

Evolving Distribution Strategies

Reaching out to Retail Investors

Success in the Indian Mutual Fund Industry, in the midst of all the growth that is evident, will depend upon strong distribution network and transparent approach towards trust building and client servicing at retail level will soon assume greater importance.



The Indian mutual fund industry has been growing at a rapid pace. Particularly over the last 4 four years the growth has been phenomenal, thanks to a booming capital market and favorable tax regime. This era of exponential growth has seen changes, refinements, innovations etc in products, practices and channel development of the AMC's. The ultimate beneficiary has been the growing and prospering investors.

The distribution channels that have evolved in India are: Independent Financial Advisors (IFA), the big distribution

firms, banks and direct selling, including online selling of mutual funds. The various factors which influence the success of distribution channel are trust, customer servicing, including multiple and accessible service points, good infrastructure, including IT support, the comfort factor & exclusivity.

An efficient and effective distribution network is as important as any other consumer industry. The customer base is huge here too. The industry since its inception has been trying hard to attract retail investors by taking well-



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calibrated steps. It has entered into previously untapped markets. There is more stress on product innovation. Three years ago, there were very few options before the high net worth individual (HNI), leave alone normal investors. Now, all investors can invest in real estate, private equity and even stocks and mutual funds abroad. The minimum investment amounts can be really small.

MF Industry - Distribution Abroad

There have been dramatic changes in the manner in which mutual funds are sold abroad. Before 1980, most funds were vended through a broker, who provided advice, assistance and ongoing service to the buyer. The unit holder paid for these distribution services through a front-end sales charge when he bought the fund. Funds sold through finance professionals such as brokers have since adopted alternatives to the front-end sales charge.

The alternative payment methods typically include a fee based on assets that may also be in combination with a front-end or back-end sales charge. In many cases, funds offer several different share classes, all of which invest in the same underlying portfolio of assets, but each share class may offer shareholders different methods of paying for broker services.

With the expansion in distribution channels, many fund sponsors have moved from single-channel distribution strategies in favor of multi-channel distribution. The changes in fund distribution have been accompanied by a significant decrease in the average cost of distribution services incurred by mutual fund buyers. The decline in distribution costs reflects a variety of developments, including competition between funds, expansion of the 401(k) plan market and other markets with low distribution costs, and increased availability of lower-cost advice to investors. Presently funds are sold abroad through five principal distribution channels: 1. Direct channel, 2. Advice channel, 3. Retirement plan channel, 4. Supermarket channel, 5. Institutional channel.

The first four channels primarily serve individual investors. In the direct channel, investors carry out transactions directly with mutual funds. In the advice, retirement plan and supermarket channels, individual investors use third parties or intermediaries that conduct transactions with mutual funds on their behalf. The most important feature of

the advice channel is the provision of investment advice and ongoing assistance to fund investors by financial advisers at full-service securities firms, banks, insurance agencies, and Financial Planning outfits.

The retirement plan channel primarily consists of employer-sponsored defined contribution plans in which employers provide mutual funds and other investments for purchase by plan participants through payroll deductions. The supermarket channel is made up of discount brokers that offer mutual funds from a large number of fund sponsors. Many of the fund offerings are subject to no transaction charges or sales loads. Businesses, financial institutions, endowments, foundations and other institutional investors use the institutional channel to conduct transactions either directly with mutual funds or through third parties.

The Indian mutual fund industry will also evolve on the above lines over a period of time. SEBI's latest move – no-load for direct investments - is the first step towards it.

Retailisation of the Indian MF Industry

As already stated in brief, the retail push to MFs in India has been spearheaded by the big distribution houses, IFAs and banks, including PSBs. MFs are now expanding their own networks to this end. Online distribution, while catching up among the computer-savvy segment of the public, will not be a very significant contributor, at least in the near future.

