

Alternative Investment Funds

Alternative Investment Funds (AIF for short) are those funds created or established in India as a privately pooled investment vehicle in order to collect funds from specific investors as per a previously defined investment policy.

Recently the Union Cabinet had approved the creation of an Alternative Investment Fund of Rs. 25,000 crore to revive affordable housing projects.

This article will give details about the Alternative Investment Funds within the context of the Civil Services Examination.

Overview of Alternative Investment Funds

Alternative Investment Funds consist of investment funds pooled in together which is then used in investing private equity, hedge funds etc

Regulation 2(1)(b) of the Regulation Act, 2012 of Securities and Exchange Board of India (SEBI) lays down the definition of AIFs. Through a company, or a Limited Liability Partnership (LLP) and Alternative Investment Fund can be established.

AIF does not include funds that are included in the regulations of the SEBI which oversee fund management activities. Other exemptions include family trusts, employee welfare trusts or gratuity trusts.

***Note:** The SEBI granted further exemptions to AIFs on investment committee framework in January 2021. The exemption in AIF rule is conditional upon a capital commitment of at least Rs 70 crore from each investor accompanied by a suitable waiver.

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Types of Alternative Investment Funds

As per the Securities and Exchange Board of India, AIFS are divided into three categories. They are as follows:

1. Category 1 AIFS

These funds are invested in businesses that are new or have the potential to grow financially such as StartUps, Small and Medium Enterprises. The government encourages investments in these ventures as they have a positive impact on the economy with regards to high output and job creation.

Examples of this category are as follows:

- Infrastructure Funds
- Angel Funds
- Venture Capital Funds
- Social Venture Funds

2. Category 2 AIFS

Under this category, funds that are invested in equity securities and debt securities are included. Those funds not already under Category 1 and 3 respectively are also included. No concession is given by the government for any investment made for Category 2 AIFS

Examples of this category are as follows:

- Fund of Funds
- Debt Funds
- Private Equity Funds

3. Category 3 AIFS

Category 3 AIFs are those funds which give returns under a short period of time. These funds use complex and diverse trading strategies to achieve their goals. There is no known concession or incentive given towards these funds specifically by the government

Examples of this category are as follows:

- Hedge Funds
- Private Investment in Public Equity Funds

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Benefits and Drawbacks of Alternative Investment Funds

Like all financial instruments, Alternative Investment Funds have come with their share of benefits and drawbacks. They are as follows:

Benefits:

- Alternative Investments may help in reducing volatility that is commonly associated with traditional investments as their performances are not dependent on the ups and downs of a stock market.
- Helps in diversification in terms of markets strategies and investment styles

- Strong potential in improving performance.

Drawbacks

- A high investment amount is required, something which is not possible for small-scaled investors.
- Alternative investment funds are complex funds and due diligence is needed before deciding to invest in them.

Frequently Asked Questions about Alternative Investment Funds

What is a Debt Fund?

A debt fund is a fund whose primary purpose is to be invested in debt or debt securities

What is Fund of Funds?

A fund of funds (FOF) is a pooled investment which invests in other types of funds. It is also known as a multi-manager investment. An FOF is aimed at achieving broad diversification and proper asset allocation.

What is the Corpus of an AIF?

“Corpus” is the total amount of funds committed by investors to the AIF by way of a written contract or any such document as on a particular date.