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MUTUAL FUND IN INDIA– PAST SCENARIO,PRESENT HURDELS AND FUTURE ACTIONS PLANES FOR TRANSFORMATIONAL GROWTH.

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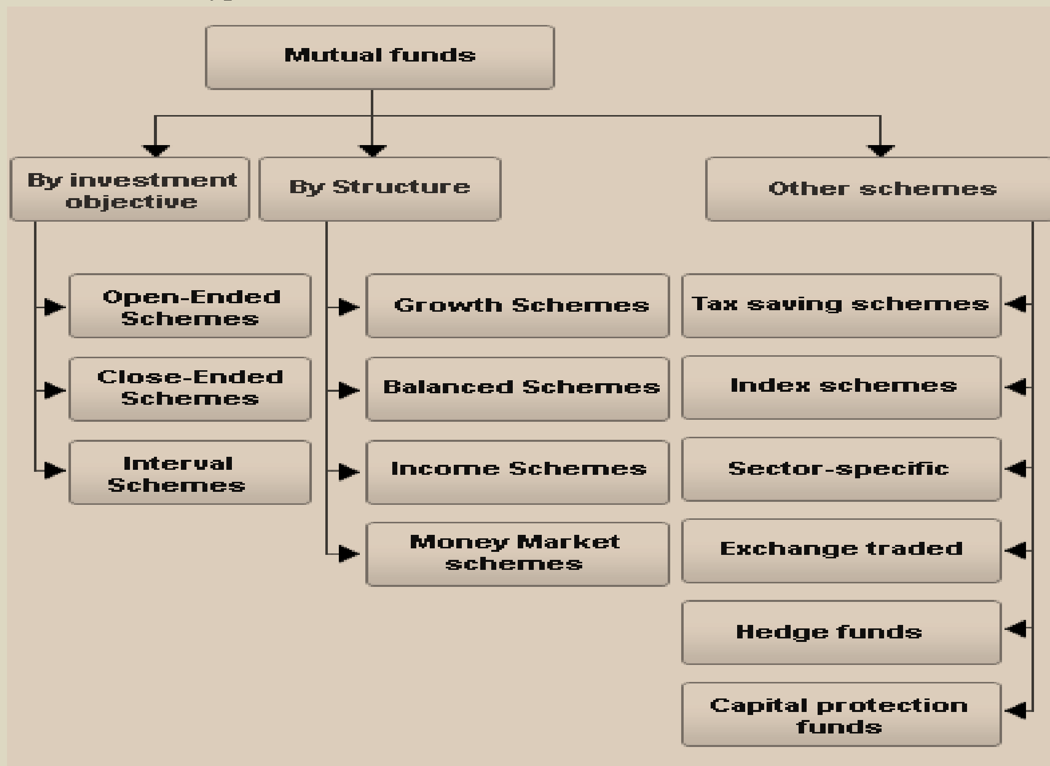
INTRODUCTION:

Mutual fund is pools of saving invested by investor who have common financial goal which is manage by professional .The intrinsic value or market value of mutual funds is Net Asset Value (NAV). Net Asset Value is the market value of the assets of the scheme minus its liabilities. The per unit NAV is the net asset value of the scheme divided by the number of units outstanding on the Valuation Date. By structure there are mainly two types of MF open ended and closed ended in open ended investor can invest in fund in any time after IPO of fund but in closed ended fund issuing shares of stock in blocks at the time of IPO of fund and under no obligation to repurchase them back but it can be traded on stock exchange.

Table 03: Different Types Of Mutual Fund



ARE MUTUAL FUND AND EQUITY TRADED FUND (ETF) SAME?

ETF is similar to a mutual fund in that it offers investors a proportionate share in a pool of stocks, bonds, and other assets. It is governed by the Investment Company Act of 1940 like mutual funds and is most commonly structured as an open-end investment company. For example, like a mutual fund, an ETF is required to post the mark-to-market net asset value (NAV) of its portfolio at the end of each trading day and must conform to the main investor protection mechanisms of the Investment Company Act, including limitations on leverage, daily valuation and liquidity requirements, prohibitions on transactions with affiliates, and rigorous disclosure obligations. Despite these similarities, key features differentiate ETFs from mutual funds.

