Comparative Study of Mutual Fund and Traditional investment

*Dr. Anurag Kumar Jha
Assistant Professor
Institute of Business Management , Darbhanga, Bihar

ABSTRACT

A Mutual Fund is a trust that pools the savings of a number of investors who allocate a common financial goal. The money thus collected is then invested in capital market instruments such as shares, debentures, government and other securities. The income earned through investments and the capital appreciation realised is shared by its unit holders in proportion to the number of units owned by them. Thus a Mutual Fund is the most suitable investment for the common man as it offers an opportunity to invest in a diversified, Multidimensional professionally managed basket of securities at a relatively low cost. The large amount of money collected by mutual funds from 2004 onwards indicates that they have emerged as an important savings vehicle of investors and with their war chests of money. they also became significant institutional investors in the capital market. The accelerated growth of mutual funds highlights a need for Comparative Analysis of Mutual Fund and Traditional Investment.

***Keyword**- Traditional Investment, capital Market Investment, Investor*

Introduction

Investors always look for safer investment avenues and want to maximize their returns in accordance with their risk tolerance. One tries to invest money as early as possible so that the money will grow accordingly in his lifetime. Choosing a wise investing option is very crucial because a balance is required to be maintained between the risks and returns involved. Return is motivating force and the principal reward in the investment process. One of the important reason that's why one needs to invest wisely is to meet the cost of inflation. Inflation is the rate at which the cost of living increases at that time. The cost of living is simply what it cost to buy the goods and services one needs to live. Inflation causes money to lose value because it will not buy the same amount of a goods or services in the future as it does now or did in the past. Savings, when not invested will gradually lose its value due to inflation or rise price level. Hence if a person saves, investment becomes a compulsion and not an option. Usually investors in a country like India prefer bank deposits and insurances as their favorite instruments of investments. The increasing awareness towards the structured products and financial literacy has drawn investors or Householders' attention towards mutual funds and equity markets. These draw our attention for comparison of resource mobilization towards these investment avenues and draw some conclusive remarks between Mutual Fund Investment and Traditional Investment.

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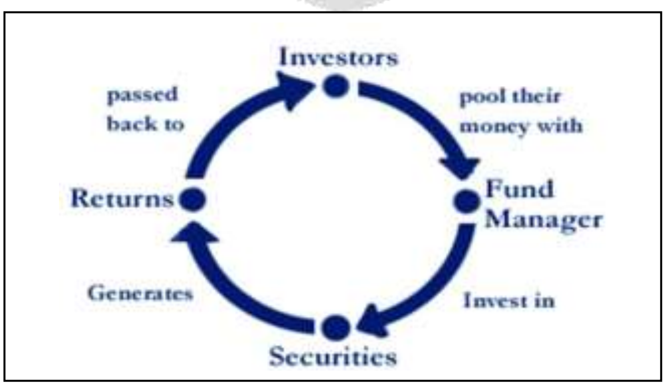

Literature Review

In the commercial history of Egyptians, it was stated that the shares were sold in vessels and caravans, in order to spread the risk of business ventures. After sometime, in 1822, an investment trust called ‘Society General de Belgique’ was formed in Belgium. The institution was formed by the royal family of Holland before the separation of Belgium and Holland. The institution has acquired securities in wide range of companies and practiced the precept of diversification. Later, the investment trust concept attracted many countries and considerable progress was made in Switzerland, a little in France, Germany and rest of the Europe.

The concept of investment trust gained momentum in Great Britain. The first investment trust, ‘The Foreign and Colonial Government Trust’ was founded in London in 1868. Later in 1873, the Scottish American Trust was established by Robert Fleming at Dundee. At that time, British bonds were selling foreign government bonds and were yielding a return ranging between five and six percent. The investors were impressed with the higher return on foreign bonds but were not ready to assume the risk of investing in one foreign investment. The Scottish Investment Trust was formed in order to diversify the risk. In England, the early institutions were created under a legal form, known as the OLD ENGLISH TRUST.

The persons who have acquired experience large trust estates were appointed as trustees, and capital was entrusted to them for purchasing securities. British investment trusts are successful and presently they are popular with unit trusts. The period 1925-29, witnessed a substantial expansion of investment trust movement in the US.

