MOTILAL OSWAL MUTUAL FUND INDEX FUNDS

Motilal Oswal Presents

Investors' Survey on Passive Funds - 2023

Results are in - ***Investors warming up to passive funds in India!***

The investment landscape in India is evolving rapidly on the back of a supportive regulatory environment, rise of digital investing platforms and product innovation by the mutual fund houses. Investors have started to realize the importance of mutual funds for long-term wealth creation, not just in the metro cities but also in many tier-2 and tier-3 cities.

Within the overall mutual fund industry, passive funds have taken center-stage over the last few years, **gaining market share from 1.4% of AUM in 2015 to over 17% today**.

A passive fund is a type of Index Fund or ETF that aims to provide returns that are very similar to the underlying benchmark, like the Nifty 50 or Nifty 500. To achieve this, passive funds hold the same portfolio as underlying index in terms of stocks and their weights. Passive funds offer several benefits to investors – they are **easy to understand, effective for wealth creation, and are economical** in the sense that they have lower expenses.

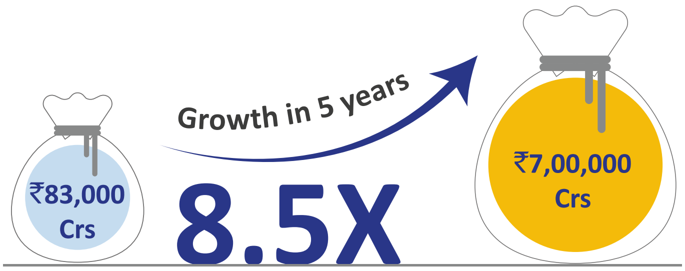
Investors warming up to Passive Funds

A recent survey of more than 2,000 investors by Motilal Oswal Mutual Fund found that:

61% **of investors say they have invested in at least 1 passive fund, underscoring the fast-growing adoption of passive funds in India.**

Exponential AUM growth

At the end of FY-2018, the AUM of all passive funds put together stood at around ₹83,000 Crs. This now stands at more than ₹7,00,000 Crs as of Mar-2023, swelling 8.5x in just 5 years at a staggering 54% CAGR.

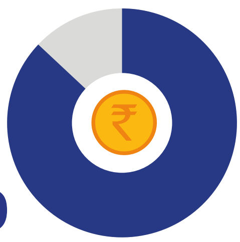


Index Funds lead the way

Interestingly, investors seem to have a preference between Index Funds & ETFs with 87% of respondents investing via Index Funds vs just 41% investing via ETFs. We think this is because ETFs are bought and sold on the stock exchanges and require an investor to have a demat account. On the other hand, investing in Index Funds has no such requirement and is comparatively straight-forward similar to any mutual fund transaction.

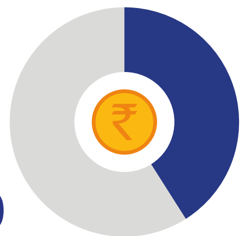
Investing via Index Funds

87%



Investing via ETFs

41%



So, why invest in passive funds?

On being asked why they chose to invest in passive funds, 57% of respondents said the low-cost nature of passive funds is the largest factor, followed by the simplicity of these funds (56%), and the fact that they tend to deliver market returns (54%).

57% Low Cost

56% Simplicity

54% Market Returns

How investors select a passive fund?

The survey results show that investors are most concerned with the expense ratio (68% of respondents) of a passive fund when making a decision about which fund to invest in. This is followed by the brand of the mutual fund house (58%), fund size / AUM (43%), and tracking error (34%).