One major difference is that retail investors buy and sell ETF shares on a stock exchange through a broker-dealer, much like they would any other type of stock. In contrast, mutual

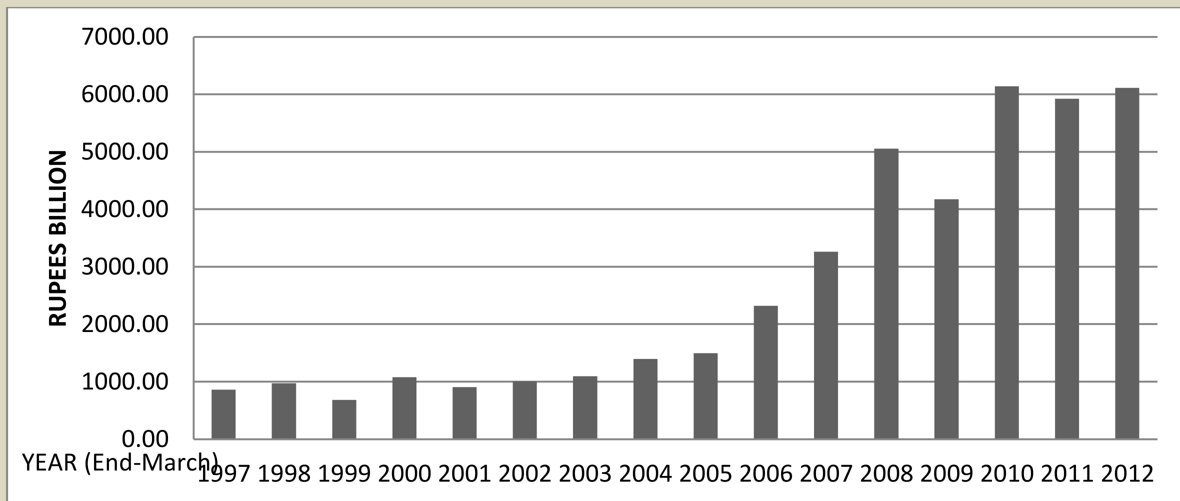
fund shares are not listed on stock exchanges. Rather, retail investors buy and sell mutual fund shares through a variety of distribution channels, including through investment professionals—full-service brokers, independent financial planners, bank or savings institution representatives, or insurance agents— or directly from a fund company or discount broker.

Pricing also differs between mutual funds and ETFs. Mutual funds are "forward priced," which means that although investors can place orders to buy or sell shares throughout the day, all orders placed during the day will receive the same price—the NAV—the next time it is computed. Most mutual funds calculate their NAV as of 4:00 p.m. eastern time because that is the time U.S. stock exchanges typically close. In contrast, the price of an ETF share is continuously determined on a stock exchange. Consequently, the price at which investors buy and sell ETF shares may not necessarily equal the NAV of the portfolio of securities in the ETF. Two investors selling the same ETF shares at different times on the same day may receive different prices for their shares, both of which may differ from the ETF's NAV

PAST SCENARIO

The mutual fund industry in India started in 1963 with the formation of Unit Trust of India, at the initiative of the Government of India and Reserve Bank of India. The history of mutual funds in India can be broadly divided into four distinct phases

TABLE 01: ASSETS UNDER MANAGEMENT OF MUTUAL FUNDS



Note : Data for 2012 are provisional.
Source : Securities and Exchange Board of India.

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.

Table 02: Overview Indian Mutual Fund Industry

MF Industry					
	UTI	Bank/ Financial Institution Sponsored	Private Sector - Indian	JV-Predominantly Indian	JV-Predominantly Foreign
Key Players	UTI AMC	SBI (JV), LIC, Canara Bank & BoB Asset	Reliance, Tata AMC, Kotak Mahindra	Prudential ICICI, HDFC, Birla Sun life, DSPML	Franklin Templeton, Standard Chartered, HSBC
Total Market Share	9.1%	8.7%	30.4%	31.2%	20.6%
Number of Players	1	4	10	6	12

Source: Article by Prof Ravi Anshuman,"Mutual fund Competition-search for sustainable strategy" Indian Institute Of Management –Bangalore,

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.

PRESENT HURDLES

1.Low Financial Literacy Among Investors

Low customer awareness levels and financial literacy pose the biggest challenge to channelizing household savings into mutual funds. The general lack of understanding of mutual fund products amongst Indian investors is pervasive in metros and Tier 2 cities alike and majority of them draw little distinction in their approach to investing in mutual funds and direct stock market investments. A large majority of retail investors lack an understanding of risk-return, asset allocation and portfolio diversification concepts. Low awareness of SIPs in India has resulted in a majority of the customers investing in a lump sum manner.

