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Investment Through Mutual Fund

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Abstract

Indian Mutual Fund Industry is increasing by leaps and bound . Since its inception in 1964 there was only 25 cr. Assets under management like a sapling but now it has grown into a big banyan tree with assets of Rs. 4,81,749 cr under assets management companies up to march 2010. It shows that people are investing through Mutual fund due to its low risk, uniqueness and special benefits. In the present research paper an endeavour is made to aware the investment community about the Mutual Fund schemes, its growth during the years and investment strategy to make extra ordinary return from the investment in various schemes of Mutual Fund operated by both public and private sector.

1. INTRODUCTION

Investment in stock market is very risky but man is greedy by nature so he remains exploring the ways of maximizing his returns on his investment. He is not satisfied with the fixed returns instruments of savings. So his greed encourages him to take high risk on his investment. The old saying about the investment is absolutely fit here "as the more is the risk, the more would the gain".

2. DEFINING MUTUAL FUND

A Mutual Fund is a trust that pools the savings of a number of investors who share a common financial goal. Anybody with an investible surplus of as little as a few hundred rupees can invest in Mutual Funds.These investors buy units of a particular Mutual Fund scheme that has a defined investment objective and strategy. The money thus collected is then invested by the fund manager in different types of securities. These could range from shares to debentures to money market instruments, depending upon the scheme's stated objectives. The income earned through these investments and the capital appreciation realised by the scheme are 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, professionally managed basket of securities at a relatively low cost.

SEBI is the regulatory body to control and regulate the securities market and Mutual Fund industry in India. So it is an important entity of Mutual Fund Business.

Growth Of Mutual Fund Industry: The mutual fund industry in India started in 1963 with the formation of Unit Trust of India, at the initiative of the Government of

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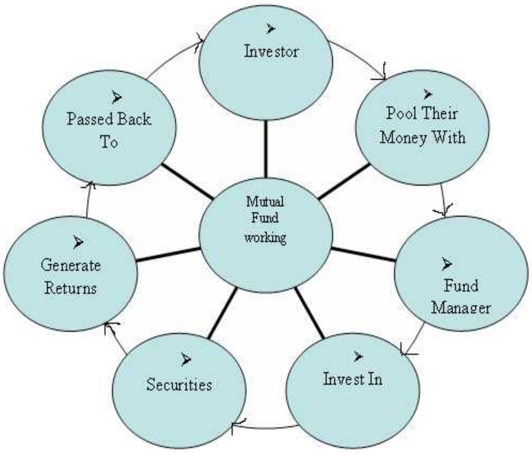
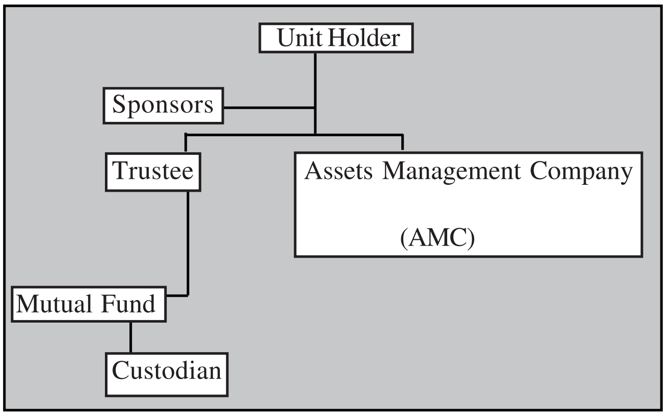
The flow chart below describes broadly the working of a mutual fund



Entities Involved in Mutual Fund Business :- The following entities are involved in Mutual fund business.



India and Reserve Bank of India. The growth of mutual funds in India can be broadly divided into four distinct phases

First Phase – 1964-87 : Unit Trust of India (UTI) was established on 1963 by an Act of Parliament. It was set up by the Reserve Bank of India and functioned under the Regulatory and administrative control of the Reserve Bank of India. In 1978 UTI was de-linked from the RBI and the Industrial Development Bank of India (IDBI) took over the regulatory and administrative control in place of RBI. The first scheme launched by UTI was Unit Scheme 1964. At the end of 1988 UTI had Rs.6,700 crores of assets under management.

