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ELSS Mutual Fund: A Comprehensive Study of Tax Saving Funds

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ABSTRACT

Mutual funds are a good investment option for small investors who want easy access, liquidity, straightforward exits, and remove investment management risk. Professional fund managers manage funds for the individual investor. Mutual funds' performance is usually tracked as the change in the total market cap of the fund—derived by the aggregating performance of the underlying investments. The holding of mutual fund 'units', represents the share of holdings in a particular scheme. These units can be purchased or redeemed at fund's current net asset value (NAV). ELSS (Equity-linked Savings Scheme) Mutual Funds are a popular investment option in India that offers dual benefits of tax-saving and potential wealth creation. In this study we will explore the aspects of ELSS Mutual Funds, their tax benefits, and factors to be consider before investing. Equity Linked Savings Scheme or ELSS mutual funds are one of the best investment options for those who are looking for wealth generation, regular returns and saving taxes at the same time. These are excellent tax-saving investment options that an investor can opt for generating profits in the long run.

KEYWORDS: Mutual Fund, NAV (Net asset value), ELSS (Equity-linked Savings Scheme), Tax Saving Funds.

INTRODUCTION

A mutual fund is an investment option that collects money from several investors and invests these funds in various financial instruments like bonds, stocks, shares, money market instruments, gold, etc. The holding of mutual fund 'units', represents the share of holdings in a particular scheme. These units can be purchased or redeemed at fund's current net asset value (NAV). These NAVs keep fluctuating, according to the performance of the unit's holdings. All the mutual funds are registered with SEBI. Mutual funds are run by investment professionals companies who allocate funds to generate revenue or capital gains for the investors. They function within the provisions of SEBI to protect the interests of the investor.

LITERATURE REVIEWS

Nittan, A., & Sonia, C. (2019),the findings of their research, the factors of education, income, and occupation are significantly associated with the risk perception of investors in mutual funds for the purpose of making investment decisions, whereas neither gender nor age are associated.

Vibhav Pratap, Dr. Vibha Singh, Ashish Kr. Gautam (2020) examined five best performing mutual fund companies operating in India. To ascertain the top scheme from these companies, they had applied various statistical tools, like standard deviation, beta, Sharpe ratio, Treynor ratio, Jensen alpha. These statistical parameters help authors evaluate the risks and returns provided by these schemes. Using this parameter, it can be concluded that Birla Sunlife tax relief fund 96 performed best in the selected mutual fund ELSS.

Mittal and Agarwal (2015) evaluate the growth rate in the ELSS (tax saving mutual funds) of public and private sectors and Indian Mutual Fund Industry. The growth rate in the ELSS was more in starting years but with depression of 2008 the growth rate becomes negative for some years and then there is no consistency in growth rate

II.OBJECTIVES

The objectives of the study are as follows:
1. To understand the concept of ELSS in tax saving.
2. To compare the ELSS schemes with other traditional tax-saving instruments on the basis of their return.
3. To evaluate the benefits of the ELSS schemes.

RESEARCH METHODOLOGY

This research study is completely based on the secondary data. The required data has been collected from secondary sources. The secondary sources include the official websites of Securities Exchange Board of India (SEBI), Association of Mutual Funds in India (AMFI), journals and published research papers of various authors and the websites of the different Asset Management Company

WHAT IS MUTUAL FUND?

A mutual fund is an investment option for investors vehicle that work by pooling money together from many investors. These funds managed by a professional Fund Manager. The fund manager invests these funds in various financial instruments like bonds, stocks, shares, money market instruments, gold, etc. because of multiple benefits Mutual fund investments are becoming very popular in recent year. These funds are managed by specialists that will help in investing money, and earn attractive returns on investment.

TYPES OF MUTUAL FUNDS

The Securities and Exchange Board of India (SEBI) has classified mutual funds on the following basis:

TYPES OF FUNDS BASED ON ASSET CLASS

Debt funds- One of the best fixed income investment funds is a debt fund. Debt funds are mutual funds that invest in corporate bonds, government bonds, corporate debt, money market instruments, etc. They are suitable for people who want a stable income and are risk averse.

Equity funds- They are a good choice if you want to invest for long term goals such as retirement planning or buying a house as the level of risk comes down over time. Equity funds are also called stock funds.

