

## BUILD CORE PORTFOLIO AROUND LARGE CAP ETFs WITH AN AIM TO BEAT VOLATILITY

**In the three months ended April 27, 2020, Nifty 50 TRI and Nifty Next 50 TRI fell just 23% and 19%, respectively, compared with 29-37% by mid-caps and small caps.**

The equity markets have taken a severe beating amid the Covid-19 pandemic and concerns about the potential economic damage from the lockdowns. Despite the market volatility, large companies with stable businesses, significant market presence, strong cash flows and steady dividend payouts, among other parameters, continue to fare better. Their stocks have performed better than the broad market and the stocks in the lower market capitalisation.

Read on to find out more about large cap stocks for better investment opportunities during market volatility and downturn and how exchange traded funds (ETFs) in this space may be a suitable ally for investors in such trying times.

### Why large caps?

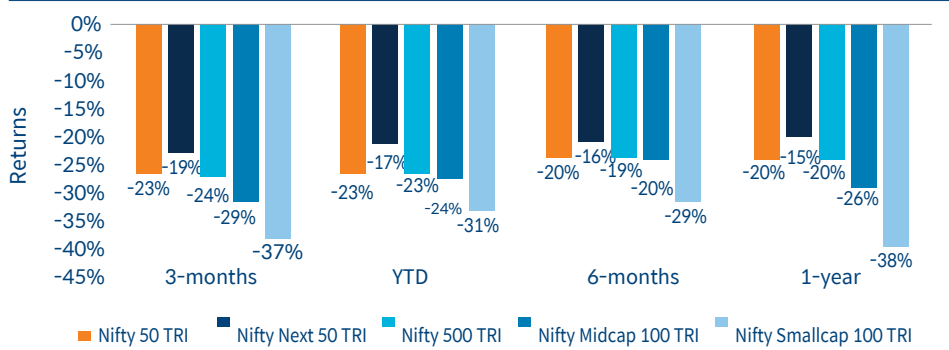
Large caps are companies with stable businesses and given their size and track record, these companies are relatively less volatile during market downturns and are usually good compounders in the long term. Run by experienced management, large caps are at the matured life cycle stage compared with mid- and small-sized companies, which are in the middle or early life cycle stage with a strong growth potential, but more vulnerable to a business or economic downturn.

This was witnessed recently when the Covid-19 pandemic rattled the equity markets. Large caps, represented by Nifty 50 TRI and also Nifty Next 50 TRI (highlighted in black and orange in Chart 1), have fallen less than the small and mid-caps (Nifty Midcap 100 TRI and Nifty Small cap 100 TRI). Thus during times of volatility, large caps has performed better than midcaps and small caps.

In the three months ended April 27, 2020, Nifty 50 TRI and Nifty Next 50 TRI fell just 23% and 19%, respectively, compared with 29-37% by mid-caps and small caps.

Investors can invest in these stocks through a professional fund management route.

**Chart 1 – Large have fared well vis-à-vis small and mid-caps during the recent market carnage**



Notes: Data for the period ended April 27, 2020  
 Source: CRISIL Research  
 Past performance may or may not sustain in future.

### How to invest?

Now that it is clear that large cap stocks are an active opportunity for investors for their core portfolio, we move on to the next question: during times of volatility, should investors start investing in large caps directly? Well that's tricky, considering the amount of money needed to invest directly in each of the 100 large cap stocks (as per Securities and Exchange Board of India definition). Instead, investors can opt for the mutual fund route.