Second Phase – 1987-1993 : (Entry of Public Sector Funds) - 1987 marked the entry of non- UTI, public sector mutual funds set up by public sector banks and Life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC). SBI Mutual Fund was the first non- UTI Mutual Fund established in June 1987 followed by Canbank Mutual Fund (Dec 87), Punjab National Bank Mutual Fund (Aug 89), Indian Bank Mutual Fund (Nov 89), Bank of India (Jun 90), Bank of Baroda Mutual Fund (Oct 92). LIC established its mutual fund in June 1989 while GIC had set up its mutual fund in December 1990. At the end of 1993, the mutual fund industry had assets under management of Rs.47,004 crores.

Third Phase – 1993-2003 (Entry of Private Sector Funds) : 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 (now merged with Franklin Templeton) was the first private sector mutual fund registered in July 1993. The 1993 SEBI (Mutual Fund) Regulations were substituted by a more comprehensive and revised Mutual Fund Regulations in 1996. The industry now functions under the SEBI (Mutual Fund) Regulations 1996. 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.44,541 crores of assets under management was way ahead of other mutual funds.

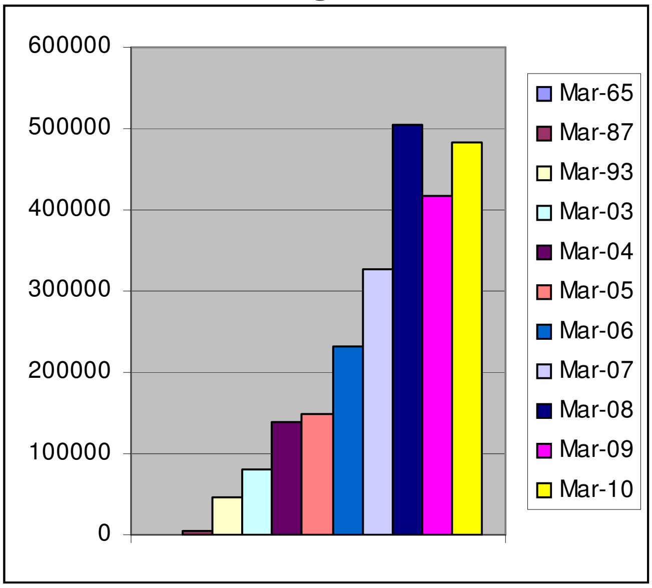
Fourth Phase – since February 2003 : In February 2003, following the repeal of the Unit Trust of India Act 1963 UTI was bifurcated into two separate entities. One is the Specified Undertaking of the Unit Trust of India with assets under management of Rs.29,835 crores as at the end of January 2003, representing 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. The second is the UTI Mutual Fund, sponsored by SBI, PNB, BOB and LIC. It is registered with SEBI and functions under the Mutual Fund Regulations. With the bifurcation of the erstwhile UTI which had in March 2000 more than Rs.76,000 crores of assets under management and with the setting up of a UTI Mutual Fund, conforming to the SEBI Mutual Fund Regulations, and with recent mergers taking place among different private sector funds, the mutual fund industry has entered its current phase of consolidation and growth. The tables indicates the growth of assets over the years.

Table 1
Growth in Assets Under Management

YEAR	AUM(Rs in Crores)
Mar-65	25
Mar-87	4564
Mar-93	47000
Mar-03	79464
Mar-04	139616
Mar-05	149554
Mar-06	231862
Mar-07	326388
Mar-08	505152
Mar-09	417300
Mar-10	481749

Source: AMFI

Growth in Assets Under Management Through Chart



3. MUTUAL FUND SCHEMES AND THEIR CLASSIFICATION

a) On the Basis of Structure

Open-Ended Scheme: These do not have a fixed maturity. You deal with the Mutual Fund for your investments and redemptions. The key feature is liquidity. You can conveniently buy and sell your units at Net Asset Value(NAV) related prices, at any point of time

