



Rise of Alternate Investment Funds

Financial Services



Primus Partners India

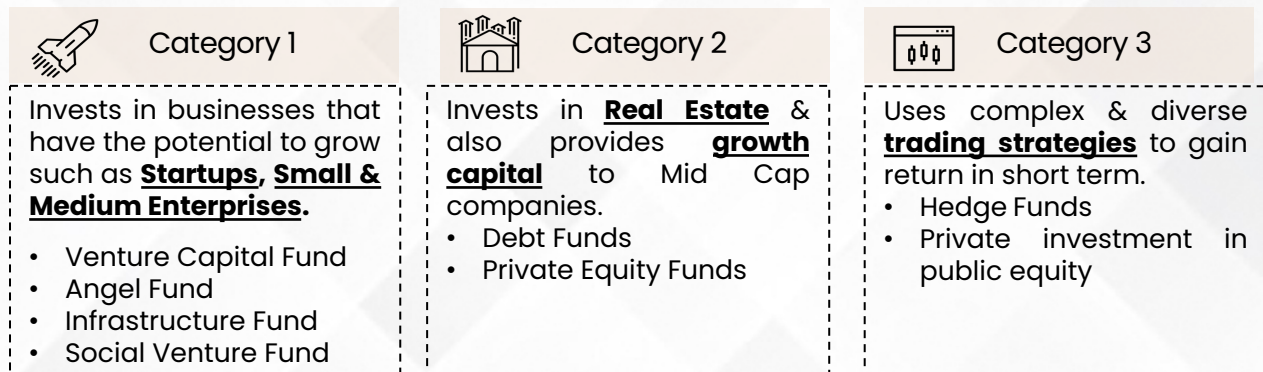


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Growth gathers pace for AIF

AIFs are privately pooled investment vehicles targeting HNI/UNHNIs

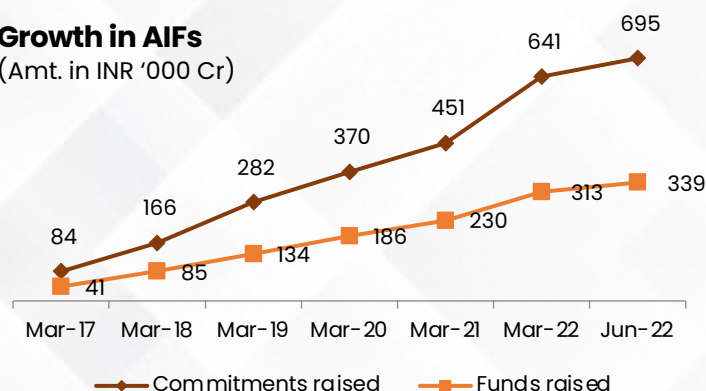
AIFs are privately pooled investment vehicles (Min investment of INR 1 Cr) that collect funds (foreign or Indian) for investing in listed & unlisted asset classes. In India, AIFs are categorized as below:



As HNIs look for diversification, AIF funds has grown over 8-fold since March '17

Growth in AIFs

(Amt. in INR '000 Cr)



- ❖ As on June 22, investments made constitute 92% of funds raised, up from 86% as on Mar '17.
- ❖ Category 2 AIF constituted 81% & 71% of the total commitments & funds raised respectively.
- ❖ Growth of Category 2 funds can be attributed to traction towards PE funds & real estate funds.

Despite growth, AIF's share in managed funds low, indicating high growth potential

	India	US	Europe
Share of AIF	AIF: 7% MF: 93%	AIF: 36% MF: 64%	AIF: 40% MF: 60%
Investment Threshold	INR 1 Cr	No limit	No limit
Investor Limitation	Max 1000 investors	Only Accredited investors	Retail participation allowed
Commission %	2-3%	1-2%	1-2%

Over the past 5 years, MF AUM grew at 16%, while AIFs investments grew at 52% indicating a shift in preference towards diversified investment tools. Given this, coupled with an underpenetrated AIF market, AIFs are poised to grow at a CAGR of 25% by 2025, led by advent of wealth managers.