68% Expense Ratio

58% Mutual Fund Brand

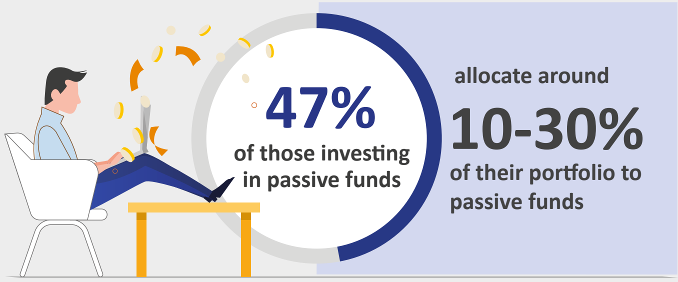
43% Fund Size / AUM

34% Tracking Error

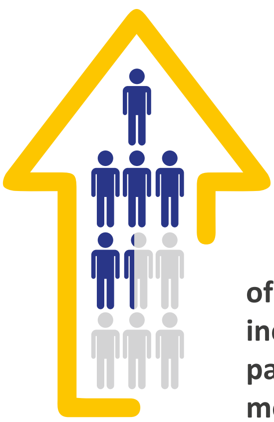
We feel that this may be slightly misplaced, and investors might be better off choosing funds with a low tracking error. Tracking error is a measure that tells you how closely any fund is following or "tracking" its benchmark index. It shows the amount of variability (or difference) between the returns of the fund and the returns of the benchmark. In simpler terms, a lower tracking error indicates that the fund closely follows the benchmark, while a higher tracking error suggests more divergence.

Investor preferences for allocations to passive funds

Nearly half of those investing in passive funds allocate 10-30% of their portfolio to passive funds. About 15% allocate 31-50%, and 12% have allocated more than 50% of their portfolio. On the other hand, 28% of investors have a less than 10% allocation to passive funds.



Increasing allocations to Passive Funds



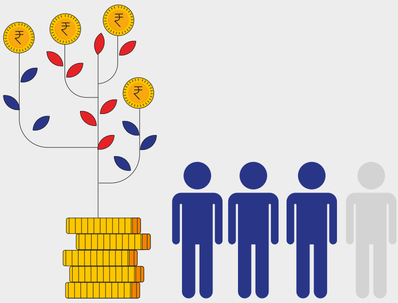
53%

of investors say they increased their allocation to passive funds in the last 12 months

More than half of the respondents said that they had increased their allocation to passive funds in the last 12 months. 1 in 4 investors said that they are planning to increase their allocation to passive funds in the future.

These trends indicate that Indian investors have started warming up to passive funds over the last few years. This is very encouraging for the industry and is broadly in-line with what we have seen in the United States where passive funds account for more than half of all equity assets.

Investors prefer SIPs over Lumpsums, Social Media over News Outlets



3 in 4

Investors prefer to invest using SIP's

More than 75% of respondents said that they preferred to invest regularly every month using SIPs, while only 42% said that they leaned towards Lumpsum. Interestingly, the preference for SIPs was equally strong among those who invest in passive funds and those who do not.

This universal preference for SIPs shows that they are simple, yet very effective in long-term wealth creation. The more disciplined approach to investing has also proven to be a great way to tide over market volatility, allowing investors to cut through the noise. As of Mar-2023, monthly SIP inflows crossed the ₹14,000 Crs mark for the first time, staying above the ₹10,000 Crs mark for 19 months straight.

Investors relying more on Social Media

60%

of respondents get information on markets and investments from Social Media platforms

More than 60% of respondents said that they get information on markets and investments from Social Media platforms like Twitter, Instagram, etc. On the other hand, only around 26% said they follow traditional news/media outlets for information related to investing. There was a higher preference for social media in those that do not invest in passive funds, while the passive fund investors turned more towards newsletters and blogs online.

Most investors trust their own research

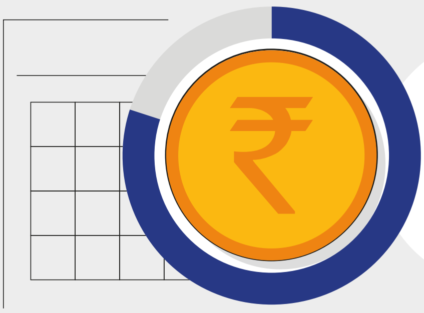
3 in 4

Investors make investment decisions based on their own research

Nearly 75% of all respondents said that they relied primarily on their own research while making investment decisions, while ~18% said that their investment decisions were influenced by friends & family. Interestingly, those who do not invest in passive funds were more likely to involve their financial advisors in making investment decisions while those who invest in passive funds were more likely to make their own investment decisions.

