.08	7.6	9.7	72.4	10.29	16.62	5.98
Edelweiss Mid Cap Fund	Mid Cap	5,070	2	1	0.0	0.2	0.7	0.1	0.0	0.1	0.1
Invesco India Midcap Fund	Mid Cap	4,238	2	1	3.0	17.1	65.2	16.8	1.0	13.6	14.2
Baroda BNP Paribas Mid Cap Fund	Mid Cap	1,791	1	1	3.8	10.9	71.8	13.8	3.5	12.3	14.7

## Key Findings

- The scheme's liquidity is just one of many parameters and not the only thing which determines its long-term performance.
- This stress test analysis shows that mid cap and small cap schemes are risky and therefore suitable for investors who are ready to take high risk and for a long-term tenure.
- Within our SK approved MF Top Picks the "HDFC small Cap" scheme require maximum number of days of 42 days to liquidate 50% of holdings as compared to the category average of 14 days and this can be attributed to the corpus the scheme is managing. An average of 36 days is required to liquidate 50% of holdings for the top 5 schemes based on AUM and within the category, the "SBI SMALL CAP FUND" requires the maximum number (60 days) to liquidate 50% of their holdings.

## Call to Action for Investor

- The "Tata Small Cap Fund" requires 35 days to liquidate 50% of holdings and this is significantly higher as compared to its size as the similar size schemes of "ICICI and Aditya Birla Sun Life" require around 10 days to liquidate 50% of their holdings. Investors should shift their "Tata Small Cap Fund" allocation to "HSBC Small Cap Fund".
- Considering the current mid-cap and small cap schemes performance, the portfolio allocation of mid cap and small cap could have increased compared to other categories and this is the time to rebalance the portfolio as per the risk appetite of the investor and with the help of expert.
- The investor who want to invest lumpsum in mid-cap and small-cap schemes should invest in staggered way and investor with SIP investment, should continue their long-term SIPs.

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