The banking houses promoted investment trusts to unload the unsaleable securities and to control the companies without investing substantial amounts of their own money. Every financial group started forming some sort of investment trusts. As there were hardly any rules and regulations, mismanagement in these institutions was wide spread. During the great depression of the 30s the investors had staggering losses from these trusts. In 1933, the US Congress directed the Securities and Exchange Commission (SEC) to investigate the operations of the American Investment Trusts. The SEC recommended the passage of legislation which materialized is 1940. The Investment Companies Act 1940 provides rules and regulations for the establishment and management of mutual funds.

The mutual fund industry has witnessed three interrelated stages of development in terms of entry of players.

1. **Phase I - 1964 – 1974**
2. **Phase-II- 1974- 1987**
3. **Phase III - 1987 - 1993**
4. **Phase IV - 1993 - 1996**
5. **Phase V - 1996 - 2004**
6. **Phase VI - 2004 onwards**

This period was marked by the operations of a single institution, UTI, which prepared ground for the future mutual fund industry.

The first decade of UTI’s operations (1964-74) was the formative period. The first, and still the most popular, product launched by UTI was unit 64. Due to the immense popularity of Unit 64, UTI launched a reinvestment plan in 1966-67. Another popular scheme, Unit linked insurance plan (ULIP), was launched in 1971. By the end of June 1974 there were 6lakh unit holders with UTI. The unit capital totalled Rs152 crore and investible funds Rs 172 crore.

The second phase of operations (1974-84) was one of consolidation and expansion. In this period UTI was declined from RBI. The period was marked by the introduction of openended growth funds. Six new schemes were introduced during 1981-84. By the end of June 1984, the investible funds crossed Rs 1000 crore and unit holders numbered to 17 lakh. During 1984-87, innovative and widely accepted schemes like Children’s Gift Growth Fund (1986) and Master share (1987) were launched. The first Indian offshore fund, India Fund, was launched in August 1986.

Third Phase Period (1984-1993) was marked by the entry of non-UTI public sector mutual funds in the market, bringing in competition. With the opening up of the economy many public sector financial institutions established mutual funds in India. However, the mutual funds industry remained the exclusive domain of public sector in this period. The first non-UTI mutual fund—SBI Mutual fund—was launched by the State bank of India in November 1987. This was followed by Canbank mutual Fund scheme (launched in December 1987), LIC Mutual

Fund Scheme (launched in June 1989) and Indian Bank Mutual Fund Scheme (launched in January 1990). The entry of public sector mutual funds created waves in the market and attracted small investors. The cumulative mobilization of resources went up from Rs 4563.68 crore in 1987 (mobilized by UTI alone) to Rs 19110.92 crore in 1990 (mobilized collectively by UTI, SBI mutual Fund, Canbank Mutual Fund, LIC Mutual Fund and Indian bank Mutual Fund)- 319 per cent increase.

Phase Fourth (1993 to 1996) Emergence of a Competitive Market (emergence of private sector funds) A new era in the mutual fund industry began with the entry of private sector funds in 1993, posing a serious competition to the existing public sector funds. The new private sector funds have distinctive operational advantages:

1. Most of them are jointly floated by Indian organizations along with experienced foreign asset management companies, facilitating access to the latest technology and foreign fund management strategies.
2. Private sector funds are able to attract the best managerial talents from the public sector.
3. Starting of mutual funds has been easier for them because infrastructural inputs created by the public sector mutual funds were already available.

The first private sector mutual fund to launch a scheme was the Madras based Kothari Pioneer Mutual Fund. It launched the open-ended Prima Fund in November 1993.

Phase Fifth (1996 to 2004) Growth and SEBI Regulations- The mutual fund industry witnessed robust growth and stricter regulation from the SEBI after the year 1996. The mobilization of funds and the number of players operating in the industry reached new heights as investors started showing more interest in mutual funds. Investors' interests were safeguarded by SEBI and the Government offered tax benefits to the investors in order to encourage them.

