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Emerging trends and future of mutual fund industry in India

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ABSTRACT

Put your money in trust, not trust in money' attracts the small investors who are risk neutral or risk averse. Small investors prefer some kind of collective investment vehicle which can pool their managerial resources, invest it in securities and distribute returns among them on cooperative principles. This led to the growth of mutual fund industry in developed and developing capital market. The mutual fund industry in India, which is a little over three decades old, has undergone a sea change since the introduction of mutual fund regulations in 1993.This research paper covers various aspects of mutual funds industry in India, Starting with the basic concept of mutual fund, it throws light on the growth of Indian mutual fund industry and its present status, the different types of mutual funds based on structure, investment and special schemes, performance, problems and future of mutual funds industry in India.

Introduction

A small investor is afraid of entering into the securities market because of his limited resources, absence of relevant information and lack of portfolio managerial skill. However, he wishes to invest his money in securities. 'Put your in trust, not trust in money' attracts the small investors who are risk neutral or risk averse. Small investors prefer some kind of collective investment vehicle which can pool their marginal resources. Invest it in securities and distribute returns among them on corporate principles. This led to the growth of mutual fund industry both in the developed and developing capital market.

Origin of mutual funds in India:

The concept of mutual funds in India is not very old. It is a new feather in the cap of Indian capital market. It only showed up in sixties after a century old history elsewhere in the world. Reacting to the needs for a more active mobilization of household savings to provide investible resources to industry, the idea of first mutual fund in India was born out of the far-sighted vision of Sri. T. Krishnamachari , the then finance minister. H e wrote to then Prime Minister Pandit Jawarhar Lal Nehru outlining the need for an institution which would serve as conduit for these resources to the Indian capital market and RBI was entrusted to create this special institution. The idea of mutual began to take shape in India in 1963 with the set-up and enactment of Unit Trust of India when the UTI Act 1963 was framed to operate both as a financial institution and an investment trust.

Meaning of a mutual fund:

A mutual fund is a special type of institution, a trust or investment company which acts as an investment intermediary and channelizes the savings of large number of people in the corporate securities in such a way that investors get steady returns, capital appreciation and a low risTYPES OF MUTUAL FUNDS

A mutual fund can have several 'funds' under its management. These different funds can be categorized by structure, investment objective and others. The following flow chart will illustrate it.

Types of mutual funds

A. Structure	B .Investment Objective	C. Others
Open ended Fund	Growth Funds	Tax Saving Funds
Close ended Fund	Income Funds Exchange	Traded Funds
Internal Fund	Balanced Funds	Index Funds
	Money Market Funds	Sector Specific Funds

Review of Related Literature

A brief account of research works published in books, financial dailies, magazines and research journals explaining the concepts of mutual funds, its significance, features, schemes, methods of finding out a mutual prospects, how to select a scheme etc., are cited below.

Gupta Amitab (2000) identified that the IMFI had come a long way since its inception in 1964. The transformation in the previous decade was the outcome of policy initiatives taken by the Government of India to break the monolithic structure of the industry in 1987 by permitting public sector banks and insurance sectors to enter the market.

Ramesh Chander (2000) examined 34 mutual fund schemes with reference to the three fund characteristics with 91days treasury bills rated as risk –free investment from January 1994-December 1997. Returns based on NAV of many schemes were superior and highly volatile as compared to BSE SENSEX. Open-ended schemes out performed the close –end schemes in terms of return. Income funds outsmarted growth and balanced funds. Banks and UTI sponsored schemes performed fairly well in relation to sponsorship. The study revealed the poor market timing ability of mutual fund investment. The researcher also identified that twelve factors explained the majority of total variance in portfolio management practices.

