CHAPTER 2

MUTUAL FUND INDUSTRY OVERVIEW

2.1 CONCEPT OF MUTUAL FUND

As defined by the Association of Mutual Funds in India (AMFI), an apex body of all registered asset management companies, “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 thousand rupees can invest in mutual fund units according to their stated investment objective and strategy.” According to Securities and Exchange Board of India (SEBI) Regulations 1996, “Mutual Fund means a fund established in the form of a trust to raise monies through the sale of its units to the public or a section of the public under one or more schemes for investing in securities, including money market instruments.” As defined by the mutual Fund Book of Investment Company Institute of the U.S., “A mutual fund is a financial service organization that receives money from shareholders, invests it, earns returns on it, attempts to make it grow and agrees to pay the shareholder for the current value of his investment.”

Mutual fund is a special type of institution that acts as an investment conduit. It is a professionally managed investment organisation that pools the money of many individual investors having similar investment objectives. The money thus collected is invested by the fund manager in different types of securities as shares, debentures, money market instruments and so on, depending upon the objective of the scheme. Income earned and capital appreciations thus realised by the schemes are shared by its unit holders in proportion to the number of units owned by them. Therefore, mutual fund is an investment institution, which assembles the savings of individuals and institutions and conduit these savings in corporate securities. Thus it endows the individual investors, with an opportunity to invest in a diversified, professionally managed portfolio at a relatively low cost.

Mutual funds mobilise savings, particularly from the small and household sectors, for investment in capital and money market. Basically, these institutions professionally manage the funds of individuals and institutions that may not have such high degree of expertise and
sufficient time to deal with the complexities of different investment avenues, legal provisions associated and impulse and vicissitude of financial markets. Figure 2.1 depicts its working.

![Mutual Fund operation flow chart](http://www.amfiindia.com/showhtml.aspx?page=mfconcept)

**Figure 2.1:** Mutual Fund operation flow chart


### 2.1.1 BENEFITS

Mutual funds have been endowed with many advantages over other forms and avenues of investment. Especially, investors having limited resources in terms of capital and ability to carry out detailed research and market monitoring, reward many benefits from these. Major advantages are listed below:

1. **Professional Management:** One of the most important benefits of the mutual fund investment is the availability of highly professional management services. Mutual funds are managed by professionally experienced and highly skilled managers, backed by a dedicated investment research team with sound knowledge of the market and wide experience in investment. Making investment is not a full time assignment for investors. So they cannot have a professional attitude towards it. The professional fund managers, who supervise the fund’s portfolio, take desirable decisions as which securities to be bought and sold and decisions for the timing of such buy and sell. They have extensive research facilities at their disposal to investigate and constantly supervise the fund. The performance of mutual fund schemes depends on the quality of fund managers employed.
ii. **Diversification:** Mutual Funds invest in a number of companies across a broad cross section of industries and sectors. This diversification reduces the risk because rarely do all stocks decline at the same time and in the same proportion. In this way, investors hold a diversified portfolio even with a small amount of investment that would otherwise requires a big amount of capital.

iii. **Convenient Administration:** Mutual Funds save time and make investing easy and convenient as investing in a Mutual Fund scheme reduces paperwork and helps to avoid many problems such as bad deliveries, delayed payments and unnecessary follow up with brokers and companies.

iv. **Return Potential:** Over a medium to long term, mutual funds have the potential to provide a high return as they invest in a diversified basket of selected securities.

v. **Low Costs:** Mutual Funds are a relatively less expensive mode of investment as compared to directly investing in the capital markets because of the benefits of scale in brokerage, custodial and other fees.

vi. **Liquidity:** Liquidity is a distinct advantage of mutual funds over other investment options as there is always a market for its units. For open-ended schemes, investors can always approach the fund for repurchase and get their money back promptly at Net Asset Value (NAV) related prices. With close-ended schemes, they can sell their units on a stock exchange at the prevailing market price or avail the facility of repurchase through Mutual Funds at NAV related prices which some close-ended and interval schemes offer to the investors periodically.

vii. **Transparency:** Investors get regular information on the value of their investment in addition to disclosure on the specific investments made by the scheme, the proportion invested in each class of assets and the fund manager’s investment strategy and outlook.

viii. **Flexibility:** Through features such as Systematic Investment Plans (SIP), Systematic Withdrawal Plans (SWP) and dividend reinvestment plans, one can systematically invest or withdraw funds according to his requirements and expediency.
ix. **Choice of Schemes:** Mutual Funds offer a variety of schemes to suit investors’ varying needs over a lifetime. Given the plethora of options at hand, investors can select schemes on the basis of their investment objectives as growth of capital, safety of principal, current income or tax-exempt income and risk spectrum.

x. **Well Regulated:** All Mutual Funds are registered with SEBI and they function within the provisions of strict regulations designed to protect the interests of investors. Also, their operations are monitored regularly by SEBI.

xi. **Switching:** Many mutual funds allow investors to switch from one fund to another. For example, if investor’s objective changes from capital gains to income, they can switch from growth to income funds and vice versa.

xii. **Attract Foreign Capital:** The functioning of mutual funds is not limited to domestic sphere only. In addition to attracting domestic savings, some funds offer their units abroad and attract foreign capital.

xiii. **Advantages to Industrial Concern:** Through mutual funds, needy industrial concerns avail a relatively bigger lot of capital. Therefore, it reduces their burden for raising finance directly from individual savers.