SEBI (Mutual Funds) Regulations, 1996 was introduced by SEBI that set uniform standards for all mutual funds in India. The Union Budget in 1999 exempted all dividend incomes in the hands of investors free from income tax. Various Investor Awareness Programmes were launched during this phase, both by SEBI and AMFI, with an objective to educate investors and make them informed about the mutual fund industry. In February 2003, the UTI Act was repealed and UTI was stripped of its Special legal status as a trust formed by an Act of Parliament. The primary objective behind this was to bring all mutual fund players on the same level.

Phase Sixth - 2004 Onwards (Growth and Consolidation) After the year 2003, during this phase, the flow of funds into the mutual funds industry considerably increased. This was due to tax benefits and improvement in quality of investor service which has resulted into a positive growth in the mutual fund industry in India. However, in the year 2003, due to the revocation of the Unit Trust of India Act, 1963, UTI was bifurcated into two separate entities. This Phase is known for division of UTI into separate entities. The phase had harsh experience for UTI. It was divided into two separate entities. One is the Specified Undertaking of the Unit Trust of India; running under the supervision and the rules framed by Government of India and does not come under the purview of the Mutual Fund Regulations.

Assets Under Management (**AUM**) of Indian **Mutual Fund** Industry as on July 31st , 2020 stood at ₹ 27,11,894 crore.

Friend, et al1 ., (1962) made an extensive and systematic study of 152 mutual funds found that mutual fund schemes earned an average annual return of 12.4 percent, while their composite benchmark earned a return of 12.6 percent. Their alpha was negative with 20 basis points. Overall results did not suggest widespread inefficiency in the industry. Comparison of fund returns with turnover and expense categories did not reveal a strong relationship.

Treynor and Mazuy (1966) are the first to investigate and present their findings of mutual fund managers' ability to time market returns, i.e. adjust the fund's exposure prior to market advances or declines. They stated that in the presence of market timing ability, the relationship between a fund's return and the market return is convex. This means that during times of positive market returns, funds ride along or increase systematic risk, whereas during down markets fund's decrease market exposure and outperform the market.

McDonald and John (1974) examined 123 mutual funds and identified the existence of positive relationship between objectives and risk. The study identified the existence of positive relationship between return and risk. The relationship between objective and risk-adjusted performance indicated that, more aggressive funds experienced better results.

Vidhyashankar S. (1990) identified a shift from bank or company deposits to mutual funds due to its superiority by way of ensuring a healthy and orderly development of capital market with adequate investor protection through SEBI interference. The study identified that mutual funds in the Indian capital market have a bright future as one of the predominant instruments of savings by the end of the century.

Vaid, Seema's (1994) study revealed that the industry showed a continuous growth in savings mobilization and the number of unit holders during the period 1987 to 1992. 58.40 percent of resources mobilized by the industry were through income schemes. UTI accounted for 83.90 percent of industry mobilization. Pure growth schemes displayed a sound investment pattern with 81.80 percent of portfolios in equity scrips and had identified that semi-urban and rural areas were not adequately tapped by the mutual funds inspite of satisfactory returns. Offshore funds showed best performance during 1985-86.

Rao, Mohana P. (1998) opined that, UTI followed by LIC Mutual Fund dominated the market with 54 and 15 schemes respectively. His interview with 120 respondents showed that, 96 percent invested in UTI due to better service and return. 50 percent of shareholding and 25 percent of unit-holding respondents were from metro cities. Investor's services, income–cum-growth option and capital appreciation were very important aspects while choosing a fund. He identified that the close-end schemes were very popular among investors and respondents in general expected private sector funds to improve the quality of services, investors' confidence besides reducing fraud and mismanagement.

Gupta Amitabh (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.

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's for mutual fund appraisal. The ANOVA results indicated that, occupational status; age had insignificant influence on the choice of scheme. Salaried and retired categories had priority for past record and safety in their mutual fund investment decisions.