Most investors want to 'Sit tight'

More than 80% of respondents said that they were planning to hold their investments for more than 3 years, while 16% planned to hold for 1-3 years. Only 3% of investors said that they were looking to liquidate their investments in less than a year.



More than **80%**

of investors plan to hold their investments for more than 3 years

This trend is very encouraging and it is great to see the average Indian investor have such a clear preference for holding their investments for the long term. The mindset of long-term investing allows investors to ignore short-term market fluctuations and benefit from the long-term growth potential of companies. It also allows the investment portfolio to enjoy the benefit of compounding of returns. All of this increases the likelihood of achieving one's financial goals.

Factor Investing gains traction with Quality & Value in the lead

Nearly 30% of the respondents said that they were aware of Factor / Smart-Beta funds. However, only 13% said that they had invested in at least 1 such Factor fund. Within the respondents that did invest in Factor funds, 57% had invested in funds based on the Quality factor while 46% invested in Value factor. Momentum and Low Volatility factors were slightly less popular with participation from roughly 40% of investors.

- Value
- Momentum
- Quality
- Low volatility

30%

of investors say that they are aware of Factor / Smart-Beta funds

Smart Beta funds are a type of passive investment fund that use a rules-based approach to selecting stocks, rather than the traditional market-cap weighting approach. They sit between traditional active and passive styles of investing and aim to offer the best of both worlds. Given that this category is fairly new in India and is largely unexplored by investors and distributors alike, these are encouraging numbers.

Wrapping up – encouraging trends for the industry

INVESTORS ARE WARMING UP TO PASSIVE FUNDS

The investment landscape in India is evolving rapidly, with investors increasingly warming up to passive funds. This is due to a number of factors, including the low cost of passive funds, their simplicity, and their ability to deliver market returns. Investors are also increasingly aware of the benefits of factor investing, that sits between traditional active and passive investing styles. As the Indian investment market continues to grow and mature, it seems likely that passive funds will continue to gain traction. This is good news for investors, as passive funds offer a simple and cost-effective way to build wealth over the long term.

Annexure

Objective of this survey

The rationale behind conducting this survey was to understand:

- **Investor awareness of passive funds -** How aware are investors in India about passive funds? Do they understand the different options that are available to them?
- **Factors that drive investment decisions -** What sources of information do investors rely on when making investment decisions? What factors are most important to them when choosing a passive fund?
- **Challenges faced by investors -** What challenges do investors face when trying to invest in passive funds? Are there any gaps that need to be addressed?

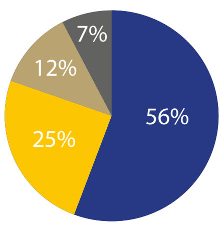
The findings of this survey can help educate investors about the benefits of passive investing. Further, they can also be used by mutual fund companies, regulators, and other stakeholders to improve the availability and accessibility of passive funds in India.

Approach to the Survey

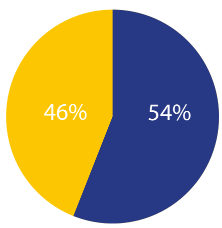
We conducted an online survey from February to May 2023 where we collected over 2,000 responses from all around the country. The survey was open to everyone, including investors of Motilal Oswal Mutual Fund (active & passive funds) as well as those not invested with us. We ended up with a good pool of respondents with a variety of age groups and income levels. As only mutual fund investors were targeted, it may not be appropriate to generalise the findings for the entire population as only a small fraction (less than 5%) of Indians actually invest in mutual funds. Therefore, findings must be viewed in context of mutual fund investors only.

There were some questions in the survey where respondents could choose multiple answers. Hence, responses for these questions will not add up to 100%.

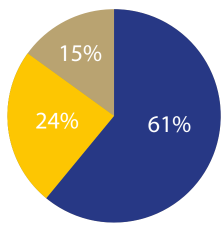
Overview of basic demographic data of the respondents



56% of the respondents were in the 18 – 35 age bracket while roughly 7% were older than 65.



54% of the respondents were staying in a metropolitan city.



61% of the respondents said their annual income was less than 10 lakhs, while only 15% earned more than 20 lakhs

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