In a country, where 55 per cent of domestic savings go into bank fixed deposits, the mutual fund industry sees a huge scope for growth. "Investors are still not aware that inflation eats into a chunk of their savings and they need instruments that give healthy inflation adjusted returns. Equity mutual funds are the best way to beat inflation and the mutual fund industry needs to drive home this message among investors," says Jaideep Bhattacharya, chief marketing officer, UTI Mutual Fund. The Association of Mutual Funds in India (Amfi) has initiated a programme under which each fund house needs to organise at least five investor awareness programmes every month. However, the mutual fund industry estimates that the cost of investor education could go into thousands of crores of rupees and it can't bear the cost alone.

2.Low Retail Participation

The mutual fund industry appears to be on a losing streak. Ever since the Securities and Exchange Board of India (SEBI) banned entry loads-charges collected by fund houses from investors at the time of investment- the number of retail investors in mutual funds has been falling consistently. The number of investor folios dropped by 10 lakh between September 2009 and September 2010. Equity funds have seen the closure of around 19 lakh folios over a year since September 2009. The entry load ban came into effect in August 2009. Industry players, financial planners ('distributor' is a taboo word ever since the regulator banned entry loads and asked mutual fund agents to offer advisory services for a fee) and investors' representatives have been spending hours on deliberations and meetings to find a solution to stop the mass exodus. However, the industry doesn't seem to have a definite plan to get out of the precarious situation.

3. Inaccessibility in smaller towns and cities

Due to lack of an efficient distribution network Over half of household savings are currently locked in bank deposits as investors prefer products that protect their principal and ensure assured returns.

4. Performance related Problems

The investor prefers safety of the principal amount, regular returns, long-term growth, income tax benefits, etc. The mutual fund schemes have been designed based on the preferences of the investors, changes in stock/capital market, and returns on various instruments and changing profile of the investors. The schemes are framed and conceptualized by the top management of the mutual funds and marketed by their branches and through the agents. The agents and the sales executives of the mutual funds assure higher returns to the investors and paint a rosy picture about the mutual funds while marketing schemes. The mutual funds in our country have been quite wrongly promoted as an alternative to equity investing and created very high expectations in the minds of the investors. The ignorance of the investors about mutual funds coupled with aggressive selling by promising higher returns to the investors have resulted into loss of investors' confidence due to inability to provide higher returns. All mutual funds set a higher target for mobilization of savings from the investor by launching new schemes and expanding investor base. The agents or distributor of mutual funds are more governed by commissions and incentives they get for selling the schemes and not by the requirements of the investors and quality of the products. They share commissions with the investors and don't explain the risk factors to them.

5.Mutual Fund Expenses

Investors in mutual funds incur two primary types of expenses and fees: ongoing expenses and sales load fees. Ongoing fund expenses cover portfolio management, fund administration, daily fund accounting and pricing, shareholder services (such as call centers and websites), distribution charges known as 12b-1 fees, and other miscellaneous costs of operating the fund. These expenses are included in a fund's expense ratio—the fund's annual expenses expressed as a percentage of fund assets. Since expenses are paid from fund assets, investors pay these expenses indirectly. In contrast, sales loads are fees that investors pay directly either at the time of share purchase (front-end loads), when shares are redeemed (back-end loads), or over time (level loads).

To prevent this, SEBI has a cap on the maximum amount that a fund can charge on the weekly average assets of the scheme. For instance, it is a maximum of 2.5 per cent (will additional allowance 0.3 per cent given for selling in Tier II and Tier III cities) for active equity funds. It is lower for debt funds and index funds. This charge is made on the total assets of the scheme. Your NAV per unit is arrived at, after such a charge. Simply put, the return that you calculate on your NAV is after deduction of expense ratio. Earlier, SEBI had a cap on the individual components of the expenses such as fund management fee and distribution cost. But a few months ago, it removed such internal caps. As long as funds adhere to the overall limit, they can incur these costs in any proportion. SEBI also provided a recent option for investors to buy funds directly from AMCs (not through the distributor). If bought directly, the NAV – called the direct plan NAV – will not bear the fee paid to distributor. That means the direct plan NAV will be higher than the regular NAV to that extent.