Agrawal , Ashok Motilal (2000) opined that mutual funds had made a remarkable progress during 1987-95. The

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cumulative investible funds of the mutual funds industry recorded a sky-rocketing growth since 1987 and reached Rs.8059 crores by December 31,1995 from Rs.4564 crores during 1986-87

Gupta Amitabh (2001) evaluated the performance of 73 selected schemes with different investment objectives, both from the public and private sector using Market Index and Fundex. NAV of both close-end and open-end schemes from April 1994 to March 1999 were tested. The sample schemes were not adequately diversified. Risk and return of schemes were not in conformity with their objectives and there were no evidence of market timing abilities of mutual fund industry in India.

Roshni Jayam's (2002) study brought out that equities had a good chance of appreciation in future. The researcher was of the view that investors should correctly judge their investment objective and risk appetite before picking schemes, diversified equity funds were typically safer than others and the index funds were the best when market movements were not certain. The researcher suggested systematic withdrawal plan with growth option was more suitable for investors in need of regular cash inflows.

Bansa Manish's (2003) survey revealed that the percentage of investors holding only UTI schemes reduced. The unit holders' loyalty seemed to have become a myth as investors' were looking for performance.

Singh, Jaspal and Subhash Chander (2003) identified that past record and growth prospects influenced the choice of scheme. Investors in mutual funds expected repurchase facility, prompt service and adequate information. Return, portfolio selection and NAV were important criteria for the appraisal of mutual fund. The study indicated that occupational status, age had insignificant influence on the choice of scheme.

Venkateshwaralu M (2004) had analysed investors from the twin cities of Hyderabad and Secunderbad. Investors preferred to invest in open-end schemes with growth objectives. The study revealed that the size of income class is independent of preference pattern and dependent on the choice of fund floating institution. Reasonable returns and long-term strategy adopted by the scheme were the criteria of scheme selection. Investors perceived that too many restrictions led to the average performance of mutual funds in India.

Sondhi H J and Jain P K (2005) examined 17 public and 19 private sector mutual fund equity schemes.The study revealed that majority of the sample schemes earned better returns better than the market. Private equity schemes had superior performance due to their popularity, fund management practices, well- researched stock selection and timing skills. More than ¾ of public sector schemes were unable to achieve better returns in spite of higher investor confidence associated with high safety. The funds did not show consistency in performance.

Muthappan P K and Damodharan K (2006) evaluated 40 schemes for the period April 1995 to March 2000. The study identified that majority of the schemes earned returns higher than the market but lower than 91 days Treasury bill rate. The average risk of schemes was higher than the market. The risk and return of the schemes were not always in conformity with their stated investment objectives. The sample schemes were not adequately diversified. The study concludes that the Indian Mutual funds were not properly diversified.

Sanjay Kant Khare (2007) opined that investors could purchase stocks or bonds with much lower trading costs through mutual funds and enjoy the advantages of diversification and lower risk. The researcher identified that, with a higher savings rate of 23%,channelizing savings into mutual funds sector has been growing rapidly as retail.

Statement Of The Problem

With liberalization, the Indian industrial sector wants cheaper funds to face global competition. Banking intermediaries today cannot afford to reduce their margins but household sector demands better returns. All these factors have spawned the success of a new intermediary called mutual funds. The mutual fund industry in India, which is a little over three decades old, has undergone a sea change since the introduction of mutual fund regulations in 1993. It was in this year that private and foreign mutual funds started participating in the industry. Today, the industry consists of the UTI, mutual funds sponsored by public sector banks, insurance corporations and those set up by private and foreign funds. The entry of private sector mutual funds has imparted competitive efficiency in the industry, helped investors to choose from funds with different maturity periods and offered different risk-return trade-offs. Hence, there arises a need for studying the growth, performance and problems of mutual funds in India.

Objectives of the study:

The study was planned with the following objectives:

- To study the growth of mutual funds industry in India
- To study the performance of mutual funds in India
- To study the problems of mutual funds in India.
- To study the future of Indian mutual fund industry
- To suggest measures for the satisfactory performance of mutual funds in India.

