PERFORMANCE OF EQUITY WITH SPECIAL REFERENCE TO RELIANCE INDUSTRIES

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"Financial peace isn't the acquisition of stuff. It's learning to live on less than you make, so you can give money back and have money to invest. You can't win until you do this."

– "Dave Ramsey"

Abstract

The need for money can never be satisfied. Every person aims to earn more & more in a shorter span of time & such income sources attract the public. Investment in equity funds at the right time is such an income source for potential customers, its diverse investment options proves suitable for the general public. Investment in equity is a legal, risky option with greater results. In this paper we will focus on the comparative analysis of performance of large cap funds & small cap funds with special reference to reliance industries & CNX Nifty will aim at finding a pattern of investment, understand the trend of returns & analyze the comparison of Large & Small Cap Funds.

Keywords

Investment, Equity, Large Cap Funds, Small Cap Funds, Risk, Return, Capitalization, Price Stability

Introduction

There are many options for investing money suitable to one's requirement, namely: savings a/c, fixed deposit, debentures, equity etc. each of the options have their own positive & negative aspects, amongst all equity is considered to be the most dynamic option with highest return. In this paper we will focus on the equity as an investment option.

We will first look at its definition, "Money that is invested in a firm by its owner(s) or holder(s) of common stock (ordinary shares) but which is not returned in the normal course of the business. Investors recover it only when they sell their shareholdings to other investors, or when the assets of the firm are liquidated and proceeds distributed among them after satisfying the firm's obligations. Also called equity contribution."

An equity investment generally refers to the buying and holding of shares of stock on a stock market by individuals and firms in anticipation of income from dividends and capital gains, as the value of the stock rises. Typically equity holders receive voting rights, meaning that they can vote on candidates for the board of directors (shown on a diversification of the fund(s) and to obtain the skill of the professional fund managers in charge of the fund(s). An alternative, which is usually employed by large private investors and pension funds, is to hold shares directly; in the institutional environment many clients who own portfolios have what are called segregated funds, as opposed to or in addition to the pooled mutual fund alternatives. In equity stock, there is a common saying that prevails, that to have higher returns, one needs to bear higher risks. In stock market, every investment is measured in terms of two aspects, Risk & Return.

The time of investment & the selection of fund are very crucial, i.e. one should analyze the market & the stock in which money is to be invested beforehand.

There are various options for diverse investment needs, which are:

- Balanced Funds

These are hybrid funds which invest in both equity and debt. The equity and debt portions are diversified (in terms of sectors and companies) to avoid concentration of risk.

- Large-Cap Funds

A diversified portfolio of top 50-100 companies in terms of market capitalization makes them safer for first-time investors. This gives stability as stocks of large companies are usually less volatile than that of mid- and small-cap companies. The upside potential of these funds is lower too.

- Index Funds

The portfolio of these funds replicates an index. These funds hold stocks in the same proportion as their weight in the index.

- Tax-Saving Funds

Also known as equity-linked saving schemes (ELSS), these are the favorites of most retail investors. The reason is that the investment is eligible for tax deduction under Section 80C of the Income Tax Act. These are diversified equity funds with a three-year lock-in and are the first choice of many first-time mutual fund investors.

- Monthly Income Plans (MIPs)

MIPs can be a good option for someone looking to park a part of his/her retirement corpus. MIPs are hybrid schemes with 80-85 per cent funds in debt and 15-20 per cent in equity. Equity helps generate returns higher than what a bank FD gives, but makes the portfolio risky.

These funds offer regular dividends-monthly, quarterly; half-yearly-and hence can be a source of regular income for the retired. Equity is the most fruitful investment option the only thing one needs to get right is the time & selection of investment option.

We will study & compare the returns of Reliance Group & CNX Nifty, & draw conclusions on the type of investment to be adopted according to market conditions.