Demand for AIFs increasing as a result of growing affluence & preference to diversify

The last 5 years have seen **wealth in India increase dramatically** as the number of HNIs, UHNIs & Billionaires in the country grows.

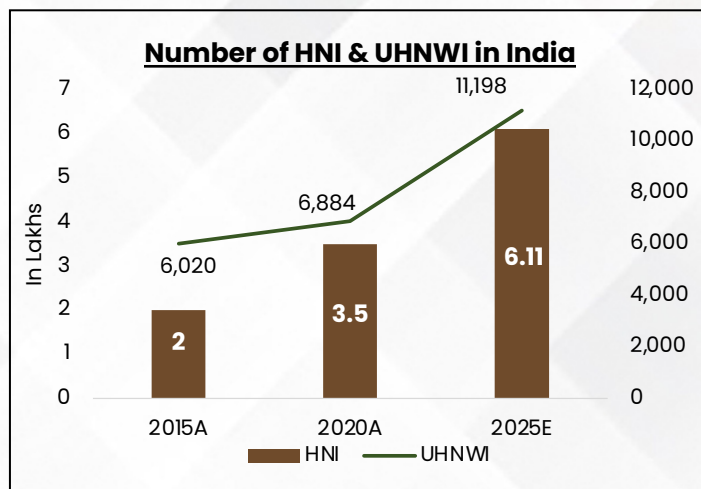
HNIs & UHNIs are individuals with net assets worth at-least \$1 Million & \$30 Million respectively.

The number of Indian HNIs has grown by 48% from 2.36 Lakh in 2016 to 3.5 Lakh in 2020.

The number is expected to go up to 6.1 Lakh by 2025, growing at an expected rate of 75% in 5 years against the global expected growth rate of 41%.

UHNIs are similarly expected to grow from 6,884 in 2020 to 11,198 in 2025 at 63% which is more than double the global expected growth rate of 27% in the same period.

In terms of the number of billionaires by country, **India now ranks third, behind only USA & China with 145 Billionaires as of March 2022.**



7 Lakh

No. of adult in India having wealth more than INR 7 Cr

3 Lakh

HNIs having investible surplus of more than INR 5 Cr in 2020

9 Lakh+

HNIs by 2027

Why AIFs are gaining popularity among the wealthy

Investors in India have started to diversify beyond traditional Equity & Debt classes to maintain a specific Risk-Return mix in the portfolio & to possibly earn higher returns.

Since AIFs are privately pooled investment funds with a minimum investment limit of 1 Crore, it is imperative that HNIs are the primary source of funds. HNIs benefit by investing in AIFs as they are an excellent option for generating consistent, higher returns with relative convenience & safety.

The AIF industry is the fastest-growing investment forum in India when compared to the traditional mutual funds or portfolio management services (PMS) industry. With robust diversification & inflation hedging, the rate of return prospect in AIFs is higher than that of orthodox investment avenues.

Salient features driving popularity of AIFs



Offer customization & diversification in the portfolio, serve as a buffer during market fluctuations



Offer Liquidity, Resilience & advantages of Equity Markets with much lower draw downs



Better source of passive income compared to many traditional instruments like debentures or bonds



Mitigate volatility as they are unrelated or less related to stock markets

Increased investor confidence has led to major players of financial eco-system venturing into AIF

Over the past 5 years, growth in the AIF industry has been phenomenal despite onset of the Covid-19 pandemic. Presently, AIFs have become a popular investment avenue amongst investors looking for sophisticated investment options providing higher risk-adjusted returns amid increasing volatility in the equity markets. This has led to an **increase in registered AIF in India from 181 to 979, growing at a CAGR of 27% from 2015 to 2022.**

Number of AIFs Registered in India



Major players of financial eco-system have ventured in the AIF space:

- ❖ Entities like **Indian Renewable Energy Development Agency Limited (IREDA)** are in the process of setting up a debt fund in the form of an AIF to tap large Institutional Investors (Insurance Funds, ESG Funds, Pension funds etc.).
- ❖ **Non-banking Financial Companies (NBFC)** via subsidiaries are gathering pace to enter the AIF industry
- ❖ AIF industry is the fastest-growing investment forum with several **banks plunging into the AIF space & leveraging its existing customer base.**
- ❖ **AIF Aggregators & Portals** such as PMS Bazaar, PMS AIF World & many others are leveraging the digital streak to enable investors to enter the AIF market easily.

