

MUTUAL FUND ANALYSIS

Sharpe ratio in mutual funds: a past score, not a promise

What the metric can tell you — and what it cannot.

THE PRACTICAL QUESTION

Did the fund earn enough excess return to justify the volatility it took on?

The Sharpe ratio measures excess return per unit of volatility in [mutual funds](#).

READ IT AS

Return quality

Not a promise of what comes next.

THE FORMULA

The formula is simple;
the comparison is not

$$\text{Sharperatio} = \frac{\text{Fund return} - \text{Risk-free rate}}{\text{Standard deviation of returns}}$$

Sharpe ratio

Fund return

Return over the period,
often annualised.

Risk-free rate

Commonly the 91-day
Government of India
Treasury-bill yield.

Standard deviation

Total volatility in the
fund's returns.



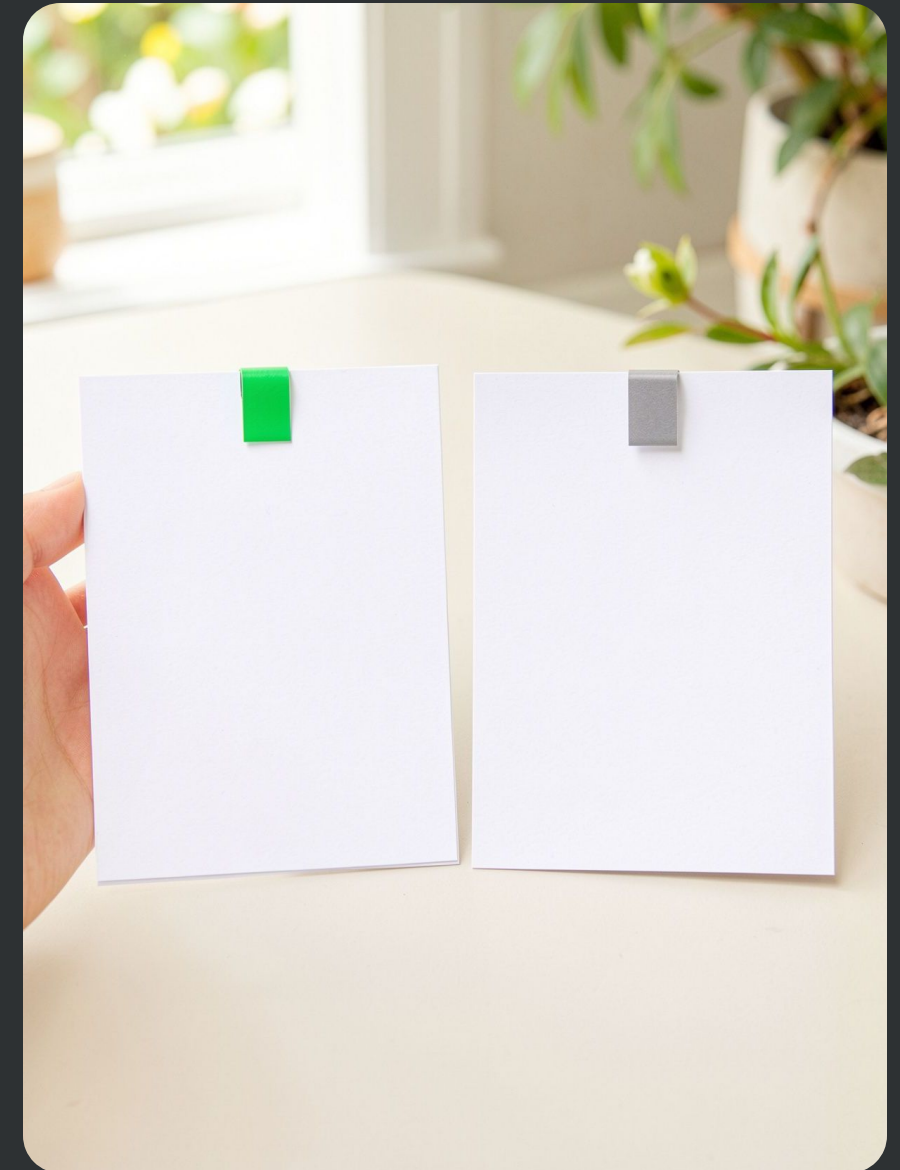
COMPARISON FRAME

Higher is better only inside the same frame

A ratio of 0.8 means 0.8 units of excess return for each unit of volatility.

A negative ratio means the fund underperformed the risk-free rate during that period.

Compare the same category over the same time window, not a small-cap fund with a liquid fund.



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RETURN QUALITY

Use it to test return quality, not just return size

Absolute return

The size of the result.

Sharpe ratio

Adds a risk lens to absolute return.

It is often calculated from trailing three-year monthly returns, but vendors can use different windows and risk-free rates. Small differences in the published number are common.

THRESHOLDS

There is no universal “good” number

01

Positive beats negative

Positive is generally better than negative.

02

Category first

Within a category, above-average is more informative than an isolated threshold.

03

Above 1 is a rule of thumb

Not a SEBI norm or safety certificate.

04

Ranges differ

Equity, debt, and arbitrage funds naturally occupy different ranges.

DATA SOURCES

Platforms can show the number; none owns the ranking

Research screens publish it

[Value Research](#), Morningstar India, and broker research screens publish Sharpe ratios alongside measures such as Sortino, alpha, and standard deviation.

Data is not a regulator-approved ranking

[AMFI](#) releases scheme returns and [other scheme data](#), but there is no regulator-approved “top Sharpe” list.

THE LIMIT

A high Sharpe ratio can still disappoint next

The ratio describes a past window. Market regime changes, interest rates, manager changes, style drift, concentration, liquidity, and credit risk can all change the next result.

A fund can look strong after an unusually calm rising market, then lag when volatility or leadership changes.

CHECK BEFORE YOU SORT

Eleven mistakes to avoid

01 Buying the highest Sharpe without checking fit.

02 Comparing across categories or mismatched time windows.

03 Treating above 1 as "safe."

04 Ignoring category averages, fees, exit loads, AUM, mandate drift, and manager changes.

05 Building an entire portfolio from one sorted list.

06 Assuming an Indian T-bill rate fits every investor's home currency.

THE REAL DECISION

Use Sharpe as one lens, then make the real decision



Choose the category for the goal and horizon first.



Check costs, mandate, portfolio risks, manager continuity, and fit.



Compare funds inside that category and time window.



Use Sortino, Treynor, or information ratio when their risk lens is more relevant.

For the full source discussion, read [Sharpe Ratio in Mutual Funds: Formula and Limits](#).