Close-Ended Schemes : Schemes that have a stipulated maturity period (ranging from 2 to 15 years) are called close-ended schemes. You can invest in the scheme at the time of the initial issue and thereafter you can buy or sell the units of the scheme on the stock exchanges where they are listed. The market price at the stock exchange could vary from the scheme'sNAV on account of demand and supply situation, unit holder's expectations and other market factors. One of the characteristics of the close-ended schemes is that they are generally traded at a discount to NAV; but closer to maturity, the discount narrows. Some close-ended schemes give you an additional option of selling your units to the Mutual Fund through periodic repurchase at NAV related prices. SEBI Regulations ensure that at least one of the two exit routes are provided to the investor under the close ended schemes.

Interval Schemes : These combine the features of open-ended and close-ended schemes. They may be traded on the stock exchange or may be open for sale or redemption during predetermined intervals at NAV related prices.

b) On the basis of Investment Goals

Growth Schemes : Aim to provide capital appreciation over the medium to long term. These schemes normally invest a majority of their funds in equities and are willing to bear short term decline in value for possible future appreciation. These schemes are not for investors seeking regular income or needing their money back in the short term. Suitability for: Investors in their prime earning years and Investors seeking growth over the long term.

Income Schemes : Aim to provide regular and steady income to investors. These schemes generally invest in fixed income securities such as bonds and corporate debentures. Capital appreciation in such schemes may be limited. Suitability for: Retired people and others with a need for capital stability and regular income and Investors who need some income to supplement their earnings.

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Balanced Schemes: Aim to provide both growth and income by periodically distributing a part of the income and capital gains they earn. They invest in both shares and fixed income securities in the proportion indicated in their offer documents. In a rising stock market, the NAV of these schemes may not normally keep pace or fall equally when the market falls. Suitability for: Investors looking for a combination of income and moderate growth.

Money Market / Liquid Schemes : Aim to provide easy liquidity, preservation of capital and moderate income. These schemes generally invest in safer, short term instruments such as treasury bills, certificates of deposit, commercial paper and interbank call money. Returns on these schemes may fluctuate, depending upon the interest rates prevailing in the market. Suitability for: Corporates and individual investors as a means to park their surplus funds for short periods or awaiting a more favourable investment alternative.

T3ax Saving Schemes (Equity Linked Saving Scheme - ELSS) : These schemes offer tax incentives to the investors under tax laws as prescribed from time to time and promote long term investments in equities through Mutual Funds. Suitability for: Investors seeking tax incentives.

Special Schemes : This category includes index schemes that attempt to replicate the performance of a particular index such as the BSE Sensex, the NSE 50 (NIFTY) or sector specific schemes which invest in specific sectors such as Technology, Infrastructure, Banking, Pharma etc. Besides, there are also schemes which invest exclusively in certain segments of the capital market, such as Large Caps, Mid Caps, Small Caps, Micro Caps, 'A' group shares, shares issued through Initial Public Offerings (IPOs), etc. Index fund schemes are suitable for investors who are satisfied with a return approximately equal to that of an index. Sectrol fund schemes are suitable for investors who have already decided to invest in a particular sector or segment.

Fixed Maturity Plans : Fixed Maturity Plans (FMPs) are investment schemes floated by mutual funds and are close-ended with a fixed tenure, the maturity period ranging from one month to three/five years. These plans are predominantly debt-oriented, while some of them may have a small equity component. The objective of such a scheme is to generate steady returns over a fixed-maturity period and protect the investor against market fluctuations. FMPs are typically passively managed fixed income schemes with the fund manager locking into investments with maturities corresponding with the maturity of the plan. FMPs are not guaranteed products.