Reasons for Increase in number of AIFs:



Introduction of online filing of applications for AIF & quarterly compliance reports by SEBI.



On-shoring the fund pooling structures via the AIF system: Permit pooling of rupee & foreign flows into an AIF as the pooling vehicle.



Simplification of AIF taxation: Granting of "pass thru status" for 2 categories of VC/PE funds amongst other smaller changes.



SEBI eliminated "lockup" of 1 year that PE investors had at IPOs of their investee companies.



Commission charged by AIFs is comparatively higher than other market linked financial products.

Banks	Category
Axis Bank	II & III
Kotak Bank	I & II
ICICI Bank	III

Financial Services Firm	Category
Motilal Oswal	III
IIFL	I, II & III
Edelweiss	I, II & III

AMCs	Category
Nippon India	II & III
Sundaram	II & III
Abakkus	III

The AIF industry has now come under the scrutiny of SEBI, with new players entering the space due to increased demand. Leading to additional compliances that drive up the expenses & are ultimately passed on to investors. Therefore, it is crucial for the regulatory bodies to continue simplifying processes to maintain the existing cost structure.

Reforms in AIF policy a sign of maturing market

Regulatory Changes & simplification of Process appeals to major players:

Indian Government along with SEBI are actively ensuring adoption of clean & transparent governance practices in the financial markets by entities operating in India. SEBI has reconstituted its AI Policy Advisory Committee (AIPAC), which advises the capital market regulators on issues that impact further development. The committee has published 3 reports which highlights major areas of reform for the AIF community.

Some of the more recent amendments in AIF policy have been geared towards promoting & expanding the scope of AIFs in India, such as:



Widening scope of Investment for Indian Funds: SEBI allowed AIFs to invest in overseas companies that may not have an India connection by way of a back office or subsidiary.



Investment in Stressed Assets: Introduction of a new sub-category under Cat I fund called 'Special Situation Funds'



Transparency: Standardizing Private Placement Memorandums (PPMs) to ensure disclosure of essential information



AIFs operating from International Financial Services Centre (IFSC) to innovate fund structures: Providing regulatory leeway such as leveraging activities, co-invest in portfolio companies & exemptions to non-resident investors to obtain PAN etc.



Expansion in the definition of Venture Capital Undertaking (VCU): By expanding the definition of VCU to include 'any company not listed on the exchange at the time of investment', even NBFCs are a part of VCU definition.

Expert Take



Mr. Abhishek Ravi
Partner, Ravi Rajan
& Co.

When the government came out with AIF regulations in 2012, capital invested was less than 1% of the capital committed, whereas the same number stands at ~50% of the capital invested as of June 2022, an exemplary CAGR of 63% in terms of capital commitments. **Global AUM under AIFs is also expected to grow from USD 10.7tn in 2020 to USD17.2tn in 2025.**

SEBI has been highly involved in the governance of these AIFs, providing comfort to domestic & foreign investors. To channelize diverse variety of funds into underserved MSMEs & address growth needs of viable & high growth MSMEs, the government introduced an SRI (Self-Reliant India) Fund.

It is an MSME scheme of 50,000 crores, structured as mother-daughter fund whereby GOI will provide 10,000 crore & rest 40,000 crores would come via the AIF route. This highlights the government's intent & positive outlook towards AIFs.

While AIFs have become more transparent for investors, compliance on fund managers has increased.

While Category II funds have taken the lead, Category I will also see growth on account of introduction of Special Situation funds by the Government. These funds invest in assets that are already under the Insolvency & Bankruptcy Code (IBC) & Security receipts issued by Asset Reconstruction Companies. These funds have already helped turnaround some major stressed assets & henceforth will receive major traction.

Rising popularity of AIFs as an avenue of financing



Mr. Shravan Shetty

Managing Director, Primus Partners

The Venture Capital Fund (VCF) has managed to raise commitments of ₹34,569.56 crore during December 2021 compared to ₹26,791.7 crore during the same period last year, showing an increase of 29%.

