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What is NAV and Why It Matters

Portfolio The term **Net Asset Value (NAV)** is one of the most commonly used metrics in mutual fund investing, yet it is often misunderstood. For many investors, a lower NAV appears “cheaper” and a higher NAV appears “expensive,” leading to decisions that are not always rational. In reality, NAV is simply a representation of a fund’s per-unit value and does not, by itself, determine whether a fund is a good investment. Understanding what NAV truly means—and what it does not—can help investors make more informed and disciplined investment decisions.

Understanding NAV

NAV, or Net Asset Value, represents the per-unit value of a mutual fund. It is calculated by taking the total value of the fund’s assets, subtracting its liabilities, and dividing the result by the total number of units outstanding. In formula terms:

$$\text{NAV} = (\text{Total Assets} - \text{Total Liabilities}) / \text{Number of Units}$$

The assets of a mutual fund include the market value of all the securities it holds—such as equities, bonds, or money market instruments—along with any accrued income. Liabilities may include management fees, operational expenses, and other payable amounts. Since the market value of the underlying securities changes daily, the NAV of a mutual fund is typically updated at the end of each trading day.

For example, if a mutual fund holds securities worth ₹100 crore and has liabilities of ₹2 crore, the net assets amount to ₹98 crore. If there are 10 crore units outstanding, the NAV would be ₹9.80 per unit. This value reflects the price at which investors can buy or sell units of the fund (subject to applicable loads, if any).

Why NAV Changes

NAV fluctuates daily because the prices of the underlying securities change. If the stocks or bonds held by the fund increase in value, the NAV rises. Conversely, if the market value of these holdings declines, the NAV falls. Additionally, dividend payouts by the fund can also affect NAV, as the payout reduces the total assets of the fund.

It is important to note that NAV movements reflect the performance of the underlying portfolio. Therefore, NAV is a mirror of the fund’s performance rather than an independent driver of returns.

Why NAV Matters

NAV is important because it provides transparency and a standardized way to measure the value of a mutual fund investment. It allows investors to track how their investment



is performing over time. A rising NAV indicates that the value of the fund's underlying assets is increasing, while a falling NAV suggests the opposite.

However, NAV's importance lies more in **tracking performance** rather than **evaluating attractiveness**. Investors often compare NAVs across funds and assume that a lower NAV offers more upside potential. This is a misconception. A fund with an NAV of ₹10 is not necessarily “cheaper” than one with an NAV of ₹100. What matters is the percentage growth, not the absolute NAV.

For instance, if you invest ₹10,000 in a fund with an NAV of ₹10, you receive 1,000 units. If the NAV rises to ₹12, your investment grows to ₹12,000—a 20% return. Similarly, if you invest ₹10,000 in a fund with an NAV of ₹100, you receive 100 units. If the NAV rises to ₹120, your investment also becomes ₹12,000—again, a 20% return. In both cases, the return is identical, regardless of the starting NAV.

Common Misconceptions Around NAV

One of the most widespread myths is that funds with lower NAVs have greater growth potential. This belief often leads investors to prefer newly launched funds (New Fund Offers or NFOs), which typically have an NAV of ₹10. However, a lower NAV does not imply undervaluation. Unlike stocks, where price can indicate value relative to earnings or assets, NAV simply reflects the current value of the fund's holdings.

Another misconception is that a higher NAV means a fund is overvalued or has limited scope for growth. In reality, a higher NAV often indicates that the fund has performed well over time. Many established funds with strong track records have higher NAVs because they have compounded returns over the years.

What Investors Should Focus on Instead

Rather than focusing on NAV levels, investors should evaluate mutual funds based on factors such as:

- Consistency of returns over different time periods
- Risk-adjusted performance
- Fund manager's track record and investment philosophy
- Expense ratio and portfolio quality
- Alignment with financial goals and risk tolerance

These factors provide a more meaningful assessment of a fund's potential than its NAV.



Role of NAV in Transactions

NAV also plays a practical role in mutual fund transactions. When investors purchase units, they do so at the applicable NAV (plus any charges, if applicable). Similarly, when redeeming units, the redemption value is based on the prevailing NAV. In systematic investment plans (SIPs), investments are made at different NAVs over time, allowing investors to benefit from rupee cost averaging.

Conclusion

NAV is a fundamental concept in mutual fund investing that reflects the per-unit value of a fund. While it is essential for tracking performance and facilitating transactions, it should not be the primary factor in investment decisions. The true measure of a mutual fund's merit lies in its ability to generate consistent, risk-adjusted returns over time.

Investors who understand the role of NAV—and avoid common misconceptions associated with it—are better positioned to make rational investment choices. Instead of chasing “low NAV” funds, a disciplined focus on long-term goals, asset allocation, and fund quality will lead to more effective wealth creation.

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* Mutual funds are subject to market risks. Please read all scheme-related documents carefully before investing. Past performance does not indicate future results. Investments are subject to market fluctuations, and there is no assurance of returns.