ExchangeTraded Funds (ETFs) : Exchange Traded Funds are essentially index funds that are listed and traded on exchanges like stocks. Globally, ETFs have opened a whole new panorama of investment opportunities to retail as well as institutional investors. ETFs enable investors to gain broad exposure to entire stock markets as well as in specific sectors with relative ease, on a real-time basis and at a lower cost than many other forms of investing. An ETF is a basket of stocks that reflects the composition of an index, like S&P CNX Nifty, BSE Sensex, CNX Bank Index, CNX PSU Bank Index, etc. The ETF's trading value is based on the net asset value of the underlying stocks that it represents. It can be compared to a stock that can be bought or sold on real time basis during the market hours. The first ETF in India, Benchmark Nifty Bees, opened for subscription on December 12, 2001 and listed on the NSE on January 8, 2002.

Capital Protection Oriented Schemes : Capital Protection Oriented Schemes are schemes that endeavour to protect the capital as the primary objective by investing in high quality fixed income securities and generate capital appreciation by investing in equity / equity related instruments as a secondary objective. The first Capital Protection Oriented Fund in India, Franklin Templeton Capital Protection Oriented Fund opened for subscription on October 31, 2006.

Gold ExchangeTraded Funds (GETFs) : Gold Exchange Traded Funds offer investors an innovative, cost-efficient and secure way to access the gold market. Gold ETFs are intended to offer investors a means of participating in the gold bullion market by buying and selling units on the Stock Exchanges, without taking physical delivery of gold. The first Gold ETF in India, Benchmark GETF, opened for subscription on February 15, 2007 and listed on the NSE on April 17, 2007.

4. CAPITAL PROTECTION ORIENTED SCHEMES

Quantitative Funds : A quantitative fund is an investment fund that selects securities based on quantitative analysis. The managers of such funds build computer based models to determine whether or not an investment is attractive. In a pure "quant shop" the final decision to buy or sell is made by the model. However, there is a middle ground where the fund manager will use human judgment in addition to a quantitative model. The first Quant based Mutual Fund Scheme in India, Lotus Agile Fund opened for subscription on October 25, 2007.

Funds Investing Abroad : With the opening up of the Indian economy, Mutual Funds have been permitted to invest in foreign securities/ American Depository Receipts (ADRs) / Global Depository Receipts (GDRs). Some of such schemes are dedicated funds for investment abroad while others invest partly in foreign securities and partly in domestic securities. While most such schemes invest in securities across the world there are also schemes which are country specific in their investment approach.

Fund of Funds (FOFs) : Fund of Funds are schemes that invest in other mutual fund schemes. The portfolio of these schemes comprise only of units of other mutual fund schemes and cash / money market securities/ short term deposits pending deployment. The first FOF was launched by Franklin Templeton Mutual Fund on October 17, 2003. Fund of Funds can be Sector specific e.g. Real Estate FOFs, Theme specific e.g. Equity FOFs, Objective specific e.g. Life Stages FOFs or Style specific e.g.Aggressive/ Cautious FOFs etc. Please bear in mind that any one scheme may not meet all your requirements for all time.

5. WHAT SHOULD BE THE INVESTMENT STRATEGY FOR MUTUAL FUND

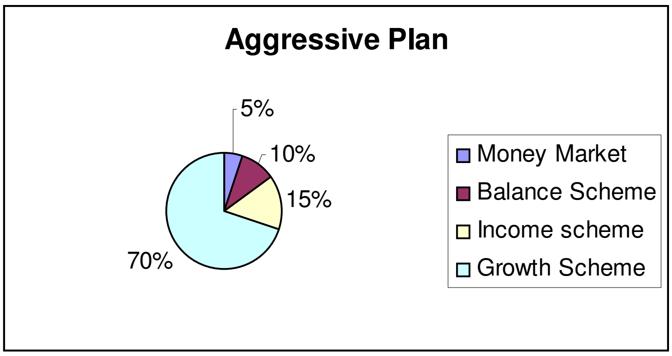
Investment strategy may vary for different types of instruments of saving. So for Mutual Fund investment the strategy too must be unique. We should follow the following strategy for Mutual fund.