Methodology of study

For methodology, an extensive literature review of secondary data from the reputed published sources like Economic survey, various books and websites on internet was carried out.

Data Analysis And Interpretation:

To Study The Growth of Mutual Funds Industry In India

Table 1 summarizes the growth of the mutual fund industry. Overall assets under management grew from Rs.102831 crore to Rs.143688 crore in 2004 or 5.1 percent of GDP. A striking feature of this growth was the success of the private sector which had an increase from 42.9% of assets in this period

Table 1. Growth of Mutual Fund Industry In India

(Rs.crores)

YEAR	ASSETS	PRIVATE MF's	PRIVATE SHARE
April 2002	1, 02,831	44,145	42.9
April 2003	89,238	65,398	73.9
March 2004	1, 43,688	1, 11,492	77.6

Source: Economic Survey 2003-2004

Table 2. Assets under management of mutual funds

(Rs. Crore)

	At end of year		
TYPE OF MF	**2002**	**2003**	**2004**
Money Market	10,801	32,424	59,447
Gilt	4,316	6,917	4,876
Income	77,469	71,258	47,451
Growth	14,371	22,938	31,551
Balanced	14,164	4,663	5,472
ELSS	1479	1893	1,740
	1,22,000	1,40,093	1,50,537

Economic Survey; 2004-2005, p-80

The mutual fund industry has experienced slow growth in recent years. With assets under management nearly stagnant at

Rs.1, 50,537 crores. The above table depicts that the bulk of mutual funder assets continue to be in debt securities. However, assets in growth funds rose sharply in 2004 to reach Rs.31,551 crore. The reason can be associated with India becoming a retail market where house holds directly own the bulk of securities. The assets under management of the mutual funds industry as on 31st March 2005 stood at Rs.1,49,554 crore as against Rs.1,39,616 crore a year ago, an increase of 7.2% over the year and was expected to grow further to touch Rs. 195000 crore by August end recording a nearly 26% growth on a year on year basis. The big jump in the assets under management in the recent months can be attributed to the increase in number of new diversified equity schmes and marketing efforts put by MFs issuing companies

Table 3. Investments By Mutual Funds

(Rs.in crores)

	Equality	Debt
MFs	448	16987
FIIs	44123	1759

Source: SEBI Annual Report 2004-2005

The above table shows that investment by mutual funds in Indian equities is only 1% of what foreign institutional investors have invested. According to the SEBI annual report for 2004-2005, FIIs invested Rs.44123 crore in the Indian market, mutual funds increased merely Rs.448 crore.However, the net investments by mutual funds in debt at Rs.16,987 crore was much higher than that by FII at Rs.1759 crore. The net resource mobilization by mutual funds declined by 95.3% to Rs.2200 crore in 2004-2005 as compared with Rs.46808 crore in the previous year

Table 4. Number of Mutual Fund Schemes As On 31st March 2005

Nature of scheme	Number
Income/debt oriented	227
Growth/Equity oriented	188
Balanced	35
Total	450

The above table depicts that there were 450 mutual fund schemes as on 31st March 2005 of which 227 were income/debt oriented schemes, 188 were growth /equity oriented schemes and the remaining 35 were balanced schemes.

Table 5. Changing Fund Preferences

Percentage of assets				
Year	**Equity funds**	**Debt funds**	**Mixed funds**	**Money market/ Liquid funds**
1990	21.19	54.17	27.70	0
1993	43.88	29.91	26.62	0
1996	18.02	39.67	39.91	0
1999	21.92	48.37	25.29	2.17

Source: The Economic Times, January 3, 2000

The above table depicts the changing fund preferences of mutual funds. It is evident that market preferences keep changing every few years.

