

# Fund Management Capability: Rating Methodology

## Executive Summary

CRISIL Fund Management Capability Rating is a scheme level rating to assess a fund’s management capability and quality of investment processes. The emphasis is on the quality of the investment management team, investment strategies, and processes to determine the scheme’s ability to fulfil investment objectives consistently. A high score on these parameters will have a strong linkage with healthy long-term performance of the scheme.

## Scope

This article provides an overview of the criteria and processes used to assign CRISIL Fund Management Capability ratings. The criteria document articulates CRISIL’s rating scale and methodology — qualitative and quantitative factors used for such analysis. It also explains the validity and surveillance process for the assigned ratings.

## Rating Scale

The rating is assigned on a five-point rating scale ranging from CRISIL Fund Management Capability Level-1 to CRISIL Fund Management Capability Level-5.

CRISIL Fund Management Capability Level-1	Schemes rated CRISIL Fund Management Capability Level – 1 are judged to possess <b>Highest</b> standards in fund management capability and investment processes
CRISIL Fund Management Capability Level-2	Schemes rated CRISIL Fund Management Capability Level – 2 are judged to possess <b>High</b> standards in fund management capability and investment processes
CRISIL Fund Management Capability Level-3	Schemes rated CRISIL Fund Management Capability Level – 3 are judged to possess <b>Above-average</b> standards in fund management capability and investment processes
CRISIL Fund Management Capability Level-4	Schemes rated CRISIL Fund Management Capability Level – 4 are judged to possess <b>Average</b> standards in fund management capability and investment processes
CRISIL Fund Management Capability Level-5	Schemes rated CRISIL Fund Management Capability Level – 5 are judged to possess <b>Poor</b> standards in fund management capability and investment processes



## Rating Methodology

CRISIL's assessment of the scheme being rated covers two broad parameters:

1. Fund Management Assessment
2. Performance Assessment

A detailed evaluation of each of these parameters is delineated below:

### 1. Fund Management Assessment

The ability of schemes to meet their investment objective consistently over a long period is critically dependent on the quality of the management, strategies and the investment processes being followed. CRISIL's Fund Management Capability Rating looks at the following qualitative parameters which determine whether the fund's returns are likely to be consistent with its investment objective and compare well with its peers set over a longer period of time:

- **Organisation structure**

CRISIL examines the ownership pattern and structure of the investment vehicle under which the scheme has been housed. CRISIL assesses the profile of the sponsors and other joint venture partners/ shareholders and the fit with their long-term business plans. CRISIL will also examine the profile of the board of directors/ trustees and the quality and competence of the senior management team in place.

- **Investment team**

CRISIL assesses composition of the fund's investment team and their qualification and past relevant fund management experience. CRISIL also examines their experience to manage funds through various market and economic cycles. The stability of the investment team, and their ability to work cohesively is assessed to evaluate their ability to generate stable performance over a long time horizon. In addition, the evaluation includes assessment of the quality of support functions including research and operations.

- **Investment decision-making process and discipline**

The objective is to assess philosophy of the investment team, the decision making process and discipline, and its consistency with the stated investment objective of the scheme. This is critical to achieve targeted performance over time in a consistent manner. CRISIL evaluates the consistency of the process through evaluation of the policy documents including investment, risk management and compliance policies. CRISIL also assesses the quality and effectiveness of the investment decision making process. As part of the process, CRISIL also assesses the role played by the Chief Investment Officer (CIO) in the entire decision making process. CRISIL also evaluates the practices and procedures followed to manage various types of inherent risks, and reviews audit reports to gauge the actual implementation of the policies, monitoring lapses in implementation, and the feedback mechanism.

- **Client communication, transparency and disclosure**

Client servicing forms the starting point of service standard perceptions for most investors. CRISIL will assess the various disclosure standards along with the quality and frequency of disclosures. CRISIL will assess the consistency of the fund title with the investment objective, transparency in portfolio disclosures, expenses, performance comparison with peers. CRISIL will also evaluate the client support function and the effectiveness of the same in handling customers and resolving their queries.

In addition to the above, CRISIL will assess other parameters including past instances of any severe regulatory indictment, and imposition of penalties.

## **2. Performance Assessment**

CRISIL will assess the scheme's past performance (if any) over a sufficiently long time horizon as well as the performance of the other existing and past schemes managed by the investment team to assess their performance track record. CRISIL will also benchmark the performance of the scheme with the relevant peers and benchmarks as part of the process.

CRISIL will also assess the size of the assets under management of the scheme and the growth in the same to assess the investor interest in the scheme. Assets being managed by the same investment team across schemes with similar investment strategy and investment objective will also be analysed.

## **Validity and Surveillance**

A Fund Management Capability Rating is valid for one year. Once a scheme is rated, CRISIL places the scheme under continuous surveillance to monitor for any variability in any of the key parameters driving the rating which can have an impact on the rating. In addition, any event likely to impact the rating, such as change in ownership/management, a merger or acquisition, or regulatory issues would also result in a detailed review of the rating.

Fund Management Capability Rating can be withdrawn based on a written request sent to CRISIL. CRISIL will place the rating on 'Notice of Withdrawal' for a period of three months from the date of formal communication in public domain. Subsequent to completion of the notice period, CRISIL will withdraw the rating.

## **Conclusion**

CRISIL Fund Management Capability Rating helps differentiate the rated scheme from its peers by highlighting inherent strengths and improving the positioning of the scheme and reach, with a wider investor base. It also enhances credibility through an independent, unbiased, and reliable opinion. It also facilitates investors take a well-informed and stable decision that exceeds reliance on past performance alone.

## About CRISIL Limited

CRISIL is a global analytical company providing ratings, research, and risk and policy advisory services. We are India's leading ratings agency. We are also the foremost provider of high-end research to the world's largest banks and leading corporations.

## About CRISIL Ratings

CRISIL Ratings is India's leading rating agency. We pioneered the concept of credit rating in India in 1987. With a tradition of independence, analytical rigour and innovation, we have a leadership position. We have rated over 75,000 entities, by far the largest number in India. We are a full-service rating agency. We rate the entire range of debt instruments: bank loans, certificates of deposit, commercial paper, non-convertible debentures, bank hybrid capital instruments, asset-backed securities, mortgage-backed securities, perpetual bonds, and partial guarantees. CRISIL sets the standards in every aspect of the credit rating business. We have instituted several innovations in India including rating municipal bonds, partially guaranteed instruments and microfinance institutions. We pioneered a globally unique and affordable rating service for Small and Medium Enterprises (SMEs). This has significantly expanded the market for ratings and is improving SMEs' access to affordable finance. We have an active outreach programme with issuers, investors and regulators to maintain a high level of transparency regarding our rating criteria and to disseminate our analytical insights and knowledge.

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