Literature Review

1) In A White Paper on Private Equity Data and Research; Robert Harris, Tim Jenkinson, Rüdiger Stuck assesses currently available sources of private equity data and research on private equity, focusing on several key questions. A major culprit was the existing lack of comprehensive, high quality data for research and benchmarking in this asset class. Our comparison of results from currently available data sources strengthens that view. If each data provider's sample were a random draw from the underlying universe of net-to-LP returns, we'd expect similar messages to emerge across all data sources.

2) Josh Lerner, Morten Sorensen, Per Stromberg, in their research paper, Private Equity and Long-Run Investment: The Case of Innovation engages in a long-standing controversy that whether LBOs relieve managers from short term pressures from public shareholders, or whether LBO funds themselves are driven by short-term profit motives and sacrifices long-term growth to boost short-term performance. We investigate 495 transactions with a focus on one form of long-term activities, namely investments in innovation as measured by patenting activity.

3) Private Equity Performance: What Do We Know? is the contribution of Robert S. Harris, Tim Jenkinsonand & Steven N. Kaplan, in which, they study the performance of nearly 1400 U.S. buyout and venture capital funds using a new dataset from Burgiss. We find better buyout fund performance than has previously been documented – performance consistently has exceeded that of public markets. Outperformance versus the S&P 500 averages 20% to 27% over a fund's life and more than 3% annually. Venture capital funds outperformed public equities in the 1990s, but underperformed in the 2000s. Our conclusions are robust to various indices and risk controls. Performance in Cambridge Associates and Preqin is qualitatively similar to that in Burgiss, but is lower in Thomson Venture Economics.

4) Independent equity research: How we do it, and why it matters to investors by Aaron M. Cooper, CFA Director of Equity Research suggests that over longer time frames, earnings matter most. Valuation — the relationship between price and earnings or between price and free cash flow, to take two common examples that indicate a stock's relatives "cheapness" — is rarely all that matters. Valuation need to be coupled with improvements in a firm's business prospects — or a catalyst for realizing a higher valuation.

5) Research Paper for National Stock Exchange on Imbalances Created because of Structured Products in Indian Equity markets by GopiKrishna Suvanam & Amit Trivedi studies the effect of hedging of structured products on exchange traded equity products. We look at various aspects of the structured product markets including the motivation to buy, the risks of the products, the hedging behavior and the effect of hedging on exchange traded products. We conclude the hedging would be volatility supportive in a sell off and would be volatility suppressing in significant rally. We also suggest introduction of some new exchange products that would make the hedging process easy and also would help some retail investors express their view in a better fashion without the transaction costs involved in structured products.

6) Independent Equity Research Reports by CRISIL- Sponsored by NSE IPFT NSE in association with CRISIL has initiated Independent Equity Research Report (IER) on certain companies. IER is reckoned among the best practices globally in the equity research space, especially because it adds a valuable dimension to equity research-independence. This initiative is sponsored by NSE IPFT. IER has following benefits for the company.
   - Improved liquidity
   - Easy access to capital
   - Enhanced visibility across investors
   - Supports investor relations
   - Increased transparency

7) Private Equity Investment Trend in India - Pre and Post Global Financial Crisis by Dr. Smita Shukla & Dr. Anjali Gokhru in their research paper, talked about the Global financial crisis & its negative impact on growth rate of developed as well as developing economies like USA, UK, Germany, France, China, India, Brazil, Russia etc. Negative impact of the global financial crisis continues to be felt till date. Recent Dubai financial crisis is a case to point. Recent growth exhibited by some major global economies also indicates that global economic recovery is in process, though it is still in very nascent stages. Global financial crisis has also negatively impacted private equity investments worldwide. This paper attempts to understand the changing trend of private equity investment in India, pre and post global crisis and also delves into the negative impact of global financial crisis on private equity investments in India.

8) Trends in the Indian Private Equity Market, by Frost & Sullivan. This literary work, after introducing its readers to the Indian Equity Market, displays the trends of investment in equity till the period of August 2011 & pin points the sector – wise investment.