To Study the Performance of Mutual Fund Industry In India

The above table shows that gross resource mobilization by mutual funds during 2001-2002 amounted to Rs.1,03,666 crore compared with Rs.59,430 crore during the previous year 2000-2001.Private sector mutual funds accounted for 89.2 % of the total resource mobilization during April-December 2001, compared to 80% in the previous year. The public sector mutual funds accounted for 7.1% while UTI accounted 3.7% during this period. Thus, it can be concluded that mutual funds have emerged as an important segment of financial markets in India.

Table 6. Gross Resource Mobilisation By Mutual Funds

(Rs in crores)

Item	**Private sector**	**Public sector**	**UTI**	**Total**
Gross inflow				
1998-1999	7,847	1,671	13,193	22,711
1999-2000	43,726	3,817	13,698	61,241
2000-2001	75,000	5,535	12,413	92,957
April-December				
2000-2001	47,550	3,110	8,790	59,430
2001-2002	92,461	7,346	3,858	1,03,666
Redemption				
1998-1999	6,394	1,336	15,930	23,660
1999-2000	28,559	4,562	9,150	42,271
2000-2001	65,160	6,580	12,090	83,829
April-December				
2000-2001	39,360	4,970	9,310	53,640
2001-2002	78,150	5,471	9,009	92,632
Net Inflow				
1998-1999	1,452	335	2,737	-949
1999-2000	15,167	-745	4,548	18,970
2000-2001	9,849	1,645	323	9,128
April-December				
2000-2001	8,190	1,530	480	7,050
2001-2002	14,311	1,874	-5,151	11,033

Table 7. Trends in resource mobilisation (net) by mutual funds

(Crore)

Sector	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011*
UTI	7,326	10,677	-3659	15,653	-5237
PUBLIC	7,621	9,820	9380	12,499	-2956
PRIVATE	79,038	1,33,304	-34,018	54,928	20,378
TOTAL	93,985	1,53,802	-28,296	83,080	12,185

Source: SEBI Note: *As on 30th November , 2010

It may be observed from the Table 2 indicates that during 2010-2011 (as in November 2010), mutual funds mobilized Rs.12,185 crore from the market as compared to Rs,83,080 crore in 2009-2010. The market value of assets under management stood at Rs.6,65,282 crore as on November 2010 as compared to Rs.6,13,979 crore as on 31st March 2010, showing an increase of 8.5 percent

To study the problems of mutual funds in India

The following are some of the main problems that are being faced by Indian Mutual Funds

1. **Liquidity Crisis**: Mutual Funds in India face liquidity problems. Investors are not able to draw back from some of the schemes. There is no exit route."Bad delivery " has caused a lot of problems and liquidity crisis for the mutual funds.
2. **Lack of Innovation**: Mutual funds in India have not been able to provide innovative schemes in terms of risk, liquidity and choice of the investors.
3. **Inadequate Research**: Most of the mutual funds in India are suffering due to inadequate research facilities. Most of the funds depend upon external research and have no facilities for in-house research. They should provide more money on the research and development if they want to be successful in future.
4. **Conventional Pattern of Investment**: Mutual funds in India have been following conservative pattern of investment. They

have not been able to diversify the risk to a larger extent, which has caused low return on investments.

5**. No Provision for Performance Guarantee**: Mutual funds in India have so far failed to provide performance guarantee to the investors. In some cases, there has been erosion of capital.

6. **Inadequate Disclosures**: There have not been adequate and timely disclosures of material information to the investors by the mutual funds in India.

7. **Delays In Services**: Mutual funds in India have also not been able to provide quick and adequate service to the investors. In many cases, there is no response to the investor's grievances.

8. No Rural Sector Investment Base: Indian mutual funds, so far, have not been able to create rural sector investment base. Sufficient efforts have not been made to educate the potential investors. Mutual funds should launch investor's education programmer and expand their activities in rural areas.

9. Poor Risk Management: About 50% of the mutual funds are not managing properly and another 50% do not have documented risk procedures or dedicated risk managers.

