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   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

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INDIAN MUTUAL FUND MARKET: AN OVERVIEW

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ABSTRACT

India is considered for years as one of the attractive investment destinations worldwide. There are many opportunities for investments where Mutual fund is one of them. Indian mutual funds industry has witnessed a rapid growth in the past few years driven by several favourable economic and demographic factors. With the growing volatility in the stock market, retail investors are looking forward to mutual funds as their investment avenues. Hence, it is of utmost significance to understand mutual fund industry, which is an alternative for direct investment in stock market. As such, this paper makes an attempt to review the various literatures available in the mutual fund industry to understand the performance of funds and investment decision of small active retail investors. The study shows that high competitions among the private and public players in the industry have affected the performance of the mutual funds. It is also found that retail investors are still confused about the mutual funds as an investment avenue. In order to attain sustained profitable growth, the industry should focus on developing distribution networks, increasing retail participation and expanding the reach of mutual funds by conducting awareness programs and extending financial literacy.

KEYWORDS

Fund Performance, Investment Behaviours, Mutual Fund and Retail Investors.

1. INTRODUCTION

A mutual fund is a financial intermediary that pools the saving of investors for collective investment in a diversified portfolio of securities. A fund is 'mutual' as all of its returns minus its expenses are shared by the fund's investors (Pathak, 2008). The Securities and Exchange Board of India (Mutual Funds) Regulation Act, 1993 defines a mutual fund as "a fund established in the form of a trust by a sponsor, to raise money by the trustees through the sales of units to the public, under one or more schemes, for investigating in securities in accordance with these regulations" (Gurusamy, 2007). Mutual fund is considered to be a better opportunity where savings are collected from investors and diverted to the capital market to generate better returns for them with lower risk and volatility.

A tremendous growth has been witnessed in India since 1991. With liberalization in India economy, there has been a sea change in the financial market. Consistent with this evolution, Indian mutual funds industry has also witnessed a rapid growth. The reason behind such a considerable attraction towards mutual funds was essentially due to assured returns along with security to investors' investment (Sanyasi, 2013). Large market potential, rising income, high saving rate, growing risk appetite, comprehensive regulatory framework by SEBI, favourable tax policies, introduction of new products, increasing awareness etc have made mutual funds a preferred investment option (Rekha, 2012). Small investors face many hardships in stock market investment decision making. They cannot afford to have vast knowledge of market behaviour and lack knowledge about maximising gains by proper selection and timing of investment. As such, mutual funds are the secured way for small investors to enter the capital market (Viramgami, 2009).

The revolution in last decade was the outcome of policy proposal taken by the Government of India where by public sector banks and insurance sectors were permitted to enter the fund market (Gupta, 2000). In a short span of less than one decade, India has observed a changed in the investment pattern of small and medium investors. India's market for mutual fund has witnessed a CAGR of about 29% in a five year period from 2004-2008 as against global average of 4% which accounts as the most rapidly growing market in the world (Gupta, 2011). India has secured the best position among the top ten globally reputed mutual funds as far as growths of the funds are concerned. It has even moved from 27th place to 26th place in the recent past. Mutual funds transactions on the stock exchanges have also witnessed an inspiring growth over the years. They indeed have been playing a stabilising role in the ever volatile stock markets (Chary and Masood, 2010-2011). The regulating authorities namely Securities and Exchange Board of India (SEBI) and Association of Mutual Funds in India (AMFI) supervising and regulating mutual fund industry are trying to guard and protect the investors in India (Santhi and Gurunathan, 2011). Mutual funds have been penetrating into rural areas with diversified products and better corporate governance. Retail investors are steadily banishing of the stock market and diverting savings into mutual funds sector. They acquire stocks or bonds through mutual funds at lower trading costs and get the benefit of diversification and risk minimization (Khare, 2007). Penetration of mutual fund market has been only 13.7% unit holders from rural area and 38% from urban area. It portrays a very sluggish growth in the industry. However, with a booming economy and 32.4% saving rate in India, there are lots of scope for favourable growth of mutual fund industry in India (Pandey, Rathore and Khare, 2007).

1.1 PLAN OF THE PAPER

The structure of the paper has been divided into four parts. Section 1 deals with introduction, section 2 presents the theoretical background of mutual fund and section 3 focuses on the findings of some of the earlier studies and conclusions of the study appears in section 4.