FUTURE ACTION PLANES FOR TRANSFORMATIONAL GROWTH

The regulator SEBI is of the view that, as with other sectors of the economy, a long-term policy for mutual funds is critical to mobilizing domestic savings for economic expansion and achieving inclusive growth.

1.SEBI and Government of India should invest PF (Provident Fund) amount in MF like other developed nations as USA and other. Yes ,It is little but risky as market is volatile but If Indian government institutions invest in share market, they provide stability to the market. They are not like FII, which are always looking for opportunity to come and go from India market depending upon global economical developments.

2.There is a need for Mutual Funds, especially gilt funds, to complement the role of PDs in promoting retail holding in government securities. Mutual Funds are supposed to tap retail investors, who in turn, to the extent that they have long horizons, provide stability to the market. They also benefit small investors by providing them access to risk-free gilt edged securities.

3.The Mutual funds are allowed to participate in the Interest Rate Swap (IRS) market for the purpose of hedging their own balance sheet risks. However, their participation has remained quite muted. The IRS market, although very liquid, suffers from a low customer base of around 1 per cent. The Mutual Funds may increase the use of IRS for hedging their interest rate risk which would help in broadening and deepening of the IRS market.

4.Mutual Funds are also allowed by SEBI to trade on Interest Rate Futures (IRF). IRF contracts on 10-year notional coupon bonds were launched on NSE in August 2009. The product witnessed significant activity during the initial period, but liquidity tapered off subsequently. RBI has already issued guidelines for futures contracts on 91-day T-Bills, which are expected to be introduced shortly. RBI is also considering introduction of IRF contracts on 2- year and 5-year G-Secs. If the reason for Mutual Funds not actively participating in the G-Sec market is the underlying interest rate risk, then they obviously should make use of the IRF to hedge their interest rate risk. Their active participation will give impetus to the development of the IRF market.

5.Should expense ratio matter?

If you asked a US-based investor, this question will seem preposterous. This is because, in developed markets, where returns are often in single digits, the expense ratio can cause a dent in the amount you can take home. But in markets such as India, where equity funds have comfortably managed double digit returns, expense ratio has not really mattered much, especially in equity funds. What you see as returns in your fund is after such expense ratio. For instance, the average return of equity funds over the last 10 years was 23 per cent annually. This return, which is post expenses, is high enough.

When it matters ,

1.That said, there are times when your expense ratio will matter. Here's an indicative list as to when it matters most:1. Index funds are passively managed. If you see an index fund having a higher expense ratio than most other peers, then you should probably avoid it.

2. Debt funds are not geared to generate high returns like equities. Hence, you will do well to check both the asset size and the expense ratio with similar category peers. A fund with mediocre returns and high expense ratio has to be relooked, before investing.

3. If you hold an equity fund that is struggling to beat its benchmark, it is possible that its expense ratio is preventing it from inching up by 1-2 percentage points over its benchmark. Hence, if you are reviewing some of your under performers in your portfolio, check their expense ratio as well.

4. When you are looking at a fund-of-fund or a feeder fund that invests in another international fund, check the offer document for the expense ratio. Do note that the expense ratio will be what the fund incurs plus the expense of the underlying funds.

The launch of Credit Default Swap (CDS) is impending. The guidelines on introduction of plain vanilla OTC single-name CDS for corporate bonds in India would be effective from October 24, 2011. The Mutual Funds would be eligible to buy credit protection (buy CDS contracts) to hedge their underlying credit risk on corporate bonds. They would also be permitted as market-makers subject to their having strong financials and risk management capabilities as prescribed by SEBI and as and when permitted by the SEBI. It is expected that Mutual Funds' participation will provide momentum to the CDS market.

CONCLUSION

Mutual fund in India has great potential to achieve remarkable growth. As the equation and boundaries for financial markets are changing, so we should be more dynamic with the present change. It can conclude by saying that the growth must be inclusive. So we should reach beyond Metro cities and make mutual fund offerings available to people in smaller towns and cities has indeed taken up the attention of the industry.

However, several components of such an initiative, like investor education, expansioning investor participation and scheme innovation, need to be aligned in order to full inclusive growth. The industry needs to give important on the above factors, drawing out an efficient business and operating model to ensure that the inherent challenges that the industry is facing is efficiently dealt with. . However, if there is broad agreement that appropriately regulated mutual fund activity can play a large part in financial development in all its dimensions

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