2.1.2. **ORGANISATION OF MUTUAL FUNDS**

In accordance with the provisions of the Indian Trust Act, 1882 every mutual fund shall be constituted in the form of a trust. SEBI Guidelines, 1992 spell out in clear terms the establishment norms for mutual funds. It contemplated a three tier system for managing the affairs of mutual funds. The three constituents are the sponsoring company, the trustees and the assets management company (AMC). These three constituents were incorporated in SEBI Regulations, 1996 for the management of mutual funds. Apart from these three, Custodians and transfer agents are two more important constituents of mutual funds. These are presented in the figure 2.2.

i. **SPONSOR**

Sponsor of a mutual fund is akin to the promoter of a company as he gets the fund registered with SEBI. Under SEBI regulations, sponsor is defined as any person who acting alone or in combination with another body corporate establishes the mutual fund. Sponsor can
be Indian companies, banks or financial institutions, foreign entities or a joint venture between two entities. As Reliance mutual fund has been sponsored fully by an Indian entity. Whereas, funds like Fidelity mutual fund and J P Morgan mutual fund are sponsored fully by foreign entities. ICICI Prudential mutual fund has been set up as a joint venture between ICICI Bank and Prudential plc. Both sponsors have contributed to the capital of the Asset Management Company of ICICI Prudential.

SEBI has laid down the eligibility criteria for sponsor as it should have a sound track record and at least five years experience in the financial services industry. SEBI ensures that sponsor should have professional competence, financial soundness and general reputation of fairness and integrity in business transactions. At least 40 percent of the capital of AMC has to be contributed by the sponsor. Also, they identify and appoint the trustees and Asset Management Company. Sponsors are also free to get incorporated an AMC as well as to appoint a board of trustees. They, either directly or acting through trustees, will appoint a custodian to hold the fund assets. To submit trust deed and draft of memorandum and articles of association of AMC to SEBI is also a duty of sponsor. After the mutual fund is registered, sponsors technically take a backseat.

ii. TRUSTEES

Under the Indian trust act 1882, a sponsor creates mutual fund trust, which is the main body in creation of mutual funds. Trustees may be appointed as an individual or as a trustee company with the prior approval of SEBI. As defined under the SEBI regulations, 1996, trustees mean board of trustees or Trustee Company who hold the property of mutual fund for the benefit of the unit holders. A Trustee acts as the protectors of the unit holders’ interests and is the primary guardians of the unit holders’ funds and assets. Sponsor executes and registers a trust deed in favour of trustees. There must be at least 4 members in the board of trustees and least two third of them need to be independent. For example, HDFC Trustee Company Limited is the Trustee of HDFC Mutual Fund vide the Trust deed dated June 8, 2000. It has five board members, of whom three are independent.

To ensure fair dealings, mutual fund regulations require that trustee of one mutual fund cannot be a trustee of another one, unless he is an independent trustee in both the cases, and has approval of both the boards. AMC, its directors or employees shall not act as trustees of any mutual fund. Trustees must be the person with experience in financial services and
every trustee should be a person of integrity, ability and standing. SEBI has also defined the rights and obligations of trustees. Under their rights, trustees appoint AMC with the prior approval of SEBI. They approve each of the schemes floated by AMC in consultation with the sponsors. They have the right to obtain from the AMC, such information as they consider necessary to fulfil their obligations.

Trustees can even dismiss AMC with the approval of the SEBI and in accordance with the regulations. Under their obligations, trustees must ensure that the transactions of mutual funds are in accordance with the trust deed and its activities are in compliance with SEBI regulations. They must ensure that AMC has all the procedures and systems in place, and that all the fund constituents are appointed. Also, they must ensure due diligence on the part of AMC in the appointment of business associates and constituents. Trustees must furnish to SEBI, on half-yearly basis a report on the activities of the AMC.

iii. ASSET MANAGEMENT COMPANY (AMC)

Asset Management Company is the body engaged to run the show of a mutual fund. The sponsor or trustees appoint AMC to manage the affairs of the mutual fund to ensure efficient management. SEBI desires that AMC must have a sound track record in terms of net worth, dividend paying capacity, profitability, general reputation and fairness in transactions. AMC is involved in basically three activities as portfolio management, investment analysis and financial administration. Therefore, the directors of AMC should be expert in these fields. SEBI’s regulation for AMC requires that it should have a net worth of at least Rs. 10 crore at all times and that a company can act as an AMC of one mutual fund only. Also, at least 50 percent of the members of the board of an AMC have to be independent and these can be the director of another AMC also. Its chairman should be an independent person.

AMCs can not engage in any business other than that of financial advisory and investment management. Its memorandum and articles of association have to be approved by the SEBI. Statutory disclosures regarding AMCs operations should be periodically submitted to SEBI. Prior approval of the trustees is required, before a person is appointed as a director on the board of AMC. An AMC cannot invest in its own schemes until it is disclosed in the offer document. Moreover in such investments, AMC will not be eligible for fees also. The appointment of an AMC can be terminated by the majority of trustees or by 75 percent of unit holders. Example: HDFC Asset Management Company Ltd. was approved by SEBI vide its
letter dated June 30, 2000 to act as an Asset Management Company of the HDFC mutual fund. In terms of investment management agreement, the trustee appointed this AMC. HDFC holds 60 percent of the capital and Standard Life Investments holds remaining 40 percent of the capital of the AMC. Its board has 12 members of whom 6 are independent.

Apart from three constituents discussed above, Custodians and transfer agents are another two important constituents of mutual funds. These have been discussed below.

iv. **CUSTODIAN**

SEBI requires that each mutual fund shall have a custodian who is independent and registered with it. SEBI regulations provide for the appointment of a custodian by trustees of the mutual fund who are responsible for carrying on the activities of safe keeping of securities and participating in any clearing system on behalf of mutual fund. Custodian is not permitted to act as a custodian of more than one mutual fund without the prior approval of SEBI. They should be independent of the sponsors. As for example, ICICI Bank is a sponsor of ICICI Prudential Mutual fund. It is also a custodian bank. But it cannot offer its services to ICICI Prudential Mutual fund, because it is a sponsor of this fund.