9) Financing Constraints and Corporate Investment by Steven Fazzari, R. Glenn Hubbard, Bruce C. Petersen, in their paper, suggests that, some firms do not have sufficient access to external capital markets to enable them to respond to changes in the cost of capital, asset prices, or tax-based investment incentives. To the extent that firms are constrained in their ability to raise funds externally, investment spending may be sensitive to the availability of internal finance. That is, investment may display "excess sensitivity" to movements in cash flow. In this paper, work has been done within the q theory of investment, and examines the importance of a financing hierarchy created by capital-market imperfections.

10) Trends in the Ownership Cost of Equity Mutual Funds By John D. Rea and Brian K. Reid puts a point, that, most discussions of the cost of investing in equity mutual funds focus on one component of cost, the expense ratio, and ignore another significant cost, sales loads. As a result, conclusions about the total cost of mutual fund investing have often been incomplete or misleading. The paper analyzes trends in the cost of investing in equity mutual funds from 1980 to 1997 using a measure called “total shareholder cost.” This measure includes all major costs of investing in a mutual fund and is comparable to the fee and expense information required by the U.S. Securities and Exchange Commission in the mutual fund prospectus. The paper finds that the average cost of investing in equity mutual funds has dropped by more than one-third since 1980. The paper also finds evidence of economies of scale among equity funds.

11) Deciphering the Liquidity and Credit Crunch 2007-08 by Markus K. Brunnermeier, summarizes and explains the main events of the liquidity and credit crunch in 2007-08. Starting with the trends leading up to the crisis, it explains how these events unfolded and how four different amplification mechanisms magnified losses in the mortgage market into large dislocations and turmoil in financial markets.

12) Equity and bond flows to Latin America and Asia: the role of global and country factors by Punam Chuhan, Stijn Claessens, Nlandu Mamingi, This paper investigates the factors motivating the large capital flows to a number of developing countries in recent years. We use monthly US capital flows to nine Latin American and nine Asian countries to analyze the behavior of bond and equity flows. Employing a panel data approach, we find that although global factors—the drop in US interest rates and the slowdown in US industrial production—are important in explaining capital inflows, country-specific developments are at least as important, especially for Asia. We also find that equity flows are more sensitive than bond flows to global factors, but that bond flows are generally more sensitive to a country's credit rating and secondary market debt price.

13) Trend analysis of foreign institutional investors (FIIS) investment in India of monthly flows during January 2006 - October 2011, Mr.Saravanakrishnan V, the objective of FIIs to invest in any country is; return and safety of its funds. Here in this paper researchers have made an attempt to analyze the trend of FIIs investment in India. The information regarding monthly and yearly investment by Foreign Institution Investors (FII's) in India have been collected from the India Infoline Website. The period covered under the study is from January 2006 to October 2011.The findings of the study indicate that in 2009 FIIs have invested Rs. 91,067.60 Crores. While they have withdrawn Rs.60, 905.90 Crore in 2008 this is due to the effect of global meltdown and recession in world economy. During the study we found that Market size, Political scenario, Labour cost and productivity, Liberalized Trade Policy, Infrastructure, Incentives and Operating conditions and Disinvestment policy were the causes of FIIs investment in India.

14) The Disintermediation of Financial Markets: Direct Investment in Private Sector by Lily Fang, Victoria Ivashina, and Josh Lerner highlights one of the important issues in corporate financing to be the role of the financial intermediaries. It was found that the solo investments by institutions outperformed co investments & a wide range of benchmarks for traditional private equity partnership investments.

Objective for the study

- To study the pattern of returns for Large & Small cap funds.

Hypothesis for the study

- Null Hypothesis: There is no significant difference between the returns of Large cap & Small cap funds.
- Alternative Hypothesis: There is a significant difference between the returns of Large cap & Small cap funds.

Comparison between Large Cap & Small Cap Funds

The term 'cap' simply refers to the 'market capitalization' of the stock. Market capitalization, is the value of the stock that you arrive at by multiplying the stock price by the company's outstanding number of equity shares.