Essentials of a Good Distribution System

Distribution success for mutual funds or any financial product is dependent on certain key elements. These are:

- Careful product selection
- A careful selection of internal sales staff (who will sell)
- Right targeting of customers - a properly graded geographical strategy based on a demographic study will propel a smooth, seamless customer penetration and sales volumes
- Proper training - Training is the axle on which the entire distribution revolves. Continuous training of the sales force is essential in this dynamic environment
- Educating / counseling the customer about products, keeping in mind rising customer expectations and increasing buyer expertise
- After sales servicing

Role of Various Channels

Direct Selling: Direct selling is the least significant element today. Normally, only very big ticket items are done through this. Alternatively, it derives its inflows mainly from online sales. However, recent changes in regulation are all set to give this channel a fillip. MFs are gearing up by opening their own offices in more places. Also R&T Agents are expanding their infrastructure to facilitate this.

Organised distributors: Organised distributors are the backbone of MF distribution. They have infrastructure and flexibility to adapt to the need of the hour. They too have realized the importance of going to smaller centres and are establishing offices in urban and semi-urban locations. This is the sector which needs to be nurtured to expand.

Banks as distributors: Mutual fund distribution by banks

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is emerging a key element. Banks have huge potential to build and improve the retail segment, which needs to become as strong as its institutional counterpart.

Even among banks there are two major types of distributors. There are those that handle wealth management of their clients and, on their behalf, manage portfolios wherein investment in mutual funds is one asset class. Such banks have sophisticated wealth management practices with qualified staff and well-heeled clients. MNC banks, private banks and a few niche players (like HSBC, Citi, ICICI, HDFC, Kotak etc) are examples.

Then there are banks that use their networks to sell MFs as just another financial service. Most of the PSBs and other commercial banks including large cooperative banks fall under this category. For the banks the existing customer base serves as a captive prospective investor base for marketing mutual funds. They have the advantage of having already won the trust of the customer. There is no other distribution channel that can have a more effective retail penetration across Tier-II and Tier-III cities as well as across rural India. This channel has slowly realized its own potential and is now emerging as a big player.

Abroad banks are among the leading fund supermarkets. The Post Office too has been emerging as an effective channel. For all practical purposes, it can be clubbed with PSBs. Banks with post offices are likely to emerge as a very crucial channel for “financial inclusion” in the MF arena. This combination along with the online variants in the near future will dominate the distribution of mutual funds.

Independent Financial Advisors: Presently the IFA is

the friendly neighborhood guy – one who is very effective in selling the product. However, he has to manage his costs from the commission he gets. Advisory services are today given gratis. The scenario is changing and the space in advisory services will undergo a rapid change in the next few years. Financial Planning services will be much sought after and Certified Financial Planners will be in demand for their specialized services.

The Future

The potential for MF industry to grow is huge. Currently 77% of the investments in mutual fund come from super metros and Tier I towns. The scenario is most likely to change with everyone expanding. SBI MF alone has more than 100 points of acceptance across India, 28 investor service centers, 45 investor’s service desk and 52 district organizers, a base of over 20,000 agents currently. SBI’s branch network, which is one of the widest networks in the country, as well as India Post and offices of CAMS, is a part of this distribution network. Reliance and HDFC are believed to have plans to

have their presence in 400 places. UTI already has probably the largest network. The strategy, firstly, is to increase the penetration to cover Tier II-Tier III cities and rural areas.

Secondly, complementary to the first idea, enhancing investor education and awareness initiatives by the industry is getting high priority. Savvy fund houses are increasing appropriate technological infrastructure in rural areas and strengthening alternative distribution networks.

Recent regulatory changes may have temporarily brought despondency to the distribution channels but in time suitable strategies (including fee for advisory) will restore balance. Investment is an area where consultation is very important; the direct route will be used by very few investors.

What is needed is standardization of operational areas and services like inner fund house swaps, common portals providing single view of investments with the entire industry, uniform and pooled customer education including investor communication.

The country is enjoying robust economic health. This is due to the efforts of all citizens including the farmers and small workers in the most rural of rural India. The capital market owes its rise to these humble workers as much as to any one else. Therefore, the India story cannot be called a success unless these people too can partake in the capital market boom. The only way to do this is through mutual funds and it is the distribution which has to deliver. This can happen only with the support of the regulator and the industry.