2. THEORETICAL BACKGROUND OF MUTUAL FUND

A small investor saves a part of his income to meet future expenses such as education, marriage, medical purposes and purchase of products. There may be some expenses that are unforeseen. These diverse needs are expressed in terms of investment objectives as safety, liquidity and high return. In order to meet the diverse needs of a multitude of investors, mutual funds have designed and offered a wide variety of mutual fund schemes. Investors have the option of choosing from the wide variety of schemes depending upon their requirements. Schemes may be categorised in many ways. At the most primary stage, mutual funds may be close-ended or open-ended, which are the types of mutual funds categorised by their structure. The subsequently categorization of mutual fund is based on their characteristics with respect to the risk level of the asset invested, nature of asset invested, the fund's objectives, industry to which the invested assets belong, trading and investment strategies adopted, structure, frequency of dividend payment and so forth. Schemes based on an asset category of investment may be equity funds, debt funds, money market funds, gilt funds, real estate funds and so forth. Growth funds, balanced funds and income funds portray the extent of the combination of different asset categories in the investments. Industry specific or sectoral funds focus upon specific industries or sector.

In recent years, some innovative mutual funds have been launched in India to provide investors with greater access to markets like the gold market and art market. They are innovative in the sense that they are new to Indian investors. Thus, mutual funds adopt different strategies to achieve investors' objectives and accordingly offer different schemes of investments. Mutual funds are supervised by a group of professional managers. Funds' investment portfolios are persistently evaluated and revised to closely match the fund's stated investment objective.

An Asset Management Company (AMC) is required to calculate the Net Asset Value (NAV) of all open-ended schemes on a daily basis and at the least on a weekly basis for close-ended ones and publish these in a minimum of two national newspapers. The NAV of a fund at any point in time is the sum total of the market value of the assets that comprise its portfolio minus the liabilities at that time. In other words, the NAV of a fund is the amount that all the unit holders will receive if the fund is dissolved or liquidated after paying all its liabilities.

A mutual is a set up in the form of trust, which has sponsor, trustee, AMC and custodian. Sponsor is the person who acts alone or in combination with another body corporate and establishes a mutual fund. Sponsor must contribute at least 40% of the net worth of the investment managed and meet the eligibility criteria prescribed under the Securities and Exchange Board of India (Mutual Funds) regulations, 1996. The sponsor is not responsible or liable for any loss or shortfall resulting from the operation of the schemes beyond the initial contribution made by it towards setting up of mutual fund. The mutual fund is constituted as a trust in accordance with the provisions of the Indian Trusts Act, 1882 by the Sponsor. Trustee is usually a company (corporate body) or a board of trustees (body of individuals). The main responsibility of the trustee is to safeguard the interest of the unit holders and also ensure that AMC functions in the interest of investors' and in accordance with the SEBI regulations, the provisions of the trust deed and the offer document of the respective schemes. The AMC is appointed by the Trustees as the investment manager of the mutual fund. The AMC is required to be approved by SEBI to act as an AMC of the mutual fund. The AMC if so authorized by the Trust Deed appoints the Registrar and Transfer Agent to manage the mutual fund. The registrar processes the application form, redemption requests and dispatches account statements to the unit holders. The Registrar and Transfer agent also handles communications with investors' and updates investor records.

3. DISCUSSIONS

Mutual funds have attracted the attention of global practitioners and academicians in India and abroad to evaluate the performance of various schemes from time to time by considering return and risk of the investment. As there is a vast universe of companies in the field of mutual funds providing unlimited number of schemes, it becomes really hard to evaluate the performance of all companies in a single study. A few of the studies conducted in this field were pioneered by Treynor (1965), Sharpe (1966), and Jensen (1968). It was followed by numerous other studies that have evaluated the performance of portfolios and analyzed the investment behaviours of mutual fund investors.