Sondhi and Jain (2010) examined the market risk and investment performance of equity mutual funds in India. The study used a sample of 36 equity fund for a period of 3 years. The study examined whether high beta of funds have actually produced high returns over the study period. The study also examined that open-ended or close-ended categories, size of fund and the ownership pattern significantly affect risk-adjusted investment performance of equity fund. The results of the study confirmed with the empirical evidence produced by Fama (1992) that high beta funds (market risks) may not necessarily produce high returns. The study revealed that, the category, size and ownership have been significant determinants of the performance of mutual fund schemes.

Ayelen Banegas, Gabriel Montes-Rojas, Lucas Siga (2016) studied the link between monetary policy and mutual fund flows, and the potential risks to financial stability that might arise from such flows, from their study they found that monetary policy can have a direct influence on the allocation decisions of mutual fund investors.

CLASSIFICATION OF MUTUAL FUND SCHEMES

The mutual fund industry in the USA, the UK and Japan has achieved tremendous diversity in terms of innovative funds (schemes). The launching of innovative schemes in India has been rather slow due to the prevailing investment psychology and infra structural inadequacies. Mutual fund investors in India, who are largely from the upper-middle-class income group, are risk-averse and, as such, more interested in schemes with tolerable capital risk and returns over bank deposits. This has restricted innovation and launching of more risky products in the Indian market.

1. **Open-Ended Schemes** Though the first, and by far the most popular, mutual fund scheme,(Unit 64), is an open-ended scheme, open-ended schemes have not been very successful in India unlike the USA and UK. By the end of March 1996 the total schemes including UTI'S three venture funds numbered 194, out of which only 31 schemes were open-ended and the rest were close-ended. The exact data pertaining to the assets of open-ended and close-ended schemes is not readily available. However, some idea about the relative strength of open-ended and close-ended schemes can be drawn from the data compiled by UTI.
2. **Close-Ended Schemes** Close-ended schemes are more popular in India than open-ended schemes. As we have seen, of the 194 schemes as on 31 March 1996, 163 were close-ended. The popularity of close-ended

schemes is on account of two reasons. First, before the promulgation of SEBI regulations in 1993, public sector mutual funds came out with many close-ended income schemes with assured returns. Second due to the stock market boom during 1991-92, investors have preferred growth-oriented equity schemes.

OBJECTIVES OF THE STUDY

- To know the Mutual Fund Industry in general and India in particular.
- Comparative study of the returns provided by the individual Mutual Fund schemes and Traditional Investment.

STRUCTURE OF MUTUAL FUNDS IN INDIA

In developed countries like the UK and the USA the mutual fund industry is highly regulated with a view to impart operational transparency and protect investor’s interests. Since there is a clear distinction between open-ended schemes (mutual funds) and close-ended schemes, usually two different types of structural and management approaches are followed. Open-ended funds (unit trusts), in the UK follow the ‘trust approach’ while close-ended schemes (investments trust) follow the ‘corporate approach’. The management and operations of such funds are therefore guided by separate regulatory mechanisms, and rules are laid down by the separate controlling authorities. However, these distinctions are not followed in India and both the approaches, i.e., trust and corporate, have been integrated by the Indian regulatory authority, SEBI.

The formation and operations of mutual funds in India is solely guided by the securities and Exchange Board of India (Mutual Funds) Regulations, 1993 which came into force on January 1993. The regulations have since been replaced by the Securities and Exchange Board of India (Mutual Funds) Regulations 1996, through a notification on 9 December 1996. A mutual fund comprises four separate entities, namely sponsor, mutual fund trust, AMC and custodian. They are of course assisted by other independent administrative entities like banks, registrars and transfer agents

Advantages of Mutual Fund

Any investor investing in mutual fund can automatically reap the benefits of research and wider range of low cost information services. A risk-wavers investor can thus expect above the market returns at a lower cost and lower risk.