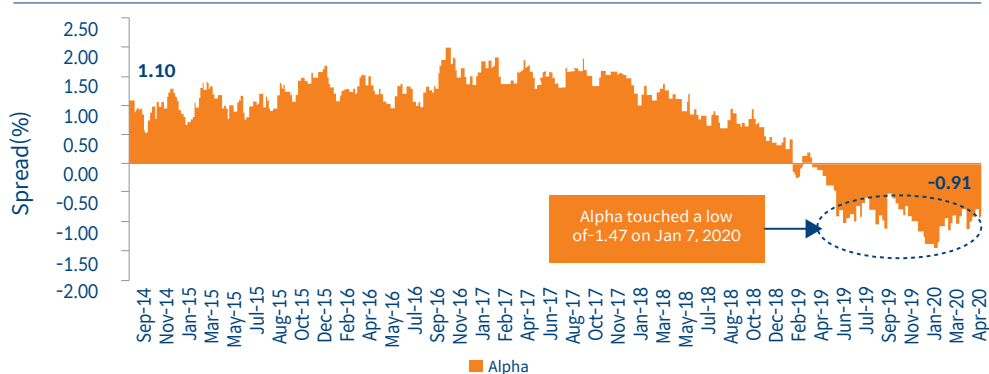
Investors can invest in these stocks through a professional fund management route. They can opt for investing through actively managed mutual funds, or passively managed mutual funds such as ETFs mirroring large cap indices. The latter is relatively cheaper than actively managed funds; for instance, the average expense ratio (costs charged by investment companies to investors for managing their money) is 0.39% in ETFs (Nifty 50 and Nifty Next 50 ETFs) as against 2.23% in actively managed large cap funds. This means a gap of nearly 184 basis points, which can make a huge difference in the long term.

Source: CRISIL Research, dated as on April 27, 2020

Additionally, falling alpha of actively managed funds has reduced the benefit for investors compared with passively managed funds.

CRISIL analysed the alpha spread by taking the five-year daily rolling returns of large cap funds versus Nifty 50. The alpha turned negative in January 2020, touching a low of -1.47 on January 7, 2020.

**Chart 2 - Consider investing in ETFs amid dip in alpha of actively managed funds versus benchmark**



Notes: Alpha is the difference between the daily five-year annualised rolling returns of a weighted large cap fund performance index based on CRISIL- ranked large cap funds, and Nifty 50 TRI as on April 27, 2020  
 Source: CRISIL Research  
 Past performance may or may not sustain in future.

Thus, ETFs either in the conventional broad market index like Nifty 50 or Nifty Next 50, can act as a stable, diversified and low-cost supplement to the existing active investment portfolio.

The performance of the Nifty 50 TRI index has been on par with large cap funds.

Decent performance has also come with low volatility which is one of our primary factor of investing in these volatile times.

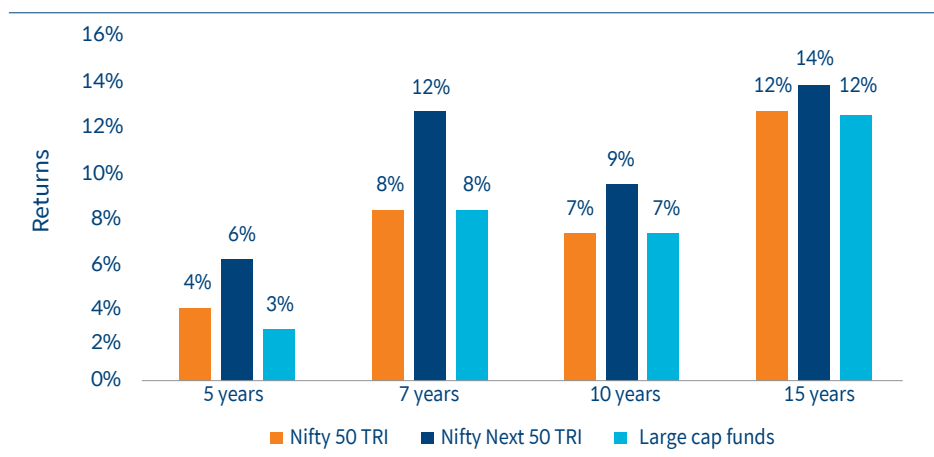
## Why Nifty 50 and Nifty Next 50?

Now that it is clear that large cap stocks are an active opportunity for investors for their core portfolio, we Nifty 50 and Nifty Next 50 encompass the entire large cap universe in the domestic stock market. Nifty 50 is the older and more tracked index between the two and comprises the top 50 large cap stocks in the country, while Nifty Next 50 index represents the next 50 companies in the large cap universe in the market capitalisation order.