i) *Investment Goals :* First of all you should decide your investment goal. What is the purpose of saving e.g- Marriage of daughter or higher education of children, regular monthly income, purchase of house, etc. The priorities of persons are different so their investment goals are different. If you do not decide your investment goals then your investment will not fulfill your expectations because when anybody invests for long term, the returns are high and vice-versa.

ii) *Risk Appetite :* Risk appetite is the other important factor to decide the return. If your risk appetite is high, you invest more in equities but if you don't want to take risk then your returns are low and you should go to debt funds. In our opinion the risk appetite of a general person depends on his age . The portion of debt in fund allocation depends on age e.g if you are at the age of 40 then in your investment ratio should be 40:60, (40% in debt or fixed instruments and 60% in equity) if you are at the age of 70 then your investment allocation should be 70:30(70% in debt or fixed instruments and 30% in equity) as a rule .

iii) *Selection of the right Mutual Fund :* There are many fund management companies and their schemes. As per your investment goals, you should decide the fund house and schemes with the help of mutual fund advisor. Role of advisor is very important to selection the mutual fund because advisor knows the schemes better than you. Generally, we decides the schemes become ourselves but in our opinion when we go to doctor, advocate, engineer, plumber, electrician, then why do we not go to financial advisor or mutual fund advisor for investment. Investment is very risky job. So in our views you should decide your mutual fund investment through mutual fund advisor only.

iv) *Pack of the Sschemes :* Investing in just one Mutual Fund Scheme may not meet all your investment needs. You may consider investing in a combination of schemes to achieve your specific goals. The following charts could prove useful in selecting a combination of schemes that satisfy your needs.



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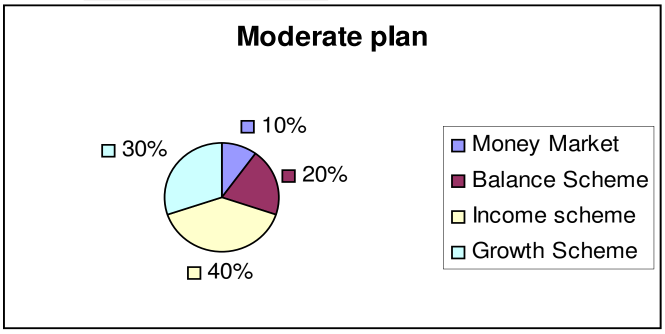

v) Regularity of Investment : There are two options of investment. First – invest all your money in one go. Second- invest your money at regular intervals. If you choose first option you may get either higher return or higher loss, in second option your return may be moderate to high. If we invest at regular intervals say monthly, quarterly we reap the benefits of cost of averaging but in lump sum investments this benefit can not be availed. So in our opinion the best way of investing is through systematic investment plan.

vi) Tax Treatment : As per the current tax laws, Dividend/Income Distribution made by mutual funds is exempt from Income Tax in the hands of investor. However, in case of debt schemes Dividend/ Income Distribution is subject to Dividend Distribution Tax. Further, there are other benefits available for investment in Mutual funds under the provisions of the prevailing tax laws. As per the current income tax rules if a person invest in mutual fund schemes (ELSS) he gets the tax benefits under section 80 C up to 1,00,00 Rs.. At the time he is getting tax benefit under section 80C as well as higher rate of return on his investment as compare to other schemes.

vii) *Start Investing as Eearly as Possible :* It is desirable to start investing early and stick to a regular investment plan. If you start now, you will make more than if you wait and invest later. The power of compounding lets you earn income on income and your money multiplies at a compounded rate of return.

All you need to do now is to get in touch with a Mutual Fund or your advisor and start investing. Reap the rewards in the years to come. Mutual Funds are suitable for every kind of investor whether starting a career or retiring, conservative or risk taking, growth oriented or income seeking

6. CONCLUSION

Mutual Fund is a very big sector. It can not be explained in few pages. An effort is made to aware the investment community about the various Mutual Fund schemes their working and the best strategy to invest in Mutual Fund schemes. If the aware investment community inculcates the tenets described above, efforts would be fruitful. In part two we would touch the other more significant aspects of Mutual Fund Investments.

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