Lackluster performance of traditional or active funds is a precursor:

The past 2 decades have seen actively managed funds perform worse than their benchmarks. In India, trailing returns data depicts that on an average, over 70% equity mutual funds underperformed in the 5-years.

Given the lackluster returns from funds & fixed income products coupled with high management fees, investors are looking at different avenues to park their assets.

Alternate investment funds (AIFs) provide investors with a diversification portal, letting investors allocate capital to various types of assets that traditional funds are not able to access.

Category II has seen major growth in the last 5 years:

In India Category II AIF is leading in terms of capital commitment, funds raised & investment. Even as of today, investors have the option to invest in real estate & infra projects, but investment process becomes easier when routed through an AIF due to no associated pricing norms, debt limits etc. Additionally, there is a possibility of tax-pass through which means the investor will be taxed & not the fund business [for Categories I & II]. Since investment managers must invest their own funds [10cr or 5% of committed

capital], there is skin in the game for these funds & motivation to yield better returns.

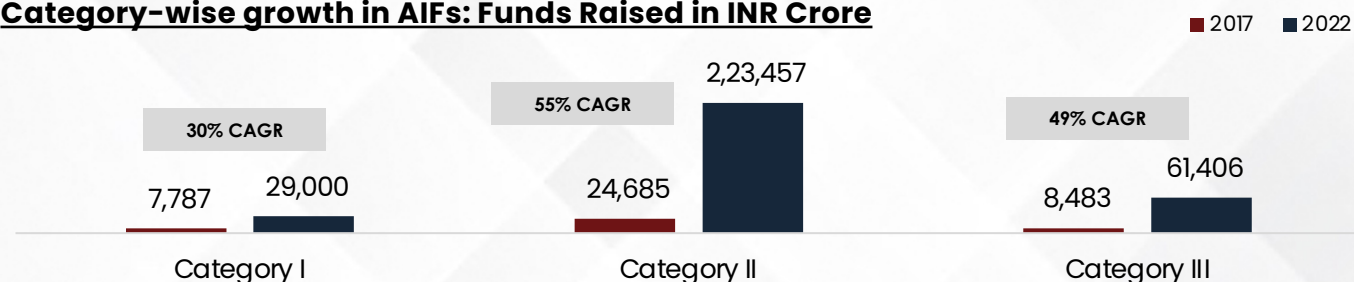
Establishing IFSC & other policy reforms are driving force behind AIF progress:

Initiatives such as the International Financial Services Centre (IFSC) in GIFT city indicate a positive outlook towards AIFs in India. Reduced tax on dividends & interest & tax-holidays are just some of the advantages available for an AIF listed in IFSC. The government has also proactively encouraged insurance & pension funds to allocate investments towards Indian AIFs. Recommendations provided by the AIPAC committee headed by Mr. Narayan Murthy provided relevant & contextual reforms for the AIF industry to help increase visibility, stability & regulatory maturity.

Major corporate players are keen to enter the AIF space as an alternative to project financing:

Large corporations have shown a keen interest in raising financing by setting up AIFs. Financing via AIF provides multiple advantages such as high degree of customization & flexibility to structure the fund for both the investor & the company. AIFs are a good alternative to the traditional project financing.

Category-wise growth in AIFs: Funds Raised in INR Crore



With positive steps towards improving regulatory landscape, unlocking domestic capital pools & increasing asset returns, AIF industry is poised to grow exponentially.