Market Capitalization = Current Stock Price x Number of Shares outstanding

Large cap funds/ stocks

A term used by the investment community to refer to companies with a market capitalization value of more than $10 billion. Large cap is an abbreviation of the term "large market capitalization". These are stocks of usually large and well-established companies that have a strong market presence and are generally considered as safe investments. One important fact about large caps is that information regarding these companies is readily available in newspapers and magazines. Most of the large cap companies have good disclosures and therefore there is no dearth of information for an investor looking into them. Market capitalization for stocks in the BSE-100 Index, for instance, ranges from Rs 200 bn to Rs 3,500 bn. large companies such as Infosys, TCS, and Wipro are classified as large cap stocks. These companies have been around in the industry long enough and have firmly established themselves as leading players. Their stocks are publicly traded and have large market capitalizations.

Small cap stocks

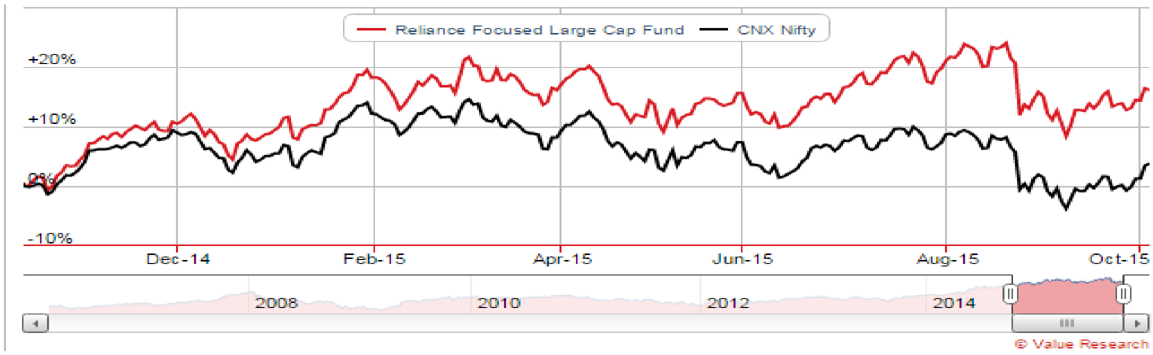
Refers to stocks with a relatively small market capitalization. The definition of small cap can vary among brokerages, but generally it is a company with a market capitalization of between $300 million and $2 billion. One of the biggest advantages of investing in small-cap stocks is the opportunity to beat institutional investors. Because mutual funds have restrictions that limit them from buying large portions of any one issuer's outstanding shares, some mutual funds would not be able to give the small cap a meaningful position in the fund. To overcome these limitations, the fund would usually have to file with the SEC, which means tipping its hand and inflating the previously attractive price.

Large cap vs. Small cap funds

Basis	Large cap funds	Small cap funds
Market capitalization	More than Rs. 200 billion	Less than Rs.50 billion
Price stability	Prices are less volatile	Fluctuation is higher than large & mid cap
Dividend potential	Steady but low returns	Dividend potential is high
Risk	Lower risk	Higher risk
Disclosures & reporting	Very efficient	Poor