- **Tax Efficiency** -In general, investors pay tax on a year-to-year basis. So if they were to earn and then re-invest any income, what they would re-invest is the amount that is available after paying tax. Mutual Fund schemes, on the other hand, do not pay any tax on their income. So the same earning in a mutual fund scheme could facilitate a higher re-investment. This differential tax treatment offers an opportunity to investors to multiply their money within a scheme, without paying tax in the interim. The incidence of taxation can be postponed until the investors needs the money—at which point of the time the income can be structured as a long-term capital gain.
- **Choice of Risk Position** -There are as many risk-level options among mutual fund schemes as the water level options in the milk sold by the unorganized milk sector in India! The choice of water level is entirely that of the buyer. The investor can either savour the water (risk) or drown in it. Each mutual fund promises a certain water (risk) level, and is expected to stick to it. Mutual fund schemes that do not stick to their promise are not worth investing in. In the case of milk, the buyer would be happy with a water level that is lower that what was promised. However, with mutual funds, variation from promised risk level is unethical, irrespective of whether it is higher or lower than the promise. The trustees are responsible for ensuring that the AMC invests as per its committed investment objective, and maintains the promised risk character of the scheme.
- **Professional Management** - Investment is a specialized and full-time activity. AMCs are expected to have the professional people and the establishment to carry out this specialized work. Further, professional managers can take more dispassionate decisions, such as selling in stop-loss situations, which investors find difficult on emotional grounds.
- **Investment Convenience** -The facility of marking investments through service centers as well as through the Internet, a facility offered by some AMCs, ensures convenience. Similarly, through standing

instructions it is possible for investors to adopt SIP, SWP or STP. Mutual funds that permit switches between schemes without any cost help investors to manage their exposures economically.

- **Liquidity**- Open-ended schemes offer liquidity through on-going sale and repurchase facility. Thus, the investor does not have to worry about finding a buyer for her investment—a risk normally associated with direct investment in the securities market.
- **Investment Lot** - Direct investment in the services market often comes with a stiff minimum investment requirement. This is particularly so in the Indian debt market, where realistic options for retail investors are only now emerging.
- **Cost Economies** - Given its size, an AMC would be in a position to negotiate better brokerage terms for the sales and purchase of its investments. No doubt the establishment costs of the AMC get loaded to its schemes, and thus changed to the scheme's investors. But there are regulations on the extent of such loading. So long as the incremental returns through professional management, tax efficiencies, and the cost economics are more than the establishment costs charged to the schemes, investors gain by investing through mutual funds.

Disadvantage of Mutual Fund

- **No Guarantees**: No investment is risk free and investment in mutual fund is not an exception to it. It implies that, anyone who invests through a mutual fund runs the risk of losing money also.
- **Adverse effect on Return on Investment**: Investment and disinvestment decisions of fund managers of AMC requires deep and clear understanding of various avenues of investment in the universe and ever changing risk and return characteristics associated with each avenue of investment. This makes fund managers to get frequently involved in churning of portfolios. This process of frequent updating the portfolio may adversely affect the return on investment to investors.
- **Returns are associated with market risk**: Investment into mutual fund is not free from the impact of market risk. Mutual funds experience price fluctuations along with the stocks that make up the fund.
- **Returns too affected by over/under diversification:** Although diversification is one of the keys to successful investing, many mutual fund investors tend to over / under diversify. The idea of diversification is to reduce the risks associated with holding a single security; over / under diversification occurs when investors acquire many funds that are highly related and, as a result, reduce benefits of diversification. At the same time, owning few securities may result to under diversification forcing investors to lose the benefits of optimum diversification.
- **It involves High Costs along with Risks:** Mutual funds provide investors with professional management, but it comes at a cost. Funds will typically have a range of different fees that reduce the overall payout.

Comparison of Other Product

The mutual fund sector operates under stricter regulations as compared to most other investment avenues apart from offering investors tax efficiency and legal comfort.

Company Fixed Deposits Versus Mutual Funds

Fixed deposits unsecured borrowing by the company accepting the deposit. Credit rating of the fixed deposit program is an indication of the inherent default risk in the investment. The moneys of investors in a mutual fund scheme are invested by the AMC in specific investment under that scheme. These investments are held and managed in trust for the benefit of the scheme's investors. On the other hand, there is no such direct correlation between a company's fixed deposit mobilization, and the avenues where it deploys these resources. A corollary of such linkages between mobilization and investment is that the gains and losses from the mutual fund scheme entirely flow through to the investors. Therefore, there can be no certainty of yield, unless a named guarantor assures a return or, to a lesser extent, if the investment is in a serial gilt scheme. On the other hand, the return under a fixed deposit is certain, subject only to the default risk of the borrower.