Hybrid funds- hybrid funds are a combination of equity and debt investments which are designed to meet the investment objective of the scheme. Every hybrid fund has a various combination of equity and debt for different types of investors.

Types of Funds Based On Investment Objective:

Growth funds: The primary goal of growth funds is to increase capital appreciation. Most of the money is invested in stocks, which can be more risky because of the high exposure to equity. It is best to invest in these funds for the long term, but if you are close to your goal, you might want to avoid them.

Income funds- Income funds are designed to provide a steady income for investors. They invest mostly in debt instruments, such as bonds, government securities, and certificates of deposit, etc. These funds are suitable for different-term goals and for those with a lower risk appetite.

Liquid funds- Liquid funds invest money in short term money market instruments, such as treasury bills, certificates of deposit, term deposits, and commercial papers. This type of fund helps to store surplus money for a period of time, such as a few days or a few months, or to set up an emergency fund.

Tax saving funds- Tax saving funds offer tax benefits under Section 80C of the Income Tax Act. When investors invest in these funds, than they acn claim deductions up to Rs 1.5 lakh each year. Equity Linked Saving Scheme (ELSS) is an example of tax saving funds.

Types Funds Based On Structure:

Open-ended mutual funds- Open-ended mutual funds are highly liquid as investors can redeem their units from the fund at any time of the day.

Close-ended mutual funds- Investors have a pre-determined maturity period and can only withdraw money from the fund when the fund matures. Equity Linked Saving Scheme: These funds are listed on the stock market and can be bought and sold at the same price as shares. However, these funds are not very liquid as trading volumes are very low.

BENEFITS IN INVESTING MUTUAL FUNDS

Diversification: The adage "don't put all your eggs in one basket" may be familiar to you
This is a well-known maxim to keep in mind when making financial investments. Investing solely in one asset exposes us to potential loss in the event of a market collapse. Therefore, by diversifying our portfolio and investing in a variety of asset classes, we can avoid this issue.

Tax benefits:
By making investments in equity linked savings schemes (ELSS), mutual fund investors are eligible to receive a tax deduction of up to Rs. 1.5 lakh. The Income Tax Act's section 80C qualifies for this tax benefit.

Returns: One of the main advantages of mutual funds is their potential for higher returns than those of traditional investment options, which are guaranteed. This is so because the performance of the market is connected to the return on mutual funds.

Professional expertise: A professional actively manages mutual funds, keeping a close eye on the fund's portfolio. Furthermore, compared to a retail investor, the manager has more time to dedicate to choosing investments

HOW TO INVEST IN MUTUAL FUNDS

1. Investors purchase mutual fund stocks from the fund itself or via a dealer for the fund, in place of from different buyers. The fee that buyers pay for the mutual fund is the price range according to percentage internet asset value (NAV) plus any prices charged on the time of purchase, together with income loads
.
2. Investment Amount: Investor can determine their invested quantity in mutual price range as according to their want and requirements.

3. Mutual fund stocks are "redeemable," which means buyers can promote the stocks lower back to the fund at any time. The fund typically have to ship you the price inside seven days.

4. Before shopping for stocks in a mutual fund, study the prospectus carefully. The prospectus includes records approximately the mutual fund's funding objectives, risks, performance, and expenses.

WHAT IS ELSS FUND?

Investors look for investment opportunities that can help them generate wealth, get regular returns, and save taxes. ELSS fund is an equity scheme with a mandatory lock-in period of three years. While there are various funding schemes to be had with inside the market, maximum of them provide returns which might be taxed in keeping with the Income Tax regulations. ELSS is the most popular tax-saving mutual fund. It is a mutual fund scheme that invests largely in equities and equity-associated securities of companies with high development prospects.

An investor can avail tax benefits of up to Rs. 150,000 from his annual taxable income under Section 80C of the Income Tax Act because of this tax benefit many tax taxpayers have turned to ELSS schemes in recent past years. There are no provisions for premature exit. These schemes invest in stocks; and stocks offer higher returns over a long period of time. For example, the ELSS category offered an average return of around 15% over 10 years. Equity Linked Savings Schemes (ELSS) refers to the schemes that invest at least 80 percent of their assets in accordance with Equity Linked Savings Scheme, 2005, notified by the Ministry of Finance. At present 42 schemes under the category of ELSS with net assets under management (AUMs) of ₹1,79,802 crore. They have the highest number of folios among all equity-oriented schemes i.e., 1.54 crore.