3.1. FUND PERFORMANCE

A few studies were carried out from time to time to evaluate the mutual fund performance in India. Jayadev (1996) attempted to evaluate the performance of two growth oriented mutual funds namely Mastergain and Magnum Express on the basis of monthly returns and compared to benchmark returns. The study concluded that the two funds had disappointed in earning better returns. Mastergain performance was superior as per Jensen and Treynor measures and on the basis of Sharpe ratio, its performance was unsatisfactory when compared with benchmark. The performance of Magnum Express was unsatisfactory on the basis of all these three measures. Gupta and Sehgal (1998) evaluated performance of 80 mutual fund schemes over four years (1992-96). The study has tested the proposition relating to fund diversification, consistency of performance, parameter of performance and risk-return relationship. The study has noticed the existence of inadequate portfolio diversification and consistency in performance among the sample schemes. Gupta (2001) assessed the outcome of 73 selected schemes with different investment objectives, both from the public and private sector using Market Index and Fundex. NAV of both close-ended and open-ended schemes from April 1994 to March 1999 were also tested. The result depicted that the selected schemes had not been properly diversified and risk and return of schemes had not fulfilled their scheme's objectives. Elango (2004) empirical work depicted that private sector schemes has outperformed public sector in terms of NAV, innovative products and in deployment of funds. Moreover, public sector funds showed low volatility as against greater inconsistency for private sector. Sondhi and Jain (2005) observed 19 private and 17 public sector mutual fund equity schemes during the period 1993-2002. There existed a lack of consistency in the performance of the funds. The returns were higher than the BSE 100 index. However, it was lower than the returns on 364 days treasury bills. Private equity schemes had outperformed due to its reputation, professional management, well-researched stock selection and timing skills. More than three-fourth of public sector schemes couldn't attain better returns in spite of higher investor confidence and high safety. Muthappan and Damodharan (2006) examined 40 schemes during April 1995 to March 2000. The study concluded that majority of the schemes has achieved superior returns compared to the market but has not performed better than 91 days Treasury bill. They further observed that 23 schemes has outperformed both in terms of total risk and systematic risk. 19 schemes performance were superior while growth schemes earned average monthly return. The average unique risk of 7.45% with an average diversification of 35.01% concluded that the sample schemes were not adequately diversified. Guha (2008) determined the return-based style analysis of equity mutual funds in India using quadratic optimization of an asset class factor model proposed by William Sharpe. The study identified the "Style Benchmarks" of each of its sample of equity funds as optimum exposure to 11 passive asset class indexes. The study evaluated the performance of the funds with respect to their style benchmarks and had observed that the performance of the funds were inferior to their style benchmarks on the average. Bhatt and Patel (2008) examined the performance of 10 mutual fund scheme using Sharpe index method. The study identified that fund having high index value had performed better than fund having low index value. Mehta (2010) evaluated the performance of 10 funds of the both UTI and SBI mutual fund schemes during 2006-07 and 2007-08 on the basis of portfolio evaluation techniques using Sharpe, Treynor and Jensen Index and FAMA. The study depicted that SBI mutual fund schemes had outperformed UTI schemes in the both the years and UTI and SBI mutual funds had superior returns in 2007-08 as compared to 2006-07. Dharmraja and Santhosh (2010) examined 5 Balance mutual fund and 5 Income mutual funds for a period of two years - Bull Run period from January 2007 to December 2007 and Bear Run period from January 2008 to February 2009. The findings showed that return during Bull Run period was maximum accompanied by high rate of risk. The performance of the Balance mutual fund was inferior to the market during the Bull Run period. During the Bear Run period, Income mutual fund has lesser risk compared to stock market. On comparing balance mutual funds and income fund, it was concluded that income funds had performed better than the balance mutual fund during Bear Run period and mutual fund investment were relatively risk free than stock market as the investment being managed by the professionals. Devi and Kumar (2010) focused on the performance of Indian and foreign equity mutual funds and had concluded that among Indian equity funds, the returns are highest for Equity Tax Savings Funds (55.87%) followed by Diversified Funds (54.73%) whereas it is just the reverse in case of foreign mutual fund as Equity Diversified Funds are the toppers in return (57.57%) followed by Equity Tax Savings Funds (82%). They further identified that there is not much difference in the returns between Indian and foreign equity index funds and equity tax savings funds. Dhume and Ramesh (2011) evaluated the performance of the few sector specific mutual funds using different approaches of performance measures. The sectors considered for the study were banking, FMCG, infrastructure, pharma and technology. The study highlighted that all the sector funds had better performance than the market except infrastructure funds. Bawa and Brar (2011) identified a few selected growth mutual funds schemes of both public sector and private sector schemes during the period 1st April 2000 to 31st March 2010 to evaluate their performance. The study concluded that the returns of private sector growth schemes had been better than public sector growth schemes. Mannar (2012) conducted a study to evaluate the performance of the four equity funds during the period from 2002 - 03 to 2011-12. Two funds were selected each from the fund houses, HDFC and ICICI Prudential. The funds selected are HDFC Top 200 (G), HDFC Capital Builder (G), ICICI Prudential Top 200 (G) and ICICI Prudential Top 200 (G). The study identified that the average performance of the HDFC top 200 scheme had been far inferior by a large factor when compared to the other schemes under study. The Performance of all the funds was to an extent better than the market with only a few rare exceptions. Inder (2012), attempted to examine the performance of index funds in comparison to market index. The study showed that index funds had been replica of the market index as they always try to capture the market sentiment.

