Source : www.thehindu.com Date : 2018-09-24

DECODING TOTAL EXPENSE RATIO

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Capital Market & SEBI

Last week, Securities and Exchange Board of India (SEBI) announced changes to total expense ratio (TER) of mutual funds. **Srikanth Meenakshi** *, founder and chief operating officer, FundsIndia.com explains about the metric. Edited excerpts:*

What is total expense ratio and why is it important for investing in mutual funds?

Mutual funds are investments where an investor entrusts his/her money with an investment manager (of an asset management company) to manage the money smartly and efficiently. This money management comes at a cost, which is usually charged as a percentage of the investment. The official regulator of mutual funds has laid down rules on how much an asset management company can charge an investor to manage their funds. For an investor this is important because it is a charge (called total expense ratio or TER in short) levied on their investment, and the money they get back from their investment is reduced by this figure. For example, if a fund charges 2% as the TER, and the fund produces a gross profit (return) of 15% in a given year, the investor would get 13% - which is the gross profit minus the TER – in their hands.

So, for an investor, TER is an important number to focus on since it has a direct impact on their returns. However, it is not the only number to look at and investors should evaluate funds based on various parameters such as consistency of performance and risk levels.

What are the changes made by SEBI now to TER?

SEBI has, across the board, lowered the TER that a fund house can charge its investors. The reduction is higher for larger funds and lower for smaller funds — larger and smaller being a measure of how much money a fund manages. The reduction has been anywhere between 0.01% to 0.44%. For very small funds, SEBI has actually increased the allowable expense ratio a little. However, in general, mutual fund investors should see a marginal reduction in the fee they were paying, which would mean they would see an increase in the returns they were getting. Also, SEBI has specified the expense ratio for funds larger than the largest funds today, in anticipation of market growth.

For very small funds, SEBI has actually increased the allowable expense ratio

END