Analysis of Reliance Large Cap Funds

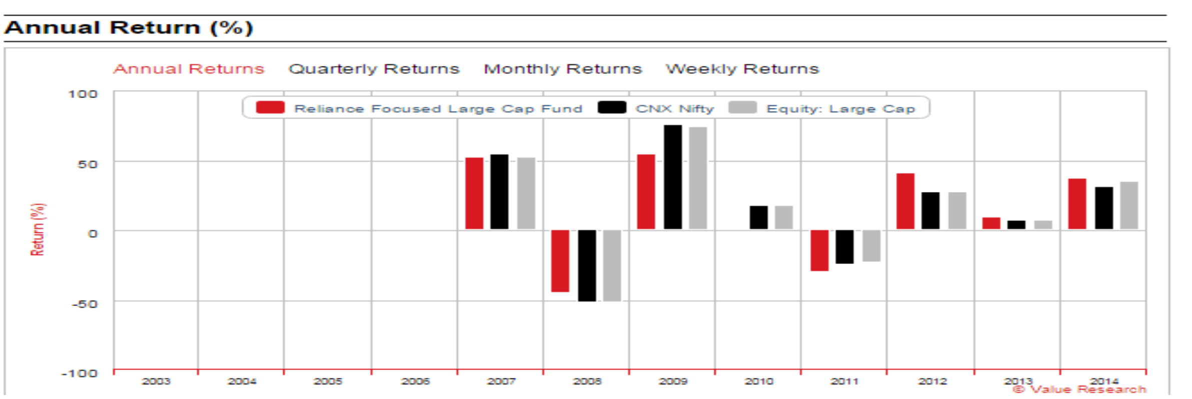
For the purpose of study, the large cap fund chosen from reliance group was Reliance Large cap Focused Group. To analyze the return pattern, the following graph becomes very useful. It compares the returns of reliance large cap fund & CNX Nifty, with the investment span of 1 year.



Line Graph: 1

We can observe the following points through this graph:

a) Since Dec 2014, both Reliance Focused Large Group Fund (RFLCF) & CNX Nifty have showed a rise above 0%. But CNX Nifty have showed a downfall in Oct 2015.
b) There are many upwards & downward movements in the graph, but, RFLCF have never been negative.
c) The best performance of RFLCF is for the period September 2015 i.e., 25%.
d) The best performance of CNX Nifty 15%.
e) RFLCF have always outperformed CNX Nifty.



Bar Graph: 1

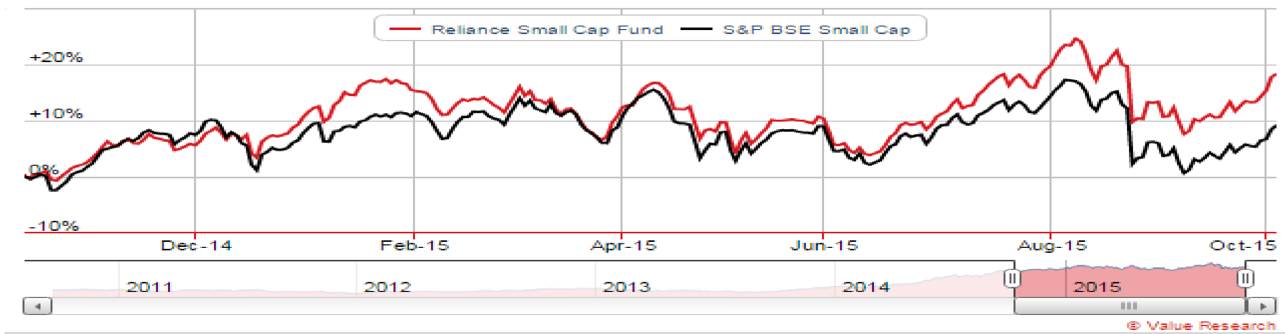
This graph shows the comparison of returns in terms of percentage from the period of 2007 to 2014. Following are the points:

a) The returns of RFLCF & CNX Nifty shows similar trends throughout, i.e. the rise & downfall in the returns for both RFLCF & CNX Nifty, goes hand in hand.
b) In spite of the same trend in rise & downfall, the RFLCF shows a better performance, the exception being in the year 2009, where the returns of RFLCF is somewhere near 55, whereas, the returns of CNX Nifty is between 60 – 70%.

c) In the two years, i.e. 2008 & 2011 RFLCF has shown negative returns, which are also less than CNX Nifty, which means, that in case of bad performance, the returns of RFLCF have not been worse.
d) But it is not the same in the case of 2011, here the performance of reliance group have been worse, as it shows a negative return of 30 – 40%, the lowest for the yr.