The appointment of any agency as custodian depends upon its track record, quality of services, experience, transparency, computerisation and other infrastructure facilities. Custodians primarily perform securities settlement functions. However, some also offer fund accounting and valuation services. The responsibilities of custodian include delivering and accepting securities and cash, to complete transactions made in the investment portfolio of mutual funds. Custodians also track and keep payouts and corporate actions such as bonus, rights, offer for sale, buy back offers, dividends, interest and redemption on the securities held by the fund. They also look after that the discrepancies and failure must be timely resolved.

v. **TRANSFER AGENT**

Registrar and transfer (R&T) agents are responsible for creating and maintaining investor records kept in numbered account called folios and servicing them. They accept and process investor transactions and also operate investor service centre (ISCs) which acts as an official points for accepting investor transactions with a fund. As for example, Computer Age Management Services (CAMS) is the R&T agent for HDFC mutual fund. R&T functions include issuing and redeeming the units and updating the unit capital account. R&T perform creating, maintaining and updating the investors’ records and enabling their transactions such
as redemption, purchase and switches. Banking the payment instruments such as drafts and cheques given by investors and notifying the AMC is also done by them. R&T send statutory and periodic information to investors and process payouts to investors in the form of dividends and redemptions.

![Organisation of Mutual Fund]

**Figure 2.2: Organisation of Mutual Fund**

**Source:** AMFI- organisation of mutual funds

### 2.2 TYPES OF MUTUAL FUNDS

A wide variety of mutual fund schemes exist according to their investment style that helps in meeting the financial goal of the investors. These are grouped into three broad categories i.e., their operations, investment objective and others.

#### 2.2.1. CLASSIFICATION BY OPERATIONS

On the basis of operations of mutual funds schemes, they have been classified into open-ended, close-ended and interval funds. These have been discussed below in detail.

i. **OPEN-ENDED FUNDS**

An open-ended fund offers its units to the investors for sale and repurchase at all the times at a price based on the net asset value (NAV) per unit. AMFI booklet has described NAV as the market value of the asset of the scheme minus its liabilities. It’s per unit value is obtained by dividing the amount of the market value of the fund’s assets (plus accrued income minus fund’s liabilities) by the number of units outstanding. Thus, the holders of the units in such funds can buy or redeem units from the fund itself at any time.
The corpus of these funds changes constantly as investors buy from or sell their units to the fund. Both the value and number of units fluctuate on a daily basis as the value of the securities and the number of investors change. The securities in the portfolio are valued at the end of each day. The value is then divided by number of units in the fund to arrive at a price per unit i.e. their net asset value. The advantages of this open ended structure are numerous as these funds are liquid, convenient, and easy to buy and sell for the investors. Axis Triple Advantage Fund, Birla Sun Life Basic Industries Fund, IDBI India Top 100 Equity Fund, L&T Contra Fund, Taurus Tax Shield, Templeton Floating Rate Income Fund, UTI - G-Sec Fund are some of the open ended mutual funds.

ii. CLOSE-ENDED FUNDS

Close-ended funds offer a fixed number of units for a fixed period of subscription to the investors as declared in their initial public offer (IPO). After subscription period is over, these funds do not allow investors to buy or redeem units directly from the fund house. However, many close-ended funds get themselves listed on stock exchange(s) and enable investors to buy or sell units of these schemes in the same fashion as for the shares of a company. The fund’s units may be traded above the NAV, called ‘selling at a premium’, or below, called ‘selling at a discount’.

The trading price depends upon a variety of things, as supply and demand and the market’s perception of the fund’s prospects, much like the price of a stock. Some close-ended funds provide an exit route to the investors by giving an option of selling back the units to the mutual fund through periodic repurchase at NAV related prices. SEBI Regulations stipulate that at least one of the two exit routes is provided to the investor i.e. either through listing on stock exchanges or repurchase facility. These mutual funds schemes disclose NAV generally on weekly basis. Canara Robeco Equity Tax Saver-93, DSP Merrill Lynch Tax Saver Fund, Tata Life Sciences and Technology Fund, JM Arbitrage Advantage Fund, Kotak Gold ETF are some of the close ended funds in India.

iii. INTERVAL FUNDS

These embrace the features of both open-ended and close-ended funds. These funds may be traded on stock exchange or may be open for sale or redemption during predetermined intervals at NAV related prices. Legally, interval funds are classified as closed-end funds, but they are very different from traditional closed-end funds in two ways. First, their shares
typically do not trade on the secondary market. Instead, their shares are subject to periodic repurchase offers by the fund at a price based on net asset value. Second, they are permitted to continuously offer their shares at a price based on the fund’s net asset value. An interval fund will make periodic repurchase offers to its shareholders, generally every three, six, or twelve months, as disclosed in the fund’s prospectus and annual report.

The price that shareholders will receive on a repurchase will be based on NAV per share determined as of a specified (and disclosed) date. Interval funds are permitted to deduct a redemption fee from the repurchase proceeds, not to exceed 2 percent of the proceeds. Fee is paid to the fund to compensate for its expenses directly related to repurchase. Interval funds may charge other fees as well. Interval funds are regulated under the Investment Company Act of 1940 and the rules adopted under that Act, in particular Rule 23C-3. These funds are also subject to the Securities Act of 1933 and the Securities Exchange Act of 1934. Reliance interval fund, Taurus quarterly interval fund-series 1, ICICI-Pru’s Interval Fund II are some of the intervals funds in India.

2.2.2 CLASSIFICATION BY INVESTMENT OBJECTIVES

In this category, funds differ significantly with one another with respect to their objectives and the type of securities, comprising their portfolio. Therefore, these funds cater to the risk and return profile of different type of investors. The following are the portfolio classification of these funds:

i. GROWTH FUND

The objective of a growth fund is to achieve capital appreciation over 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. Around 80-90 percent of corpus of these funds is invested in equity and equity linked instruments and the balance in debt and money market securities. These schemes are not for investors seeking regular income or needing their money back in the short term but are suitable for long term investors seeking capital appreciation and ready to bear a medium to high level of risk. These are also known as “nest eggs” or “long haul” investments. BNP PARIBAS Equity Fund, Canara Robeco emerging equities, DWS Investment Opportunity Fund, Fidelity Equity Fund, HSBC Dynamic Fund, Quantum Long-Term Equity Fund are some examples of growth mutual funds in India.
ii. **BALANCED FUNDS**

The aim of the balanced funds is to provide both capital appreciation and periodic returns over a long period of time. These funds have reasonable mix of equity and bond in their portfolio by investing both in shares and fixed income securities in the proportion as indicated in their offer documents.