Both fixed deposits and mutual funds offer liquidity, but subject to some differences.

1. The provider of liquidity in the case of fixed deposits is the borrowing company. In mutual funds, the liquidity provider is the scheme itself for open-end schemes, or the market in the case of close-ended schemes.
2. The basic value at which fixed deposits are encashable is not subject to market risk. However, the value at which units of a scheme are redeemed entirely depends on the market. If securities have gained in value during the period, then the investor can even earn a return that is higher than what she anticipated when she invested. Conversely, she could also end up with a loss.
3. Early encashment of fixed deposits is always subject to a penalty charged by the company that accepted the fixed deposit. Mutual fund schemes also have the option of charging a penalty on “early” redemption of units. If the NAV has appreciated adequately, then despite the exit load, the investor could earn a capital gain on her investment.

Bank Fixed Deposits Versus Mutual Funds

Bank fixed deposits are similar to company fixed deposits. The major difference is that banks are more stringently regulated than are companies. They even operate under strict requirements regarding Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) mandated by RBI. While the above are causes for comfort, bank deposits too are subject to default risk. However, given the political and economic impact of bank defaults, the government as well as Reserve Bank of India (RBI) tries to ensure that banks do not fail. Further, bank deposits up to Rs. 100, 00 are protected by the Deposit Insurance and Credit Guarantee Corporation (DICGC), so long as the bank has paid the required insurance premium of 5 paise per annum for every Rs. 100 of deposits. The monetary ceiling of Rs. 100, 000 is for all the deposits in all branches of a bank, held by the same capacity and right.

Bonds And Debentures Versus Mutual Funds

As in the case of fixed deposits, credit rating of a blood or debenture is an indication of the inherent default risk in the investment. However, unlike fixed deposits, bonds and debentures are transferable securities. While an investor may have an early encashment option from the issuer (for instance through a “put” option), liquidity is generally through a listing in the market. Implications of this are:

- If the security does not get traded in the market, then the liquidity remains on paper. In this respect, an open-ended scheme offering continuous sale /purchase option is superior.
- The value that the investor would realize in an early exit is subject to market risk. The investor could have a capital gain or a capital loss. This aspect is similar to a mutual fund scheme.

It is possible for an astute investor to earn attractive returns by directly investing in the debt market, and actively managing the positions. Given the market realities in India, however, it is difficult for most investors to actively manage their debt portfolio. Further, at times it is difficult to execute trades in the debt market even when the transaction size is as high as Rs. 1 crore. In this respect, investment in a debt scheme would be beneficial. Debt securities could be backed by a hypothecation or mortgage of identified fixed and / or current assets, e.g. secured bonds or debentures. In such a case, if there is a default, the identified assets become available for meeting redemption requirements. An unsecured bond or debenture is for all practical purposes like a fixed deposit, as far as access to assets is concerned. The investments of a mutual fund scheme are held by a custodian for the benefit of investors in the scheme. Thus, the securities that relate to a scheme are ring fenced for the benefit of its investors.

Equity Versus Mutual Funds

Investment in both equity and mutual funds are subject to market risk. An investor holding an equity security that is not traded in the market place has a problem in realizing value from it. But investment in an open-end mutual fund eliminates this direct risk of not being able to sell the investment in the market. An indirect risk remains, because the scheme has to realize its investments to pay investors. The AMC is however in a better position to handle the situation. Another benefit of equity mutual fund schemes is that they give 20 investors the benefit of portfolio diversification through a small investment. For instance, an investor can take an exposure to the index by investing a mere Rs. 5,000 in an index fund.

Life Insurance Versus Mutual Fund

Life insurance is a hedge against risk and not really investment option. So, it would be wrong to compare life insurance against any other financial product. Occasionally on account of market inefficiencies or mis-pricing of products in India, life insurance products have offered a return that is higher than a comparable "safe" fixed return security—thus, you are effectively paid for getting insured! Such opportunities are not sustainable in the long term.