Analysis of Reliance Small Cap Funds

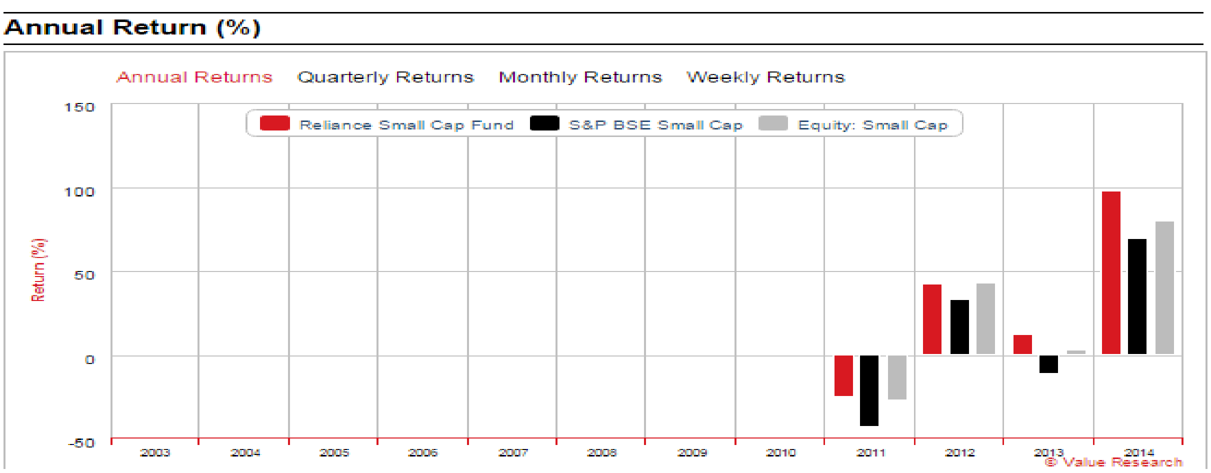
For the purpose of study, the small cap fund from reliance group was chosen. To analyze the return pattern, the following graph becomes very useful. It compares the returns of reliance large cap fund & CNX Nifty, with the investment span of 1 year.



Line Graph: 2

Following conclusions can be drawn from the chart:

a) Since the start, both the Reliance Small Cap Fund (RSCF) & CNX Nifty have shown only positive returns, i.e., above 0%.
b) In spite of many upward & downward movements, RSCF has never been negative.
c) The best performance of RSCF is recorded in Aug 2015 i.e., 25%.
d) CNX Nifty also has the highest returns in the month of Aug 2015, but it is less than that of RSCF, i.e., 15%.
e) RSCF has shown a better performance than CNX Nifty.



Bar Graph: 2

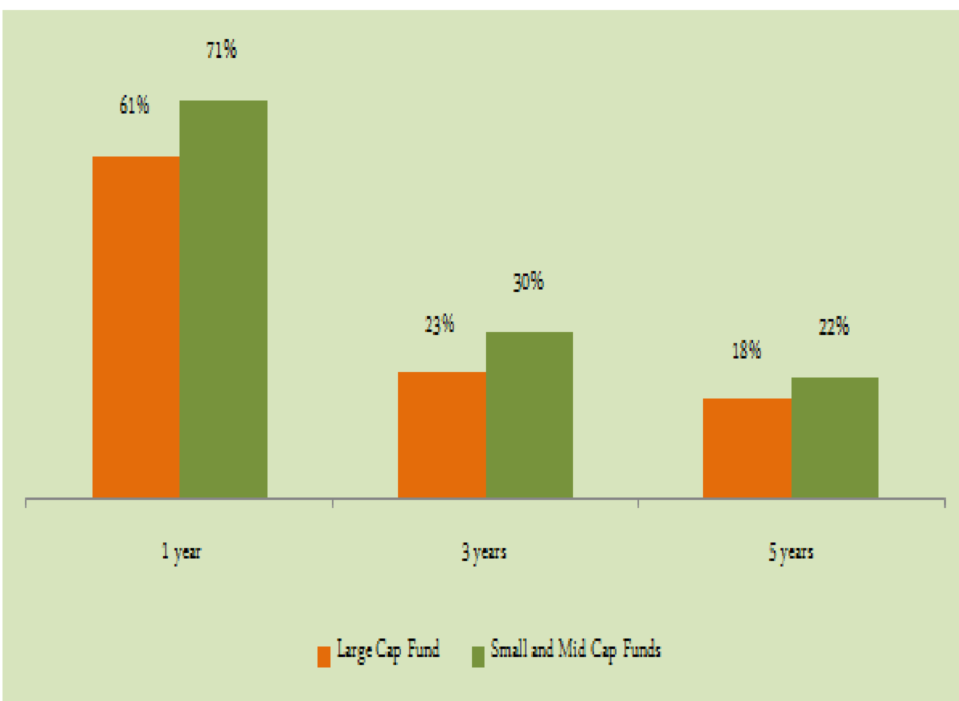
This graph shows the returns in percentage for the period of 4 yrs, i.e., from 2011 to 2014.