➤ Policy News

SEBI eases norms on AIF & VCF investments in overseas firms; drops India connection clause

Aug 19, 2022

Capital markets regulator SEBI has allowed India registered Alternative Investment Funds (AIFs) & Venture Capital Funds (VCFs) to invest in foreign entities without having an India connection. [Read more](#)

Alternative investment funds under SEBI lens as growth gathers pace; Assets up 42% so far this year

Jul 22, 2022

The Securities & Exchange Board of India (Sebi) is increasing its oversight on alternative investment funds (AIFs) — subject to light-touch regulations until now — given the pace of growth clocked by the industry. [Read more](#)

Market Regulator shifts focus to Monitoring AIFs

Jul 5, 2022

The Securities & Exchange Board of India is often criticized for failing to enforce regulations on Alternative Investment Funds (AIFs) with consistency. However, a recent SEBI order indicates a change in approach & shows that perhaps monitoring, investigation, & enforcement with regard to such funds is increasing. [Read more](#)

SEBI issues guidelines for 'Large Value Fund' for accredited investors

Jun 24, 2022

Capital markets regulator SEBI on Friday came out with new guidelines for "Large Value Fund" for accredited investors, pertaining to filing of such schemes & extension of their tenures beyond two years. [Read more](#)

SEBI amends rules governing alternative investment funds

Mar 17, 2022

Under the rules, Category III AIFs can invest not more than 10% of the investable funds in an investee company, directly or through investment in units of other AIFs, Sebi said in a notification on Wednesday. [Read more](#)

SEBI rejigs advisory committee on alternative investment policy

Feb 20, 2022

Sebi has reconstituted its alternative investment policy advisory committee, which advises the capital markets regulator on a range of issues that impact further development of the AIF space. The committee has now 20 members, as per an update by the Securities & Exchange Board of India (Sebi). [Read more](#)

➤ Industry News

How PMS & AIF have gained investors & expanded asset base

Aug 16, 2022

The PMS industry had 13.6 million clients at the end of June. PMS is different from mutual funds as all investor flows are not pooled in a single scheme. Instead, investments for each client are held in the clients' individual demat accounts. This also allows PMS solutions to be more customised to client's specific need. [Read more](#)

AIF assets surging towards ₹7-lakh crore mark

Aug 5, 2022

Option to diversify investments & low correlation with equity markets among factors attracting investors. [Read more](#)

SEBI red-flags delays in launches by AIFs: Regulator to issue guidelines

Aug 3, 2022

Nearly 300 schemes got investments more than 5 years after they were first registered, finds Sebi.

The Securities & Exchange Board of India (Sebi) has expressed its displeasure over inordinate delays in scheme launches of alternative investment funds (AIFs). [Read more](#)

hBits plans to raise Rs 5 billion through AIF

Jul 22, 2022

The platform for fractional real estate ownership, hBits, intends to raise more than Rs 5 billion through an Alternative Investment Fund (AIF) in order to invest in commercial real estate, including projects for offices, data center. [Read more](#)

AIF industry grows 7 times in 5 years as HNIs scout for diversification

Jun 29, 2022

Indian AIF industry (alternative investment funds) is standing at Rs 6.4 lakh crore commitments raised as on 31st March 2022, an incredible 7 times growth in the past 5 years. [Read more](#)

Alternative Investment Funds To Grow 25% By 2025, Says Report; What's Making Them Popular?

May 25, 2022

Asia & the emerging economies, especially India, are poised for the next big growth in alternative investment products. In terms of assets under management (AUM), AIFs in India are at the same stage that mutual funds were at, in 2009. The market & the industry is now geared towards a paradigm shift towards alternative investment funds. [Read more](#)

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About Primus Partners

Primus Partners has been set up to partner with clients in 'navigating' India, by experts with decades of experience in doing so for large global firms. Set up on the principle of 'Idea Realization', it brings to bear 'experience in action'. 'Idea Realization'— a unique approach to examine futuristic ideas required for the growth of an organization or a sector or geography, from the perspective of assured on ground implementability.

Our core strength comes from our founding partners, who are goal-oriented, with extensive hands-on experience and subject-matter expertise, which is well recognized in the industry. Our core founders form a diverse cohort of leaders from both genders with experience across industries (Public Sector, Healthcare, Transport, Education, etc), and with varied specialization (engineers, lawyers, tax professionals, management, etc).



PASSION

for providing solutions to help clients achieve their goals

RESPECT

For all and alternate viewpoints

INTEGRITY

of thoughts and actions

MASTERY

of our chosen subject to drive innovative and insightful solutions

US

Representing the Primus collective, where each individual matters

STEWARDSHIP

for building a better tomorrow

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