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## AN OVERVIEW OF MUTUAL FUNDS

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### ABSTRACT

This paper focus on the entire concepts of mutual funds industry in India. A mutual fund, also called an investment company, is an investment vehicle which pools the money of many investors. Three Boston executives in 1924 pooled their money with no idea of how popular the assemblage would become. The formation of Unit Trust of Bank of India, 1963 along with the inventiveness of Government of India. Its huge corpus enables diversification, thereby minimizing the risks and maximizing the returns. The fund's manager uses the money collected to purchase securities such as stock and bonds. The securities purchased are referred to as the fund's portfolio. This study was conducted to analyse and compare the performance of different types of mutual funds in India and concluded that equity funds outperform income funds. This study further concludes that equity fund managers possess significant market timing ability and institutions funds manager are able to time their investments, but brokers operated funds did not show market timing ability. Further, it has been found empirically that fund managers are able to time their investments with the conditions in the market, and possesses significant timing ability.

**Key words:** Mutual Fund Industry, India, Equity Fund, Money Market, Mutual Fund, Return, Risk, Diversification etc.

### 1. INTRODUCTION

Mutual fund is an investment company that pools money from shareholders and invests in a variety of securities, such as stocks, bonds and money market instruments. Most open-end Mutual funds continuously offer new shares to investors. Mutual funds invest pooled cash of many investors to meet the fund's stated investment objective. Mutual funds stand ready to sell and redeem their shares at any time at the fund's current net asset value that is total fund assets divided by shares outstanding.

In other words, a mutual fund is a managed group of owned securities of several corporations. These corporations receive dividends on the shares that they hold and realize capital gains or losses on their securities traded. Investors purchase shares in the mutual fund as if it was an individual security. After paying operating costs, the earnings of mutual fund are distributed to the investors, in proportion to the amount of money invested. Investors hope that a loss on one holding will be made up by a gain on another. Heeding the adage "Don't put all your eggs in one basket" the holders of mutual funds shares are able collectively to gain the advantage by diversifying their investments, which might be beyond their financial means individually.

## 2. OBJECTIVE

1. To understand the concept of mutual funds.
2. To study the risks of investing in Mutual Funds.
3. To analyse growth and development of mutual fund in India.

## 3. REVIEW OF LITERATURE

**Dr. Singh B K (2012)** detailed about the mutual fund operation, NAV calculation and further several demographic factors of investors towards their attitude of investment have also been considered. Chi-square test has been deployed in order to gain conclusion. Dr. Vyas R. (2012) prospected that although financial markets have turned to be expensive but different financial instrument which are introduced, require unification. Author researched about factors affecting investors for investing in mutual fund. Research highlighted that mostly investors choose bank and post office deposits as one of the investment avenues, in comparison to Mutual Fund. Equity and SIP are among the priority list. Prabhavathi Y .et al (2013) focused on understanding about the attitude, awareness and preferences of mutual fund investors. They found that mostly SIPs have been preferred and moreover, Mutual Fund is a choice of several because of better returns as well as professional fund management. Solanki A. (2016) compared the performance of selected Reliance equity schemes from the time period of 1<sup>st</sup> April 2007 to 31<sup>st</sup> March 2016 with BSE National 100 and SENSEX returns. The study concluded that the selected schemes had higher returns than the Benchmark Index. But the study considered only the open ended schemes with only growth options undertaken. Prof Prabhu G. et al (2016) believed that Mutual Fund Industry in India is at rapid growth rate. It is considered that Mutual Fund investments are less risky in comparison to investments in other securities. But it has been inferred from the study that still several investors have not been aware about the benefits of investing in Mutual Funds.

**Gayathai, S., Karthika, S. & Kumar, Gajendran L. (2010)** reviewed on Mutual Fund in India are financial instrument. A mutual fund is not an alternative investment option to stock and bonds; rather it pools the money of several investors and invests this in stocks, bonds, money market instruments and other types of securities. The owner of a mutual fund unit gets a proportional share of the fund's gains, losses, income and expenses. Mutual Fund is vehicle for investment in stocks and Bonds. Each mutual fund has a specific stated objective. The fund's objective is laid out in the fund's prospectus, which is the legal document that contains information about the fund, its history, its officers and its performance. Some popular objectives of a mutual fund are: Fund objective – what the fund will invest in; Equity (Growth) – only in stocks; Debt (Income); only in fixed-income securities; Money Market (including Gilt) – In short term money market instruments (including government securities); Balanced – Partly in stocks and partly in fixed-income securities, in order to maintain a 'balance' in returns and risk. The share value of the Mutual Funds in Indian is known as net asset value per share (NAV). The NAV is calculated on the total amount of the Mutual Funds in India, by dividing it with the number of shares issued and outstanding shares on daily basis. The company that puts together a mutual fund is called an AMC. An AMC may have several mutual fund schemes with similar or varied investment objectives. The AMC hires a professional money manager, who buys and sells securities in line with the fund's stated objective. The Securities and Exchange Board of India (SEBI) mutual fund regulations require that the fund's objectives are clearly spelt out in the prospectus. In addition, every mutual fund has a board of directors that is supposed to represent the shareholders' interests, rather than the AMC's.