a) Reliance started its Small cap funds in Sep 2010.
b) In the starting yr, i.e. 2011, itself, showed negative returns of (-20%), same as CNX Nifty, with (-40%).
c) In the year 2012, RMCF showed an average performance, with the return of 40%.
d) Its performance again decrease in the yr 2013 & it showed a return of 10%.
e) But in the year 2014, it showed a tremendous increase in its returns, with, 99%.

Analysis of Large and Small Cap Funds

In the last one year the Sensex rose by 44% generating fabulous returns for many equity investors. If we look at mutual funds, the returns have exceeded even the Sensex returns. Large cap equity mutual funds gave on average over 61% trailing annualized returns over the last one year period. The returns of small and midcap equity funds have been even higher over the last one year. The chart below shows the comparison of average annualized returns of large cap and midcap fund categories over 1 year, 3 years and 5 years investment horizon.

While small and midcap funds have the potential to give higher returns than large cap funds, the intrinsic risk of small and midcap funds is higher than large cap funds. We can see in the chart above that while the average annualized returns of small and midcap funds category are higher than that of large cap funds category, the difference narrows as the horizon lengthens. Many mutual fund investors prefer large cap funds, because the portfolio mix of such funds limits downside risks in volatile market conditions.



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The same trend has also been followed in the case stocks of Reliance group's Large & Small cap funds. As we can see through the following tables, that there is a significant difference between the returns of Large Cap & small cap funds for the investment span of 1yr, 3yrs & 5 yrs.

- The RFLCF provides with the return of 14.52 for investment span of 1 yr, which is less than the return of RSCF (17.26)
- For the span of 3 yrs also, the return of RSCF, 34.64 is more than the return of RFLCF, which sands to be 18.24.
- In the case of 5 yrs span also, the same thing follows. Here also, the return of RSCF, 20.60 is greater than the return of RFLCF, 8.24.

Peer Comparison

Fund	Launch	1-Year Ret	3-Year Ret	5-Year Ret	Expense Ratio (%)	Assets (Cr)
Reliance Focused Large Cap Fund	Mar-2006	14.52	18.24	8.24	2.40	1,080

Fund	Launch	1-Year Ret	3-Year Ret	5-Year Ret	Expense Ratio (%)	Assets (Cr)
Reliance Small Cap Fund	Sep-2010	17.26	34.64	20.60	2.49	1,695

Conclusion

For the research, the set objective was to study the pattern of returns for Large & Small cap funds. To fulfill the study of this topic, a lot of data was collected in the form of charts, graphs & tables. Based on all the data available, we compared the returns of Large & Small cap funds, & came to know, that there is a high return in Small cap funds. So we reject the null hypothesis, i.e., <u>there is a significant difference between the returns of large & small cap funds.</u>

Suggestions for investment based on the study

- Large cap funds have lesser risk & lesser returns, so one should invest in Small cap funds, as they have higher returns.
- For risk adverse people, investment in large cap funds is advisable, but the investment should only be for one year, as the returns of Large cap funds decrease with the increase in investment period.
- It is always safe, to have a proper mix of large & small cap funds so as to increase returns & balance the risk with Large cap funds.

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