Normally a balanced fund invests 60 percent out of its net assets in equity and 40 percent in fixed income securities, money market instruments and cash. Their risk profile is medium to high. These are also called “income–cum–growth” funds and are ideal for investors seeking for a combination of regular income and moderate growth. HDFC Balanced Fund, UTI Balanced Fund, Tata Balanced Funds are some of the examples of these funds in India.

iii. **INCOME FUND**

Income funds provide regular and steady income to its investors. These funds generally invests in fixed income securities such as government securities, bonds, corporate debentures, money market instruments, cash and cash equivalent while at the same time maintains a small exposure to the equity markets. Such funds are less risky as compared to equity schemes as they are not affected by the fluctuations in equity markets. Risk profile of income funds is generally from low to medium however, opportunities of capital appreciation are also limited.

These funds are ideal for investors who need some income to supplement their earnings as retired people and others with a need for capital stability and regular income. NAV of such funds are affected because of the change in interest rates in the country. If the interest rates fall, NAV of such funds are likely to increase in the short run and vice versa. Some of the examples of Indian income mutual funds are IDFC Capital Protection Oriented Fund, Kotak Hybrid Fixed Term Plan, Reliance Fixed Horizon Fund, SBI Capital Protection Oriented Fund etc.

iv. **MONEY MARKET/LIQUID FUNDS**

Money market mutual funds provide easy liquidity, preservation of capital and moderate income by investing in safer short term instruments such as treasury bills (T-bills), certificates of deposits, commercial papers and interbank call money. These funds provide
high liquidity on low risk. Returns on these schemes fluctuate according to the interest rates prevailing in the market. Money market funds are ideal for corporate as well as individual investors as a means to park their surplus funds for short periods or awaiting a more favourable investment alternative. AIG India Liquid Fund, DSP Black Rock Liquidity Fund, ICICI Prudential Liquid Plan, Tata Money Market Fund and UTI Money Market fund are some of the examples of these funds.

v. GILT FUNDS

Gilt funds, as conveniently called are mutual fund schemes dedicated exclusively to investments in government securities. Government securities mean and include central government dated securities, state government securities and treasury bills. These funds endow with the investors, safety of their investments made in government securities and reaps better returns than direct investments in these securities through investing in a variety of government securities yielding varying rate of returns. The first gilt fund in India was set up in December 1998. Gilt funds can be both short term and long term, and depending on their investment horizon, investors can choose between them.

These are ideal for those investors who are risk-averse, and at the same time, are looking for reasonable returns on their money. Gilt funds are a good option when interest rates are not expected to go up. However, these funds are not completely risk free because there is an inverse relationship between bond prices and interest rates. With the rise in interest rate, prices of government securities fall which adversely impacts the performance of gilt funds. Typically it is noticed that, higher the fund’s average maturity, higher the volatility. Advantages of gilt funds are many. As these funds are backed by government, therefore, these possess less credit risk. These funds provide retail investors a low-cost way to invest in G-sec, which otherwise was open only to large players. Also investment in Gilt funds provides for effective diversification. Baroda Pioneer Gilt Fund, IDFC GSF- Provident Fund, LIC NOMURA MF Govt Securities Fund-PF Plan, Taurus Gilt Fund and UTI - Gilt Advantage-Long Term are some of the gilt funds in India.

vi. FLOATING RATE FUND

These are the Debt mutual funds investing about 75 to 100 percent in securities such as bank loans, bonds and other debt securities that pay a floating rate interest, while the rest in fixed income securities. Floating rate funds are of two types as long term and short term. The
portfolio of the short-term fund plan is normally skewed towards short-term maturities with higher liquidity whereas the portfolio of long-term plan is skewed towards longer-term maturities however they are positioned more on the lines of short-term funds and are not very aggressive in nature.

Floating Rate securities are different from traditional bonds as most bonds have fixed interest rates which are set when they are first issued, either by a government or a corporation. That rate of interest doesn’t change for the life of the bond. Whereas, a floating rate security, has a variable interest rate that will go up and down, or “float” to reflect changes in current market rates. Depending on the particular floating rate security, the interest rate may change daily, monthly, quarterly, annually, or at another specified interval. These funds provide low but stable returns. Birla Sun Life Floating Rate-Long Term Plan, Reliance Floating Rate-Short Term Plan, LIC Nomura Floating Rate Fund is some of its examples.

vii. CASH OR TREASURY MANAGEMENT FUNDS

These funds are very similar to a liquid fund and invest predominantly in money market securities. They chose instruments with tenure of up to 364 days and may also have some exposure to longer term debt securities. Both the yield provided and the risk associated with these funds is slightly higher than the liquid funds. NAV of these funds also tend to be stable due to their focus on very short term debt, where the market to market changes tend to be low. DSP Chola Treasury Management Fund, Templeton Treasury Management fund, Tata Treasury Management Fund are some of their examples.

viii. HIGH YIELD DEBT FUNDS

High yield debt funds seek higher interest income by investing in debt instruments having lower credit ratings and therefore, higher risk of default. Lower the credit rating, higher the interest a borrower pays. These funds are also called “Junk bond funds” and are popular abroad, but not prevalent in India. Some of the high yield bond funds are ING Pioneer High Yield Adv, Fidelity Capital & Income Fund, Credit Suisse High Yield, Wells Fargo Advantage Strategic etc.

ix. FIXED MATURITY PLANS (FMP)

Fixed Maturity Plans (FMPs) are the passively managed close ended mutual fund schemes in which the portfolio is held till the maturity of the assets it has invested in. FMPs
invest in debt instruments mainly as certificate of deposits and commercial papers, whose maturity matches the maturity of the schemes. For example, if FMP is of one year duration, the maturity of bonds and debt it holds will also be exactly of one year. Debt securities are redeemed on maturity and paid to the investors. The minimum investment amount is usually Rs 5,000. FMPs vary between 30 days and five year. They are issued in a series, one fund opening after another has matured, or as interval fund. FMPs offer many benefits to investors as low sensitivity to interest rates, tax efficiency and fixed tenure.