Mutual Funds and Household Savings

Mutual funds are the fastest growing institutions in the household savings sector. Growing complications and risks in the stock market, rising tax rates and increasing inflation have pushed households towards mutual funds. The present share of mutual funds in household financial assets is over 5 per cent in the USA, 8 per cent in Germany, 3 per cent in Japan, 3 per cent in Italy and about 5 per cent in India.

The share of mutual funds in personal/household savings is one indicator of the importance of mutual funds in the savings market, but what is more important is the rate of growth of this share. In India, there has been a steady increase in the share of mutual funds in household savings (Financial assets) since 1988-89, i.e., after the entry of public sector mutual funds. Gross savings of the household sector in financial assets increased from Rs 12,118 crore in 1980-81 to Rs 1, 35, 348 crore in 1994-95.

The banking sector is the most dominant in the savings market but its role in the savings market was declined relatively. The most significant growth 1980- 81 to 1992-93 was noted in respect of units of Unit Trust of India (UTI) which increased 0.3 per cent of the total household savings in 1980-81 to 7.0 per cent in 1992-93 (but declined to 2.8 per cent in 1994-95). The percentage share of equity shares and debentures together increased from 3.4 per cent to 10.2 per cent.

However, the percentage share of bank deposits declined from 45.8 per cent in 1980-81 to 33.2 per cent in 1993-94 to register a further increase of 40.2 per cent in 1994-95. The overall bearish trend in the capital market and the sluggish performance of mutual funds contributed to the latter's decline in the new issues market 1994-95. The growth of units of UTI was much faster than that of bank deposits, LIC premia, provident funds, pensions, shares and debentures. The collection under units of UTI increased from Rs 31 crore in 1980-81 to Rs 9,087 crore in 1991-92, while the same for share/ debentures increased from Rs 412 crore to Rs 6,800 crore. For LIC the increase was from Rs 915 crore to Rs 7,303 crore, and for provident funds and pensions from Rs 2,122 crore to Rs 12,500 crore, during the same period. While collections under LIC premia and provident funds continued to increase subsequently, those under UTI, shares and debentures declined.

Mutual Funds and The Capital Market

The active involvement of mutual funds in promoting economic development can be seen not only in terms of their participation in the savings market but also in their dominant presence in the money and capital market. A developed financial market is critical to overall economic development, and mutual funds play an active role in promoting a healthy capital market. Mutual funds increase liquidity in the money market. The assets holding pattern of mutual funds in the USA indicates the dominant role of the mutual funds in the money and capital market. Moreover, they have also rendered crucial support to securitized mortgage loans and municipal bond market in the USA. In the USA, mutual funds provide very active support to the secondary market in terms of purchase of securities.

According to Laderman and Smith (1993) mutual funds provided 96 per cent of the money that went into stocks in 1993 as against 80 per cent in 1991. Mutual funds have been identified as one of the important factors pushing up market prices of securities, and it was estimated that equity mutual funds 22 accounted for 30 per cent trading of the New York Stock Exchange (NYSE) in 1993 as compared with 10 per cent in 1983. In Japan, holdings of shares (corporate equities) by investment trusts increased from 1.3 per cent in 1971 to 3.4 per cent in 1993. Similarly the market value of all the shares hold by Japanese investment trusts increased from 2 per cent of total market value to 3.1 per cent of total market value (of all listed shares). This is an indication of the growing penetration of mutual funds in the capital market. Investors' preference patterns in India has undergone a tremendous change during recent times, along with changes in the share of financial assets in the total annual savings which increased from 39.41 per cent in 1980-81 to 64.19 per cent in 1993-94. We have also noted that Indian investors have moved towards more liquid, growth-oriented tradable instruments like shares/debentures, and units of mutual funds. This shift in asset holding pattern of investors has been significantly influenced by the ‘equity’ and ‘unit’ culture. While the holders of company shares/ debentures are concentrated in urban areas, small/medium investors in semi-urban and rural areas are tending towards mutual funds.

Mutual funds in India have certainly created awareness among investors about equity-oriented investment and its benefits. Another important trend can be noted from the data. While in more countries, the growth of mutual funds has centered on one or two types of funds-equity or bond, or both-the trend in the USA and France indicates a balanced development. In these two countries the important funds, namely equity funds, bond funds and money market funds, have all developed together, indicating the diversified preference pattern typical of a mature financial market.