WHY INVEST IN ELSS TAX SAVING MUTUAL FUNDS?

Following are the reason to Invest in ELSS Tax Saving Mutual Funds

Funds Lock-in period: It comes with minimum lock-in duration of 3 years.

Equity exposure: It invests at least 80% of the investment in different types of equities.

Tax saving: Investments in ELSS are eligible for tax deduction benefits under section 80C, of income tax act, up to Rs 1.5 lakh.

Market-linked returns: It gives market-linked returns, and the returns depends on the performance of the underlying equities in the portfolio.

Diversified Portfolio: ELSS funds typically invest in different types of equities from various sectors, so that risk can be minimize.

Long Term Capital Gain (LTCG): the income earn under ELSS scheme at the end of the three-year tenure will be considered as Long Term Capital Gain (LTCG) and will be taxed according to rules and regulation of Income tax act.

HOW DO ELSS MUTUAL FUNDS WORK?

ELSS funds are diversified equity funds. These funds initially invest in stocks of listed companies. The stocks are chosen from across market capitalization (large, mid, and small caps) and sectors. The objective of these funds is to maximize capital growth over the long term. The fund manager selects stocks after conducting in-depth market research to deliver optimal risk-adjusted portfolio returns to the investors. Fund managers select stocks after conducting thorough market research to achieve optimal risk-adjusted portfolio returns. Investments in ELSS Funds are eligible for tax benefits under Section 80C of the Income Tax Act, 1961. There is no upper limit on the investment amount, but up to Rs 1.5 lakh is eligible for tax deduction under income tax act.

THINGS TO CONSIDER BEFORE INVESTING IN ELSS FUNDS

- **Fund returns:** Before you go select any fund, compare its performance with its competitors and the benchmark to know if it has beaten them consistently in the past. As we know that, no fund can be at the top level at every time, but good funds tend to appear in the top quartiles for extended periods.

- **History of the fund house:** It is recommended to choose fund houses that have performed well consistently over a long period, say five to 10 years.

- **Expense ratio:** The expense ratio shows how much of your investment goes towards managing the fund. If a fund has a low expense ratio, it means you can have higher take-home returns, so it’s always better to go for such funds.

- **Financial parameters:** To know the financial parameters we can use standard deviation, Sharpe ratio, alpha and beta to analyze the performance of a fund. A fund with a higher standard deviation and beta are more riskier than one with a lower deviation and beta.

- **Fund manager:** The fund manager plays a key role in managing the investor’s funds. The Fund manager should be competent and experienced in picking the right stocks and creating a strong portfolio.

- **SIP or Lumpsum:** Before making the investment in ELSS, you should also consider which mode you want to invest in, either SIP or lumpsum. Under the SIP method, an investor can invest a regular amount periodically generally investors prefer monthly SIP. However, under lump sum method, investor invests a huge sum of money in particular funds.

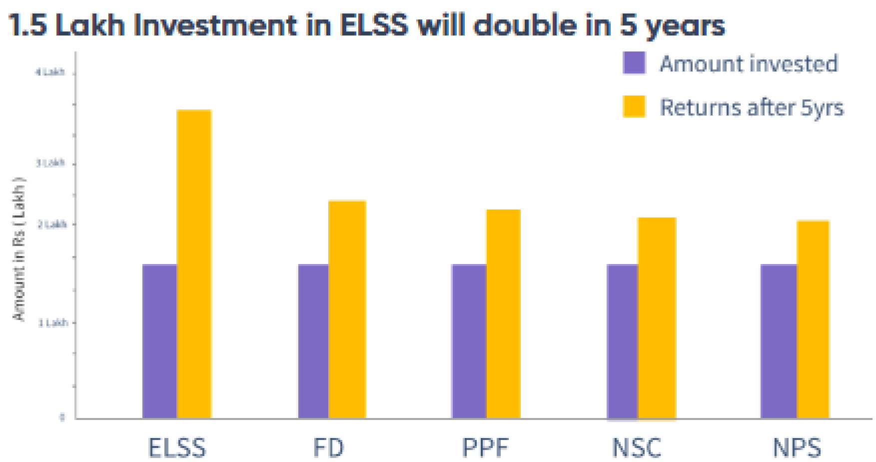
- **Investment Horizon:** The period over which investors stay invested in an investment option is referred to as the investment horizon. This investment horizon decides to risk and income needs, all of which contribute towards the selection of securities. The investment horizon can be classified as short-term, long-term, and medium-term funds.