## Performance analysis

Historical performance analysis of these indices versus large cap funds shows that Nifty Next 50 TRI index has consistently outperformed large cap funds. The performance of the Nifty 50 TRI index has been on par with large cap funds.

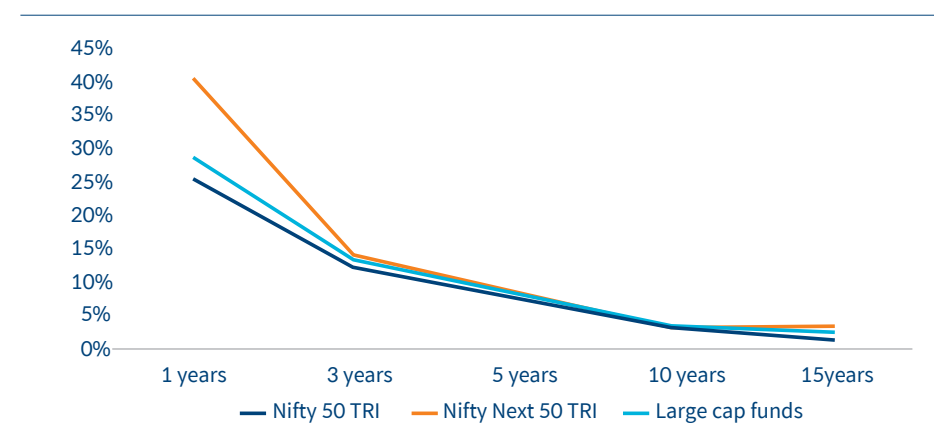
**Chart 3 - Point to point returns of Nifty 50 TRI, Nifty Next 50 TRI vis-à-vis large cap funds**



Notes: Point-to-point returns for period ended April 27, 2020  
 Large cap funds are represented by weighted large cap fund performance index based on CRISIL-ranked large cap funds  
 Source: CRISIL Research  
 Past performance may or may not sustain in future.  
 The data/performance provided above pertains to the category/index and does not in any manner constitute performance of any individual scheme of Mirae Asset Mutual Fund.

Decent performance has also come with low volatility which is one of our primary factor of investing in these volatile times. Volatility, measured by standard deviation, was at 13% and 15%, respectively, compared with 14% for large cap funds during the three-years holding period. (See chart 4) Volatility tends to reduce over the long-term horizon, as evident in the chart.

**Chart 4 - Volatility of Nifty 50 TRI, Nifty Next 50 TRI vis-à-vis large cap funds**



Notes: Volatility is represented by standard deviation  
 Time period of analysis is from January 1, 2001, to April 27, 2020  
 Large cap funds are represented by weighted large cap fund performance index based on CRISIL-ranked large cap funds  
 Source: CRISIL Research  
 Past performance may or may not sustain in future.  
 The data/performance provided above pertains to the category/index and does not in any manner constitute performance of any individual scheme of Mirae Asset Mutual Fund.

The market phase analysis reveals that the performance of Nifty 50 has been in line with or below large cap funds across most bull and bear periods. Further, Nifty Next 50 has fallen less than the large cap funds during the recent Covid-19 crisis and also during the Chinese slowdown in 2016. Nifty Next 50 has rebounded well compared with large cap funds post subprime and euro zone crises.