## 4. HISTORY OF MUTUAL FUNDS

The modern mutual funds were first introduced in Belgium in 1822. This form of investment soon spread to Great Britain and France. Mutual funds become popular in the United States in the 1920s and continue to be popular since the 1930s, especially open-end mutual funds experienced a period of tremendous growth after World War II, especially in the 1980s and 1990s. LIC established its mutual fund in June 1989 which GIC had set up its mutual fund in December 1990. With the entry of private sector funds in 1993, a new era started in the Indian mutual fund industry, giving the Indian investors a wider choice of fund families. Also, 1993 was the year in which the first Mutual Fund Regulations came into being, under which all mutual funds, except UTI were to be registered and governed. The erstwhile Kothari Pioneer was the first private sector mutual fund registered in July 1993. The number of mutual fund houses went on increasing, with many foreign mutual funds

setting up funds in India and also the Industry has witnessed several mergers and acquisitions. As at the end of January 2003, there were 33 mutual funds with total assets of Rs. 1,21,805 crores. The Unit Trust of India with Rs. 44,451 crores of assets under management was way ahead of other mutual funds. In February 2003, following the repeal of the Unit Trust of India with assets under management of Rs. 29,835 crores as at the end of January 2003, representing broadly, the assets of US 64 scheme, assured return and certain other schemes. The Specified Undertaking of Unit Trust of India, functioning under an administrator and under the rules framed by Government of India and does not come under the purview of the Mutual Fund Regulations.

## 5. STRUCTURE OF A MUTUAL FUND

A common question that a lot of investors do have is what guarantee they have that their money is safe and that the mutual fund will be solvent enough to pay the money back. There are no guarantees but the mutual fund structure is designed to address these issues. Actually, there are five levels of checks on mutual

- The highest level of checks on mutual funds comes from the super-regulator which is SEBI. Not just the operations of the fund but the announcements, corporate governance standards and the protection of investor interest are all regulated by
- Every mutual fund has to necessarily have a Board of Trustees. These trustees will represent the interests of the unit holders and will have to be from outside the fund. Normally, these are very eminent people with a reputation for integrity and fairness. This is the second level of
- Then there is the Asset Management Company consisting of the CEO, CIO, Fund managers, dealers who actually manage the fund. The fund evaluation is based on how best the fund performs and enhances the wealth for shareholders. The reputational stake for the sponsor is too high and that also acts as an automatic
- Finally, the competition and the investor sentiments also act as a natural balance. Investors are quick to think with their feet and no fund can afford to think with their feet and no fund can afford to take such a risk. Thus there are multiple levels of direct and indirect checks and balances for mutual funds.

## 6. MUTUAL FUND PROCESS WORK

It is interesting to understand the complete cycle of how mutual funds mutual from money to wealth and back to money. Here is the four-step process.

- The first role the mutual fund plays are to pool savings of small investors. Small investors with lump sum amounts of as small as Rs. 5000 and SIP outlays of just Rs. 500 can come together and put their money in a mutual
- The mutual fund translates these savings into investments. This is a very interesting and iterative process. What the fund does is to put the money in to productive avenues like equity where the funds can actually create worthwhile wealth for you. What you require is solid equity investments which mutual funds.
- Once the funds are invested, the mutual fund generates returns in the form of dividends, interest, rights, bonuses, splits, trading gains, investment gains etc. These gains are either paid out to the investor as dividends or ploughed back into the funds as wealth accretion. The choice is entirely
- The last step actually completes the mutual fund cycle. Once the funds are invested and the gains are distributed, there are two things that the investor will do. For example, if the fund has performed very well then the investor fund has performed very well then the investor has an incentive to plough back the profits into the same fund. These are called growth plans. That is how wealth creation actually happens, the corpus is continuously reinvested and the wealth compounds over a period of time. It is this cycle that makes equity funds veritable wealth creators over longer periods of time.
- Mutual funds, especially equity funds, play a very important in channelizing small savings of millions of individuals into productive equities. That is what makes them a unique product for continuous wealth creation.

## 7. TYPES OF MUTUAL FUNDS IN INDIA

As per SEBI, mutual funds can be broadly classified into 3 categories – Equity Funds, Debt Funds and Hybrid Funds.

**Equity Funds:** - An equity fund is a mutual fund in mutual fund which invests a minimum of 65% of its assets in equity and equity related instruments. It can invest the balance 0%-35% in debt or money market securities. Equity funds are capable of giving relatively high returns as they primarily invest in stocks of companies which are responsive to changes in the stock market and the economy.

**Debt Funds:** - A debt fund is a mutual fund which invests a majority of its assets in debt and money market securities. According to the Income Tax Act, a mutual fund which invests less than 65% of its total assets in equities is termed as a debt fund. Debt funds are preferred by investors mainly because they come with relatively lower levels of risk.