COMPARISON OF ELSS WITH OTHER TAX-SAVING INSTRUMENTS

There are many tax-saving options available in the market that can improve your return on investment with tax saving. These funds have fixed returns, which might not be able to outpace the impact of inflation. Every tax-saving alternative has a lock-in term of its own. One example of a lock-in term is five years for tax-saving FDs, fifteen years for PPF, and five years for NSC. The ELSS funds have the shortest lock-in period of three years when compared to these.

We can easily compare from the following table

Investments	**ELSS**	**Public Provident Fund (PPF)**	**National Savings Certificate (NSC)**	**5 Year Tax-Saving Fixed Deposits**	**National Pension System (NPS)**
Type of Investment	Mutual Fund (Equity)	Government Scheme	Government Scheme	Bank Fixed Deposit	Pension Scheme
Lock-in Period	3 years	15 years	5 years	5 years	60 years age
Risk Level	High	Low	Low	Low	Moderate to High
Expected Returns	Market-linked	7.1% (Keeps changing)	7.7% (Keeps changing)	Around 6% to 7%	Market-linked
Tax Deduction Limit (Section 80C)	Up to ₹1.5 lakh	Up to ₹1.5 lakh	Up to ₹1.5 lakh	Up to ₹1.5 lakh	Up to ₹1.5 lakh



INVESTORS IN TAX-SAVING MUTUAL FUNDS (ELSS)

ELSS funds are the best option for anyone who wants to avail benefit from tax savings and take part in the possible growth of the equity market. But because these funds are tied to the market, investors need to have a lengthy investment horizon and a moderate-to-very-high risk tolerance.

For those who are looking to build long-term wealth, ELSS Mutual Funds offer a tax-efficient and growth-oriented investing choice. Investors can take advantage of both tax savings and the growth potential of the equity market by making an investment in ELSS funds. Nonetheless, it's critical to match investment objectives with risk tolerance and financial objectives. Mutual fund is the best option for the small income group investors.

FINDINGS AND CONCLUSIONS

An Important part of financial planning goes into tax management to save taxes. However, an intelligent investor will not only save taxes but will also maximize returns from investments. Equity Linked Savings Scheme (ELSS) is one of the option that gives triple benefits to its investors; tax saving, good returns and liquidity. ELSS is a type of mutual fund that invests in equity and equity-related instruments to generate high returns.

This study provides basic awareness about Equity Linked Savings Scheme of mutual funds' performance to help the common investors in taking the rational investment decisions for allocating their resources in the correct mutual fund schemes. The major parameters namely, Liquidity, Rate of Return, tax benefits, high return, price, capital appreciation and Market share plays a vital role in investors buying decision.

Throughout its more than 20 years of operation, ordinary investors have not been particularly fond of ELSS funds as a tax-saving investing alternative because of lack of awareness and proper information. Its poor investment performance can be one of the causes of its lack of appeal. Lack of awareness and lack of trust on mutual fund companies as well as policy maker is the main reason for poor growth of mutual fund industry in India. The fluctuations in the economy and uncertainty in the financial market worldwide has intensified the competition and created a lot of pressure on the mutual fund industry to perform.

The analysis of the data reveals that the ELSS schemes have offered attractive returns over the period of study making them an attractive investment option for investors. ELSS Funds give you triple benefits of; tax saving, wealth creation and liquidity. Before buying any mutual fund scheme, it is very important for investors to consider all the necessary factors which are related to mutual funds risk as well as performance of the fund scheme. An investor must be aware about the past performance of a fund manager, reputation of fund house, category of scheme, macro-economic factors and importantly – the past performance of the scheme.

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