To study the future of Indian mutual fund industry

In spite of the above bottlenecks, the mutual fund industry is having a good prospect in our country. I t is likely to show a good progress in the coming years due to a variety of factors.

(I) SEBI is lending its full support for the promotion of the mutual fund industry directly as well as indirectly.

(II) Ever since the disbanding of the Controller of Capital Issues Office, many companies have entered into the market with a petty premium on their shares. Naturally, the small investors find them out of reach. Hence, they have to seek the blessings of the mutual fund industry. One can easily subscribe to mutual funds shares at par with one's little investment.

(Iii) In recent times, the interest rates on bank deposits have been declining. The household savers are looking for alternative avenues which could bring higher returns. The returns on the mutual fund schemes compare favorably with the returns on bank deposits.

(IV) The trend of rising PE ratio, the entry of large domestic institutional investors, the opening of the market to the foreign investors etc., would make stock market inaccessible to the small investors. Hence, they have to necessarily go to the mutual fund industry.

(V) Mutual Fund provides a wider range of products so as to meet the diverse needs of the investing public. The investors have a good choice to meet their different expectations like security, growth and liquidity.

(vi) The Government has also given the necessary impetus by providing tax concessions and tax exemptions. When the mutual fund industry is receiving a preferential treatment at the hands of the Government, it is bound to grow in future

(vii) The Department of Company Affairs has agreed to amend the companies Act to grant voting rights to companies for mutual funds.

(VIII) Mutual Funds have been permitted to underwrite shares also.

(IX) The Union Budget 1999-2000 contains many measures to encourage the mutual fund industry.

All these factors would go a long way in making mutual funds as increasingly popular, lucrative and cost efficient vehicle for investment. If mutual funds ensure good returns, quick liquidity and safety and create a good rapport with the investors, their future will be very bright

To suggest measures for satisfactory performance of mutual funds in India

As the mutual fund has entered the capital market, growing profitable enough to attract competition

Into this cherished territory encouraging competition among all the mutual fund operators, there is need to take some strategy to bring more confidence among investors for which mutual would be able to project the image successfully. The following are some of the suggestions.

(I) As the investors are unwilling to invest in mutual fund unless a minimum return is guaranteed, it is very essential to create in the mind of investors that mutual funds are market instruments and associated with market risk, hence , mutual funds could not offer guaranteed income.

(II) Growth of mutual fund tends to increase the share holdings in good companies give rise the fear of destabilizing among industrial group, hence, introduction of non-voting shares and lowering the debt-equity ratio help to remove these apprehensions.

(iii) Steps should be taken for funds to make fair and truthful disclosures of information to the investors so that subscribers know what risk they are taking by investing in fund.

(iv) Mutual funds are made by investors and investors' interest ought to be paramount by setting standard of behaviors and efficiency through self-regulations and professionalism.

(v) Mutual funds should develop product structuring to tap target customers

(VI) Mutual fund should communicate to the investors about their organization and operation.

(vii) Internet and thereby e-commerce which is inevitable now-a –days has to be introduced in mutual funds.

(ix) Proper marketing and distribution system should be developed by mutual funds

(x) Well-informed institutional market must be developed to remove market inefficiencies

(xi) Mutual funds must make efforts in investor awareness programme which is the need of the day.

Conclusion

It can be concluded that despite all the advantages linked with mutual funds, people still prefer to invest their money independently. So far mutual funds have not been able to introduce the schemes which are suitable to the needs of farmers, small entrepreneurs and merchants to tap the rural savings. Further, mutual have not yet developed product structuring to tap target customers. There is a lack of product conceptualization and innovation. Weak distribution and marketing channels are another problem which the mutual fund industry is facing today. The merchant banking industry is not sufficiently matured and this has led to the slow development of mutual fund industry. The interesting thing is that mutual funds are the most misunderstood financial products in India. Mutual fund industries are also not making efforts in investor awareness programmes which are the need of the day.

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