**Hybrid Funds:** - As the name suggests, a hybrid fund is a mutual fund which invests its assets in two or more asset classes including equities, debt, money market instruments, gold, overseas securities, etc. A hybrid fund generally invests in only two asset classes namely equity and debt, money market instruments, gold, overseas securities, etc.

## 8. GROWTH AND DEVELOPMENT OF MUTUAL FUNDS IN INDIA

The Mutual Funds industry that started its journey in the country in 1963 has turned as one of the important constituents of the financial sector. The industry has witnessed sufficient expansion and standardization in terms of products and services offered, regulatory mechanism, and the proliferation of large number of private sector funds both domestic and foreign. The fact is that the fund market in the country has graduated from offering plain vanilla equity and debt funds, to an array of diverse products such as Gold Funds (GF), Exchange Traded Funds (ETF's), and capital protection oriented funds and even the native funds (Fozia, 2013). Truly, the mutual fund industry in the country has come from long-way but the moot question is that whether it has realized its potential fully. In order to answer this question, we would need to critically analyse its growth. For this purpose, in the following Para's the growth that the mutual funds industry has achieved over a certain period of time has been analysed in respect of the following parameters:

- Number of funds
- Fund Schemes offered
- Mobilization of Funds
- Assets Under Management
- Household Savings mobilized
- Performance of AMCs in terms of earnings and profitability.

## 9. RISK ASSOCIATED WITH MUTUAL FUND

It is well said that Higher the Risk, Higher the Returns. Tolerance for risk varies from one individual to another. Hence individual disposition can be

- Conservative
- Aggressive
- Moderate

Following are techniques which would enable investor to manage the investment risk and attain the financial goals:

- Diversification

Investors must tend to diversify the portfolio that is a blend of equity shares, bonds and money market securities would definitely procure more returns rather than investing the entire amount of money into one basket. Moreover, making investments into high growth rate equity along with the high income bonds as well as stable money market would augment returns and moderate risk.

- Systematic Investment Plan

Unit Holders in order to diminish the risk, can also choose to invest specific amount periodically for some continuous interval. SIP lets invest fixed amount every month in order to buy additional units at NPV prices.

## 10. FUTURE PROSPECT OF MUTUAL FUNDS IN INDIA

- 100% growth in the last 6 years.
- Number of foreign AMC's are in the queue to enter the India markets like Fidelity Investments, US based, with over US\$1 trillion assets under management worldwide.
- Our saving rate is over 23%, highest in the world. Only channelizing these savings in mutual funds sector is required.
- We have approximately 29 mutual fund which is much less than US having more than 800. There is a big scope for expansion.
- Mutual fund can penetrate rural like the Indian insurance industry with simple and limited products.
- SEBI allowing the MF's to launch commodity mutual funds.
- Emphasis to curb the late trading practices.
- Introduction of Financial Planners who can provide need based advice.

## 11. FINDINGS

1. People employed in Private sectors and Businessman are more likely to invest in Mutual Funds, than other people working in other professions.
2. Generally, investors whose monthly income is above Rs. 20001-30000 are more likely to invest their income in Mutual Fund, to preserve their savings of at least more 20 %.
3. People generally like to save their savings in Mutual Funds, Fixed Deposits and savings Account.
4. The most popular medium of investing in Mutual Funds, is through sip and moreover people like to invest in Balanced Fund Investors more likely to hold Mutual Funds' investments for the period of 1 to 3 years and 4 to 6 years.
5. Investors more likely to invest in open-ended schemes of Mutual Fund.
6. Investor more likely to invest in growth schemes of Mutual Fund.

## 12. SUGGESTIONS

1. There should provide more awareness to the age group of 25-35 about Mutual Fund. Mutual Fund investment is subject to market risk so it is necessary to read all schemes related documents clearly by investors.
2. The duration of investment should be more than 6 years so that the return percentage will be higher.
3. Investment in Mutual Fund should be started from the age of 25-28 so the investor will get more return than expected.
4. Mutual Fund is the best platform to invest in the market with minimum risk and maximum return.
5. At the present scenario, the balanced scheme is best way to invest in Mutual Fund like SIP, MIP.

## 13. CONCLUSION

With the structural liberalisation policies no doubt India economy is likely to return to a high growth path in few years. Hence mutual fund organisations are needed to upgrade their skills and technology. Success of mutual fund however would bright be depending upon the implementation of suggestions. With regard to the Mutual Fund investor we are of the view that the investor needs to adopt two crucial skills for successful investing that is a sense of timing and investment discipline both need to be adopted at the same time. Investment in today's era is enveloped with risks like business, credit default, currency, interest rate, market etc. Mutual Fund allows investor to pool their money with which the investment manager would instigate investments and hence attempt to attain results as per the investor's objectives. Diversification and SIP allows investor to manage the risks. Sponsor, trustee, Transfer Agent, Asset Management Company etc. Forms key element Mutual Fund structure. Moreover, with the investment in Mutual Fund the investor can avail tax benefits too.

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