There is an implicit relationship between market development and product diversification, as seen in the USA and France his relationship is quite instructive for a newly developed mutual funds market like India which should make all efforts to tap the potential from all segments of investors through a variety of suitable schemes.

Mutual Funds and Corporate Finance

The private corporate sector in India is a deficit sector and the gap between demands a supply of financial resources is met by funds raised through loans, advances and issuance of securities. However, the buoyancy in the capital market has increased the reliance of the corporate sector security financing. The share of this instrument in financing the resource gap of the corporate sector has more than doubled between 1988-89 and 1991-92 from 16.72 per cent in 1988- 89 to 36.28 per cent in 1991-92. The changing pattern of corporate financing indicates that the banking sector is losing its importance vis-à-vis the ‘other financial sector’ (including mutual funds). According to the flow of funds statistics published by the RBI, the share of the banking sector in filling the resource gap of the corporate sector has declined from 54.42 per cent in 1988-89 to 2.3 per cent in 1991-92, while that of the ‘other financial sector’ (including mutual funds) has increased from 39.9 per cent to 102.58 per cent during the same period. RBI has noted that ‘The rapid growth of mutual funds and increase in term lending by OFI’s (other financial institutions) appear to have contributed to this trend. Direct financing by mutual funds to the corporate sector has substantially increased after the SEBI guidelines allowed the corporate sector to reserve 20 per cent of public issues for Indian mutual funds. Mutual funds have also widened the private placement market for corporate securities. Mutual funds have enabled the corporate sector to raise capital at reduced costs and have opened an avenue for alternate source of capital. Mutual funds in India have emerged as a critical institutional linkage among various financial segments like savings, capital market and the corporate sector. They provide much needed impetus to the money markets and stock markets, in addition to direct and indirect support to the corporate sector. Above all, mutual funds have given a new direction to the flow of personal savings and enabled small and medium investors in remote rural and semi-urban areas to reap the benefits of stock market investments. Indian mutual funds are thus playing a very crucial developmental role in allocating resources in the emerging market economy.

Conclusion

The Indian capital market having a long history spanning over a century has passed through the most radical phases. It has witnessed extraordinary developments and innovations during the nineties. One such development was the improved role of the mutual funds in financial intermediation. Mutual funds in India have fast emerged as an important instrument of household savings. Due to the flexibility and variety available in them they have the potential to rival traditional money saving instruments by attracting household sector or retail investor’s savings. India has been amongst the fastest growing markets for mutual funds since 2004, witnessing a CAGR of 29 % in the five-year period from 2004 to 2008 (though period of 2008–10 saw a decline due to global crisis) as against the global average of 4 %. The increase in revenue and profitability, however, has not been proportionate with the AUM growth in the last 10 years. Low share of global assets under management, low penetration levels, limited share of mutual funds in the household financial savings and the climbing growth rates in the last few years that are amongst the highest in the world, all point to the future scope of growth for the Indian mutual fund industry.

The Indian mutual fund industry has evolved from a single player monopoly in 1964 to a fast growing competitive market with active participation of foreign AMCs that too on the back of a strong regulatory frame work. This industry has had a swift growth because of factors like infrastructural expansion and boost in personal disposable incomes. With the rising risk enthusiasm, personal assets, and consciousness of investors, mutual funds in India are becoming a preferred investment option. With regards to the regulatory reforms also the impact on the performance has been positive signaling the healthy intentions of the bodies governing this industry which are making efforts in the form of such changes for the development of this segment. Even the restrictions are to enable them to run faster with the rapidly changing global scenario. The Net Asset Value of the Fund is the cumulative market value of the assets the fund holds, net of its liabilities. And this very NAV has been taken as the basis to evaluate the performance in this study.

The study shows that there have been drastic upward movements in the NAVs, which show that they have performed very well in terms of their market value. It can also be concluded that mutual funds in India are becoming better and better in handling market and fund specific risk both. The more experience they are gaining in the economy the more adaptable they are becoming.

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