**Table 1 - Market phase analysis**

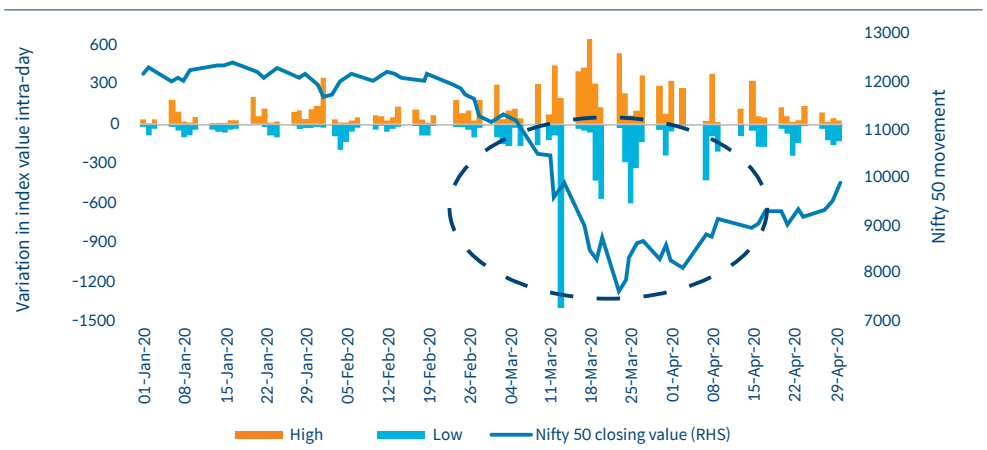
Period	Nifty Next 50 TRI	Nifty 50 TRI	Large cap funds
Subprime crisis (Jan 2008-Mar 2009)	-57.1%	-42.8%	-43.4%
Sharp bounce-back post subprime crisis (April 2009-December 2010)	81.5%	50.4%	52.9%
European crisis (January 2011-June 2013)	-1.2%	-0.7%	-1.1%
Post European crisis (July 2013-February 2015)	37.2%	29.4%	33.1%
Chinese slowdown (March 2015-February 2016)	-12.1%	-20.6%	-18.7%
Global liquidity and domestic reforms (March 2016-December 2017)	38.0%	24.5%	26.7%
Mixed domestic and global scenario (January 2018-December 2019)	-3.1%	9.5%	4.0%
Covid-19 pandemic (January 2020-April 2020)	-16.9%	-23.6%	-22.4%

Notes: Large cap funds are represented by weighted large cap fund performance index based on CRISIL-ranked large cap funds  
Returns above one year are annualised, otherwise absolute  
blue highlight signifies best performers across each phase  
Source: CRISIL Research  
Past performance may or may not sustain in future.  
The data/performance provided above pertains to the category/index and does not in any manner constitute performance of any individual scheme of Mirae Asset Mutual Fund.

ETFs thus provide a tactical opportunity to invest based on market volatility.

**Side note: An intraday tactical opportunity**

Investors can buy and sell ETFs intraday or any time during the market hours, unlike traditional equity mutual funds, where they get the closing net asset value (NAV) for investment. ETFs thus provide a tactical opportunity to invest based on market volatility. For instance, as seen from the chart below, investment in ETFs during high volatility periods, which correlate to market lows, allows investors to buy more units, thus getting a better purchase for their investment over the long term.





## Nifty closing versus its intraday high and low closing value

Notes: Data from January 1 to April 30, 2020



High represents the variation in absolute value of the high point of the index intraday versus that day's closing value



Low represents the variation in absolute value of the low point of the index intraday versus that day's closing value

Source: National Stock Exchange of India

### Summing up

Inclusion of both Nifty 50 and Nifty Next 50 ETFs can be good value additions to the active investment portfolios both in terms of core strategic portfolio and tactical investments in the current volatile market scenario.

However, due diligence of schemes in terms of expense ratio, tracking error (a measure of how closely the index fund's returns match its benchmark returns), and track record of the fund house, is a must. Investors should not panic when unprecedented events like the Covid-19 pandemic batter the stock market; instead, they should hold on to the investments for the long term.




An investor education initiative by Mirae Asset Mutual Fund.

All Mutual Fund investors have to go through a one-time KYC (Know Your Customer) process. Investors should deal only with Registered Mutual Funds (RMF). For further information on KYC, RMFs and procedure to lodge a complaint in case of any grievance, you may refer the Knowledge Center section available on the website of Mirae Asset Mutual Fund.

**Mutual Fund investments are subject to market risks, read all scheme related documents carefully.**


 **Email Us**  
customercare@miraeasset.com

 **Call Us**  
1800-2090-777 (Toll Free)  
Mon-Sat: 9 a.m. to 6 p.m.

 **Internet**  
www.miraeassetmf.co.in

 **Twitter**  
@MiraeAsset\_IN

 **Facebook**  
MiraeAssetIN

 **Contact your financial advisor for details**