ET IN THE CLASSROOM

# Portfolio Overlap in MF Schemes

**Very often investors find that even though they have invested in two different equity mutual fund schemes, their net asset values (NAVs) move up or down almost in the same proportion. This happens because the underlying portfolios of these two schemes have a high overlap. Financial planners believe such overlap reduces diversification, which is why investors should try and avoid such overlaps.**

## WHAT IS OVERLAP IN AN EQUITY MUTUAL FUND?

An equity mutual fund scheme's portfolio is built by investing in a mix of stocks depending on its objective. An investor who puts his money in different equity mutual fund schemes across a mix of fund houses, often believes his portfolio is diversified. In reality, the money might be invested in the same set of underlying stocks, which may be common to the schemes that are purchased by the investor. This is called overlap in a mutual fund.

## HOW CAN AN INVESTOR FIND OUT COMMON STOCKS IN MF SCHEMES?

Many websites help an investor know the extent of overlap between two schemes. The investor needs to provide the scheme name and feed it into the website to find overlapping funds on such websites. A person can find common and uncommon stocks in a portfolio and the percentage and quality of overlapping funds.

## WHY DO OVERLAPS HAPPEN IN YOUR FUND PORTFOLIO?

According to financial planners, portfolio overlap could happen due to the regulator's categorisation mandate or on account of a specific style adopted by an AMC. For example, as per the regulatory mandate, a large-cap scheme should have 80% of its portfolio in the top 100 stocks by market capitalisation. So even if an investor puts money in two different large-cap schemes, there is bound to be a high overlap in the portfolio. Portfolios could also have a high overlap if an investor puts money in two schemes of the same fund house. For example, if an investor puts money in a large-cap fund and a large-and-midcap fund or a focused fund of the same fund house, chances are that the large-cap portion will overlap, as many fund houses have a similar style of investing across schemes.



## HOW CAN INVESTORS REDUCE IT?

Financial planners point out that it is impossible to eliminate portfolio overlap as there will always be stocks common across schemes. However the lower the overlap the better it is and typically it should be 30-40% and not more. Some stocks which are expected to do well and are large-cap-oriented are bound to figure in most portfolios. A turnaround story or a value stock is likely to find a place in many portfolios. If a theme or a sector's outlook is good, the top stocks in that space would go into several portfolios.

Whenever a new fund is added to the portfolio, check the overlap with existing schemes. Invest in funds across categories and in schemes across AMCs to reduce overlap.

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