All You Need to Know about New Fund Offer (NFO)

A new fund offer (NFO) is essentially an invitation by an asset management company (AMC) for an investor to put their money into a new scheme floated by the company. It is a first- time subscription offer by a mutual fund that has come out with a new scheme or securities mix that is different or not available in any of its previous product baskets.

NFOs can be open-ended or close-ended and their subscription is open only for a limited period of time. Nonetheless, retail investors can still invest in these funds after their NFO subscription period at their market rate or net asset value (NAV) price.

For the layman, this can also be considered similar to an initial public offering (IPO) of equity securities. Investors must note that there are a number of differences between an IPO and NFO and they shouldn't be considered the same in any way.

How to Invest in NFOs?

Fund houses have launched NFOs both passive and active. These NFOs have been on debt and equity strategies. They have launched new funds for various reasons, such as filling the void in their existing basket of product offerings/ positive stance on sector or theme.

Since a NFO is structurally very similar to an IPO, the method to invest in one is also the same. Investors looking to invest in a NFO can do so through their registered stockbroker, demat account or mutual fund distributor.

Types of NFO

A NFO is mainly divided into two types: Open ended funds and close ended funds.

In open ended funds, the units in the NFO are available for subscription during the offer period and thereafter can be bought and sold from the open market, at any time, at the prevailing market price.

Close ended funds on the other hand are only available during a fixed tenure (mostly during the offer period) and can be redeemed only when the original investment tenure is over. This investment tenure can be anything from 3 years to 5 years or even more.

Points to ponder upon before opting for an NFO:

1. **Check the theme and objective of the NFO:**

Every NFO is released with a specific theme and objective in place. The objective can be growth, capital appreciation or value investing. On the other hand, all NFOs are based on a particular theme and invest in securities that fall under that theme or sector.

When considering an NFO, investors should study these objectives, themes, asset allocation, investment strategy and check if they align with their financial goals as well as risk taking ability.

2. **Minimum investment amount and lock- in period:**

Like normal mutual fund schemes, NFOs may be open-ended or closed-ended. NFOs may also have a definite lock- in period and minimum investment amount. All of these factors may differ from the amounts required when the fund is open for subscription at NAV or from the open market after the NFO has closed. Hence, while making an investment decision it is important to factor in these aspects and judge whether investing in the NFO is actually viable or not.

The minimum subscription amount in a new fund offer may range from INR 500 to INR 5,000.

3. **Reputation and history of the fund house:**

An NFO is an offer for a new scheme, hence it may not have a track record or historical data to study. However, the fund house it belongs to will most certainly have one. As much as it is important to study the viability of the NFO, it is also necessary to do a reputation check of the fund house it belongs to. One must analyse the past track record of the fund house as well as the fund manager before investing in the NFO. This will help you ensure that your funds are parked in a reliable scheme from a reputed company.

4. **Do not be carried away with the cost:**

Compared to a traditional mutual fund, an NFO is open to application at a NAV rate of INR 10. This low cost can often entice novice investors into parking their funds here. The biggest myth about an NFO is that it's cheap. As an investor, you have to look at the price and valuations at which the fund house is investing in the current market. Moreover, a low cost does not guarantee a good opening, fund performance or high/ sustained returns in any way. Hence, before investing, investors should go beyond the price and look at the other quantifiable attributes that will affect the fund and its investments in the long term.

5. **Other hidden costs:**

Every fund has a set percentage of costs attached to it. Funds have a progressive fee structure wherein percentage costs decrease as the fund grows in size. Though in an NFO, ascertaining the costs may be difficult – you can and definitely should estimate a ballpark figure depending on other funds in the same domain or on the same level as the new fund.

6. **Read the fine print:**

Last but not the least, it is important to read the fine print. There may be some details unique to the fund which may not be evident clearly on the face of it. Thus, it is always wise to dig deeper and do as much research as possible into the background of the fund manager, scheme information document and other stakeholders to ensure you are in safe hands. A check on your personal risk tolerance limit before investing is also a good decision.

Who Should Invest in NFO?

For investors who are looking for something new to invest in, an NFO based on a unique theme can be a good decision. One should check if the NFO is offering a unique theme or investment objective that suits your financial goals and risk appetite.

A lot of your investment decisions are also based on your faith in the sector. For example, if you are somebody who believes that the gaming sector is going to boom – an NFO investing in that sector may be a good bet for you.

Taxation

An NFO is taxed in the same way a normal mutual fund is taxed as per the Indian Income Tax Act. However, it must be noted that as per law not all mutual funds are taxed the same. Equity mutual funds and debt mutual funds have different criteria when it comes to calculating short term capital gains and long term capital gains. Hence, a conversation with your financial advisor can provide you with a clearer picture here.

Does Investing in a NFO Make Sense?

A new fund offer is a market linked security. Like any market linked security, it comes with its share of risks and rewards. Thus, any investment in a mutual fund should be based on a thorough workup and study and under the guidance of a qualified financial advisor.

Before adding a new scheme to your portfolio, it is important to evaluate your existing portfolio and see if you can afford to/ need to bring in that added element of risk. Investing in a new fund offer solely because it comes at a lower cost may not bode well with your financial plans here.

However, having said that – it is also important to be patient when it comes to judging the performance of a fund. Any new fund takes a minimum of two to three years to perform and generate valuable returns. Hence, this is only advisable for investors who are coming in for the long term.

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