They have less risk of capital loss than equity funds due to their investment in debt and money market instruments. Low interest rate sensitivity is there. As the securities are held till maturity, FMPs are not affected by interest rate volatility. The actual returns are more or less close to the indicative returns declared at the scheme's launch. FMPs carry lower cost because of minimum expenditure on fund management, as there is no requirement for a time-to-time review by fund managers to buy or sell instruments constituting the fund. Since these instruments are held till maturity, there is a cost saving in respect of buying and selling of instruments. FMPs score over fixed deposits because of their tax efficiencies both in the short-term as well in the long-term. They are similar to Fixed Deposits, but carry lower liquidity and give superior tax advantage over them. Some of the FMPs in India are ICICI Prudential Fixed Maturity Plan, Reliance Fixed Maturity Plan, Tata Fixed Maturity Plan and SBI Fixed Maturity Plan.

x. MONTHLY INCOME PLANS (MIP)

The primary objective of monthly income plan is to generate regular income for the investors. For fulfilling this purpose, these funds invest in fixed income securities so as to make monthly payment or distribution to its unit holders. Their secondary objective is growth of capital that is fulfilled through investments in equity. MIP is a marginal equity product, which works for conservative investors who are comfortable in investing a small component of their money in equity. These funds invest a very small portion of their investment in stocks as well and the rest is being invested in high-quality fixed income instruments. MIP is a good solution for those who cannot invest in two different schemes, a bond fund and an equity fund separately on their own and rebalance their portfolio regularly as these funds not only gets the asset mix right but also rebalances the portfolio from time to time. The risk profile of these funds is low to medium. DSP Black Rock Monthly Income Plan, HDFC Monthly Income
Plan, IDFC Monthly Income Plan, Reliance Monthly Income Plan are some of the examples of MIP funds in India.

xi. SECTOR FUNDS

Sector funds invest in a specified sector of the economy or in a specified industry only as information technology, oil and gas companies or in specified products. They carry the risk and return associated with these industries. Major disadvantage from investment in these funds is that being sector specific, they lack in diversification and their risk profile is also high. Sector funds are suitable for investors who have already decided to invest in a particular sector or segment. Baroda Pioneer Banking and Financial Services Fund, Reliance Media and Entertainment fund, SBI Magnum Sector Funds Umbrella–Pharma, JM Telecom Sector Fund, UTI Auto Sector Fund are some of the sector funds in India.

2.2.3. OTHERS

There are some other types of mutual funds also apart from the above stated classification. These have been discussed below in detail.

i. INDEX FUNDS

The objective of index funds is to generate capital commensurate with the index it tracks. This is done by investing in all the stocks comprising the index in approximately the same weightage that they represent in the specific index. For example, a fund that tracks the BSE Sensitive Index will invest in the same 30 securities of the index and in the same proportion. Portfolio of these funds appreciates or deprecates in more or less the same way as index they have been following. Index funds are suitable for investors, looking for a return approximately equal to that of an index. Goldman Sachs Nifty BeES 1, HDFC Index Fund - Sensex Plus Plan, IDFC Nifty Fund–Growth, Reliance Index Fund-Nifty Plan, LIC Nomura MF Index Fund-Nifty Plan, ICICI Prudential Index Fund, Tata Index Fund-Nifty Plan are some of the index funds in India.

ii. TAX SAVING FUNDS

Tax Saving Funds in India offer rebates in taxes to its investors under the Income Tax Act, Section 88. They are also known as equity-linked savings schemes (ELSS). Tax Saving Funds in India usually carry a lock-in-period of three years. Therefore, these funds are not
concerned about factors such as the pressures of redemption, performance during a short time etc. and thus keep in view the long term goal. Fund manager of the Tax Saving Funds in India invests money in instruments that are related to equity.

Tax Saving Funds are suitable for those investors who want to increase their investments and also want to get benefit from rebates in taxes. Major advantage of these funds is that they grant its investors an opportunity to make investments in an avenue that is market-linked and at the same time claim benefits in taxes. The dividends earned in Tax Saving Funds are tax free. Some of the major Tax Saving Funds in India are, Franklin India Tax Shield, HDFC Tax Saver, Sundaram Tax Saver, HDFC Long Term Advantage, Prudential ICICI Tax Plan, Birla Equity Plan, UTI Equity Tax Savings, Tata Tax Saving Fund, and Magnum Tax Gain.

iii. **EXCHANGE TRADED FUND (ETF)**

An exchange traded fund is an open ended fund that tracks an index like an index fund, but trades like a stock on an exchange just like the shares of an individual company. Unlike the share of a company, each unit of an ETF represents a portfolio of stocks. Therefore, these funds are similar to a unit of an open-ended mutual fund but with a big difference.

The difference between an ETF and an open-ended mutual fund is that the units of an ETF trade on an exchange and therefore, the investor can trade in it during market hours and the units can be sold short or margined just like shares. Another difference is the type of management. Mutual funds employ an active management strategy wherein the fund manager chooses portfolio of stocks and manages them in an endeavour to outperform the fund's benchmark.