3.2. INVESTMENT BEHAVIOURS OF MUTUAL FUND INVESTORS'

The researcher also tried to analyse a few of the studies that has been focused on the investment behaviour of mutual fund investors. Rehman, Shaikh and Kalkundrika (2011) in their study highlighted that investment decisions on mutual funds and behaviors of retail investors had based on various demographic factors like age, gender, marital status, level of market knowledge, educational qualification of retails investors and the number of dependents. Devasenathipathi, Saleendran and Shanmugasundaram (2007) in their study disclosed that 30% of the respondents in the sample group of 200 had awareness of mutual funds through consultant's advisory services, 46% respondents in the age group of 25-35 years had a lot of interest and more investments in mutual funds and 31% of the respondents had maintained mutual fund investments to meet future expenses. The study also unfolded that dividend had been the most preferred investment option for the respondents and 49% of the respondents had preferred to invest in equity fund other than the debt and balanced fund. Shanmugsundaram and Balakrishnan (2011) analyzed the investor behaviour on result announcement. It was concluded that when the result announced by the company were better than expected, 38% of the respondents desired to invest more and 40% of the respondent desired to hold the securities and 22% of investor wished to book the profit. Research further concluded that maximum number of respondent fell in the age of 21-30 years category out of which 75% of the respondents fell in the income level of below Rs.3,50,000 and 50% of the respondent were below the income level of Rs.1,50,000. Singh, and Chander (2003), identified that estimation of risk and return, portfolio selection and NAV are important criteria for mutual fund appraisal. The ANOVA results concluded that occupational status and age had immaterial influence on the choice of scheme. The important factors in the selection of schemes for salaried and retired investors were attributed to the past track record, safety and future growth prospects. Investors also expected prompt service, reliable information and also repurchase facility from the companies. Majority of retail investors were still reluctant towards mutual fund investments (Parihar, Sharma and Parihar, 2009). Rekha (2012) observed that even though there are positive factors contributing in the growth of the industry, there are a few factors inhibiting its growth which has been endorsed to low levels of customer awareness and lack of knowledge about mutual funds, limited innovation in product offerings, unwillingness to undertake even minimum risk, inaccessibility in smaller towns and cities due to lack of efficient distribution network and abysmal financial literacy. Grubber (1996) studied the performance of mutual funds and concluded that there had been a negative performance when compared to the market. He put forward even evidence of persistence of underperformance. He further concluded that in spite of inferior performance of actively managed portfolios there had been a fast growth of mutual funds industry in India. Singh (2012) argued that most of the respondents had no knowledge about the various function of mutual funds. He further argued that demographic factors, gender, income and level of education had significantly influenced the investors' attitude towards mutual funds. However, two demographic factors namely age and occupation have not been found influencing the attitude of investors' towards mutual funds. As far as the benefits provided by mutual funds are concerned, return potential and liquidity have been perceived to be most attractive by the invertors' followed by flexibility, transparency and affordability. Raju (2013) concluded that majority of dimensions had been influenced by 'stimulating factor' which indicated that the investor were under a strong influence in mutual fund investment. More specifically, it was revealed that financial advisor/ agents had been the major influencing forces over investors towards mutual funds. In fact they were the major inspiration as well as guiding factors in promotion of mutual fund business. Though the other agents like, advertisement through media, friends and relatives were also influencing the decisions of investors towards mutual fund investments, yet the financial advisor/agents influence were much more.

4. CONCLUSIONS

Indian Mutual fund industry is gradually moving towards growing phase. It is found that stock market crash, liquidity crunch in the markets, high competitions among the private and public players in the industry etc have affected the performance of the mutual funds. Despite of the fact, there have been positive returns generated by mutual funds investments. Most of the funds in the market provided the returns equal to risk free rate. Moreover, over the last few years level of awareness and interest of investors on mutual funds has increased. But level of awareness has not yet reached to mass investors. The past studies have shown that retail investors are still confused about the mutual funds and have refrained themselves from considering mutual funds as an investment avenue. In order to attain sustained profitable growth, the industry should focus on developing distribution networks, increasing retail participation and expanding the reach of mutual funds into rural areas by conducting awareness programs and extending financial literacy (Rekha 2012). Investment decision of retail investors in mutual funds can be encouraged by introducing special investment schemes and providing many offers or attractive prices (Mathivannan and Selvakumar, 2011). Chary and Masood (2010-2011) suggested that SEBI has to inculcate the culture of mutual fund investment in the minds of the investors and even focused that asset managers should develop the forecasting skills in order to manage the portfolio of the fund effectively. There is an urgent need to streamline the regulation of mutual fund industry. Capital market itself is a complex activity regulated by SEBI. So, a separate regulatory body to regulate the operation and management of mutual funds should be set up (Pandey, Rathore and Khare, 2007). There is also a need of strong transparency and disclosure policies, customer involvement, wider approach to cover Tier 2 and Tier 3 cities, up gradation of technology, innovation in products, customer satisfaction and strategies to bring more confidence among investors (Gupta 2011).

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