However, ETFs employ a passive management strategy because they are designed to closely track the performance of a specific index. ETFs experience price changes throughout the day as they are bought and sold on exchange. These funds first came into existence in the USA in 1993. The first ETF in India, Nifty BeES, was launched by Benchmark Mutual Fund, on January 8, 2002, which tracks the S&P CNX Nifty. Nifty Junior Benchmark Exchange Traded Scheme-Juniorbees, ICICI Prudential Mutual Fund-Sensex Fund-Spice, Kotak Sensex ETF, Quantum Index Fund–Qnifty, Reliance Banking Exchange Traded Fund – Relbank are some of the Exchange Traded Funds in India.
iv. GOLD EXCHANGE TRADED FUNDS

Gold ETFs are exchange traded funds that are meant to track closely the price of physical gold. Each unit of the ETF lets the investor own 1 gm of gold without physically owning it. Thus investing in a gold ETF provides the benefit of liquidity and marketability which are a limitation of owning physical gold. Gold ETF is highly liquid because these can be traded at any time during market hours. Gold ETF is marketable as investors can trade any amount in it just like a normal stock including short selling and buying on margin. Owning gold ETF is cheaper also than owning physical gold because it has no carrying cost as the cost of storing physical gold. Country’s first GETF was launched by Benchmark mutual fund as Gold BeES on February 1, 2007. This mutual fund was an open ended fund that would track domestic prices of gold through investments in physical gold. Some of the Gold Exchange Traded Funds in India are Axis Mutual Fund-Axis Gold ETF, Gold Benchmark Exchange Traded Scheme, Birla Sun Life Gold ETF, HDFC Gold Exchange Traded Fund, ICICI Prudential Gold Exchange Traded Fund, KOTAK Gold ETF, Quantum Gold Fund, Reliance Gold Exchange Traded Fund, Religare Gold Exchange Traded Fund, SBI Gold Exchange Traded Fund, UTI Gold Exchange Traded Fund.

v. FUND OF FUND (FoF)

A Fund of Fund invests in other funds. Its portfolio is not made up of securities but of other mutual funds, selected to serve a given investment objective. A fund of funds allows investors to achieve a broad diversification and an appropriate asset allocation with investments in a variety of fund categories all wrapped up into one fund. However, if the fund of funds carries an operating expense, investors may have to bear double for an expense that is already included in the expense figures of the underlying funds. Some fund of funds may invest in other mutual funds, not necessarily from the same fund house. These are called ‘Multi-Manager Fund’. Prudential ICICI was the first to introduce FoFs in India in November 2003 (SEBI Annual Report 2003–04 and Bhole, 2005) [18]. Birla Sun Life Asset Allocation Fund, Fidelity Multi Manager Cash Fund, ICICI Prudential Advisor Series, Quantum Equity Fund of Funds are some of their examples in India.

vi. QUANTITATIVE FUNDS

A quantitative fund is an investment fund that selects securities based on quantitative analysis. The managers of such funds employ a very scientific approach to investments using
a computer program that is backed by investing formulas based on historical data of price-to-earnings, price-to-book, company financials and other market parameters observed in the past 10-15 years. In this way it is determined, whether or not an investment is attractive and the final decision to buy or sell is made by the model. However, there is a middle ground where the fund manager uses human judgment in addition to a quantitative model.

Quant based investing strategy is considered as emotion-free. The first Quant based Mutual Fund Scheme in India, Lotus Agile Fund opened for subscription on October 25, 2007. At present, eight quant based mutual funds are available in India. Out of these, four funds i.e., Reliance Quant plus, Religare AGILE, Canara Robeco Large Cap Plus and Edelweiss Absolute Return belong to equity oriented category, Religare AGILE tax belongs to ELSS category, Motilal Oswal MOSt Shares M50 ETF, Motilal Oswal MoSt Shares Midcap 100 ETF and Motilal Oswal MoSt Shares NASDAQ-100 ETF are Exchange Traded Funds. These fund houses have own proprietary models based on the parameters they choose.

vii. ASSURED RETURN SCHEME FUNDS

Assured return schemes are those schemes that assure a specific return to its unit holders irrespective of performance of the scheme. A scheme cannot promise returns unless such returns are fully guaranteed by the sponsor or AMC and the schemes disclose the same in their offer document. Investors should carefully read the offer document whether return is assured for the entire period of the scheme or only for a certain period. Some schemes assure returns for one year and then after review change it at the beginning of the next year.

viii. CAPITAL PROTECTION ORIENTED

Capital protection oriented funds bestow its investors with the best of both worlds. These closed-ended debt funds invest a big chunk of their money in fixed income instruments and the balance is being invested in equities. These funds are suitable for investors who want to protect the downside risk and capture the upside in equities with a three-year perspective. One of the best features of capital-protection-oriented mutual funds is that they enable risk-averse investors to gain exposure of equities. In developed countries, such funds offer capital guarantee with some upside participation whereas, in India, these are closed-end funds that offer capital protection, without a guarantee. Axis Capital Protection Oriented Fund, Birla Sun Life Capital Protection Oriented Fund, JP Morgan India Capital Protection Oriented
Fund, Tata Capital Protection Oriented Fund, Sundaram Capital Protection Oriented Fund are some of the examples of these funds in India.

ix. ARBITRAGE FUNDS

Arbitrage funds are a niche category which tries to take advantage of the price difference between cash and futures derivatives markets for generating returns. For example a fund may purchase equity shares in the cash market and simultaneously sell the same in the futures market. Return is based on the difference in prices for same security in the two markets. The ability of these funds to generate higher returns depends on the volatility in equity markets- higher the better. Or, in other words, Arbitrage opportunities to be exploited depend upon the extent of volatility in the equity market as the higher volatility leads to the higher returns. As arbitrage funds predominantly invest in equities, they are treated at par with other equity funds for tax treatment. These funds are suitable for risk-averse investors as a relatively safer option within equities. Arbitrage funds have a low risk-return trade-off and generate moderate returns. The first arbitrage fund of the Indian mutual fund industry, launched in December 2004, was the Benchmark Derivative Fund. HDFC Arbitrage Fund, Kotak Equity Arbitrage Fund, Religare Arbitrage Fund, SBI Arbitrage opportunities Fund are some of their examples.

x. INTERNATIONAL FUNDS

International funds invest in securities internationally around the globe i.e., in foreign market instead of domestic market. These funds are more volatile as compared to the investments made in domestic funds. Also, they diversify the portfolio to a greater extent and ensure higher return as compared to the domestic market. These funds are suitable for aggressive investors who want international exposure and are ready to take higher amount of risk. Some international mutual funds in India are Franklin Asian Equity, Hang Seng BeES China, JP Morgan JF Greater China Equity Off-shore, Mirae Asset China Advantage, DSPBR World Mining Fund, ING OptiMix Global Commodities, Mirae Asset Global Commodity Stocks, HSBC Emerging Markets, Tata Growing Economies Infrastructure Plan A.

xi. REGIONAL MUTUAL FUNDS

Regional mutual funds confine their investment to a specific geographical area. Usually, those mutual funds which invest inside their own country or local funds are called as
regional funds. The main objective of these funds is to contribute towards the financial
growth of specific area or otherwise to improve the capital market in a specific geographical
area. These funds provide an advantage to its investors by carrying lesser cost and lower risk.

Regional mutual funds are different from international funds as in international funds, money is being invested in schemes or securities all over the world and they are global investments. On the other hand, in case of regional funds, investment pertains to a specific region only. Regional funds are lesser diversified than international funds and hence carry higher volatility. However, the risk factor is also less in regional funds because of the absence of exchange rate differences.

xii. LOAD/NO–LOAD FUNDS

A Load Fund is one that charges a percentage of NAV for entry in to or exit from these funds. That is, investors pay a charge each time they buy or sell units in the fund. This charge is used by the mutual fund for marketing and distribution expenses. For example, suppose the NAV per unit is Rs. 10. If the entry as well as exit load is 1%, then the investors who buy would be required to pay Rs. 10.10 and those who offer their units for repurchase to the mutual fund will get only Rs. 9.90 per unit. Load charges must be taken into consideration while making investment as these affect the yields/returns. A no-load fund is one that does not charge for entry or exit. It means the investors can enter the fund/scheme at NAV and no additional charges are payable on purchase or sale of its units.

xiii. LIFESTYLE FUNDS

The asset mix of these funds is determined by the level of risk and return that is appropriate for an individual investor. Several factors as investor’s age, risk appetite, investment purpose and the time duration of investment, determine the asset mix. The objective of lifestyle funds is to provide long term capital appreciation and/or income distribution from a diversified portfolio of equity and equity related instruments. Birla India Gennext Fund was the first lifestyle fund in India launched in June 2005. Kotak Lifestyle Fund and UTI India Lifestyle Fund are some of the lifestyle fund in India.

2.3 ATTRIBUTES OF MUTUAL FUND

In the past literature it has been found that there are various mutual fund characteristics that influence their performance. These characteristics have been called as the
attributes of mutual funds. Finance professionals and journalists frequently claim that various fund attributes are useful devices to either select the top-performing funds or eliminate the worst performers [124]. These attributes are of paramount importance and have been discussed in this section.

i. **PAST PERFORMANCE**

Past performance tells about the performance of the mutual fund in the past time periods. It is measured by the return through Net Asset Value (NAV) of the mutual fund. The NAV and its calculation have been described in detail in later sections.

ii. **ASSET SIZE**

Asset size of a mutual fund is the total market value of all the securities held in its portfolio. AMFI has described it by the Asset under Management of the mutual funds.

iii. **EXPENSE RATIO**

Total expenses of the mutual funds are divided into three components as management fees, marketing and distribution fees and other expenses including securities custodian fees, transfer agent fees, shareholder accounting expenses, auditor fees, legal fees and independent direct fees [82]. These total expenses divided by the fund average net assets is its expense ratio. As described by the Centre for Research and Security Prices (CRSP), it is the ratio of fund’s operating expenses paid by shareholders to the total investment.

iv. **LOAD STATUS**

Investment in mutual funds costs load fee to the investors. AMFI has described two types of load fee. One is entry load and second is the exit load. Entry load is the charge collected by a scheme when it sells the units. It is also called as ‘sales load’ or ‘Front-end load’. Exit load is the charge collected by a scheme when it buys back its units from the unit holders. It is also called as the ‘repurchase’ or ‘back–end’ load. SEBI has abolished entry load from all mutual fund schemes in India with effect from 1 August 2009.

v. **INVESTMENT STYLE**

Mutual fund schemes possess specific investment styles on the basis of their investment objectives like equity funds for growth of capital, income funds for regular
income, balanced funds for a balanced combination of regular income and growth and liquid funds for liquidity. It has also been classified on the basis of their functions as open ended, close ended etc. This has been discussed above in detail in section 2.3.

vi. RISK

Investment is always associated with some risk. Risk involved in the investment of some mutual fund scheme is being measured as the deviation in actual return from the expected one. Mutual fund’s risk is calculated in two ways. One is the total risk measured by the standard deviation (σ) and the other is the systematic risk measured by the beta (β). Concept of these two type of risk along with their computation has been discussed in detail in chapter 3.

vii. AGE OF THE MUTUAL FUND SCHEME

Past literature has considered age of the mutual fund as an attribute that affect their return performance because of the economies of experience. Age of the mutual fund schemes at any particular time is determined by the time period since their inception date.

2.4 ORIGIN AND GROWTH OF MUTUAL FUNDS

Mutual fund originated in the western countries. First mutual fund named, ‘Foreign and Colonial Government Trust’ was set up in United Kingdom (U.K.) in 1868. This trust was established to spread risk for investors over large number of securities. In U.S. the idea took root in the beginning of the 20th century and in 1924, first open-ended investment company was formed. A major setback for U.S.A. mutual funds was stock market crash of 1929. Enactment of the Securities and Exchange Commission (SEC) in 1933 and the investment Company Act in 1940 led to the recovery and regulation of mutual funds in the U.S.A. [32]. The post World War-II period witnessed a boost in mutual funds as people not having the knowledge of how to invest on their own and with the expectation to reap the benefit of economic growth flocked to mutual funds. In Canada, during the decade of 1920 many close ended investment companies were organised which were generally known as investment trusts. The first mutual fund in Canada to issue its share to general public was the Canadian Investment Fund in 1932. In recent years, mutual funds in Japan and Far East countries have been showing excellent performance. Countries in pacific area like Hong Kong, Thailand, Singapore and Korea have also entered this field long way. Netherlands and Mauritius are
emerging as tax havens for off-shore mutual funds. Thus, mutual funds culture is now global in scope [10].

In India, concept of mutual funds took root in 1963 with the formation of UTI mutual fund at the initiative of Government of India and Reserve Bank of India (RBI). In the year 1992, SEBI act was passed. The SEBI commend mainly three statutory objectives as: (a) to protect the interest of investors in securities; (b) to regulate the securities market; (c) to promote the development of securities market [44]. For mutual funds, SEBI formulates policies and regulates them to protect the interest of investors. First mutual fund regulations were notified by SEBI in 1993, which were then fully revised in 1996 and have been amended thereafter from time to time. As per AMFI, the history and growth of mutual funds in India can be broadly divided in to four phases as discussed below:

i. First Phase: 1964–87 (Monopoly of UTI)

ii. Second Phase: 1987–93 (Entry of Public sector Mutual Funds)

iii. Third Phase: 1993–2003 (Entry of Private sector Mutual Funds)

iv. Fourth Phase: since February 2003

2.4.1. FIRST PHASE: 1964–87 (MONOPOLY OF UTI)

UTI was established in 1963 through an act of parliament. It was set up by RBI and functioned under its regulatory and administrative control. In 1978, UTI was delinked from RBI and the Industrial Development Bank of India (IDBI) took over the regulatory and administrative control in place of RBI. The first scheme launched under UTI was Unit Scheme 64 in June 1964. After Unit Scheme 64, between 1971 and 1987, UTI introduced seven more schemes targeted for different segments of the investor. The asset under management of UTI had increased from Rs. 246.7 million in 1964-65 to Rs. 45,636.8 million in 1986-87.4

2.4.2. SECOND PHASE: 1987–93 (ENTRY OF PUBLIC SECTOR MUTUAL FUNDS)

The monopoly of UTI came to an end in 1987 when Government of India permitted commercial banks in public sector to set up subsidiaries operating as trusts to perform the

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4 Source: http://www.amfiindia.com
functions of mutual funds. The first non-UTI mutual fund was State Bank of India Mutual Fund established in June, 1987 followed by Canbank Mutual Fund (Dec., 1987), Punjab National Bank Mutual Fund (Aug., 1989), Indian Bank Mutual Fund (Nov., 1989), Bank of India Mutual Fund (June, 1990), Bank of Baroda Mutual Fund (Oct., 1992). Life Insurance Corporation of India (LIC), established its mutual fund in June 1989 while General Insurance Corporation of India (GIC), had set up its mutual fund in December 1990. These mutual funds enlarged the investor community and investible funds. From 1987 to 1992-93, Indian mutual fund industry expanded seven times in terms of asset under management. At the end of 1993, the mutual fund industry had assets under management of Rs. 4,70,040 millions.5

Surprisingly, there were no rules or guidelines at that time when these institutions appeared in the market with various products. Also, these institutions started offering assured returns on the mutual fund schemes and soon this created a race among mutual funds to surpass each other in offering assured returns. With this trend, investors started perceiving mutual funds as an alternative to bank deposits. This led to intervention by RBI and it issued first set of guidelines in July, 1989, for the orderly functioning of the mutual funds. Some of the important aspects of RBI guidelines were constitution and management of the mutual fund, their investment objectives and policies, pricing policy, income distribution, statement of accounts and disclosures. However, these guidelines were applicable only to mutual funds established by public sector banks and not to others.

The Abid Hussain Committee on capital markets emphasized need for strengthening the regulatory framework for mutual funds and also recommended for setting up of joint sector mutual funds [79]. Thus, the Ministry of Finance, Government of India, issued another set of guidelines in June, 1990, similar to those issued earlier by RBI, to give a healthy outfit of mutual fund functioning. In March, 1991, Government of India handed over the function of regulating mutual funds to SEBI. Then all the existing mutual funds were directed by SEBI to make their disclosures in two sets. One set for the investors and another for the SEBI. In October, 1991, SEBI issued guidelines for the formation of AMC. In this way, a two tier structure was developed for mutual funds-one being trust and other AMC. In February, 1992, on the recommendation of Dave committee, Government of India announced a comprehensive set of guidelines for the operation of mutual funds in order to safeguard the interest of investors and to encourage the growth of capital markets. Further, the Government

5Source: [http://www.amfiindia.com]
also decided to extend the industry of mutual funds to the private and joint sectors. In February, 1992, the Union Finance Ministry allowed the private sector to float mutual funds as declared by the Finance Minister in his 1991-92 budget speech. Consequently, SEBI issued guidelines for establishing private sector mutual funds which were further improved in SEBI (Mutual Funds) Regulations 1993.

2.4.3. THIRD PHASE: 1993-2003 (ENTRY OF PRIVATE SECTOR MUTUAL FUNDS)

A new era started in Indian Mutual Fund industry with the entry of private sector funds in 1993, which provided Indian investors a wider choice of fund families. Also, this was the year in which 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. Introduction of private sector mutual funds also opened a way for foreign asset management companies to set up joint venture with domestic mutual funds. The period of rapid expansion of mutual funds was also marked by a decline in stock prices. The market conditions resulted in an attrition of NAVs. The discounts on the prices of quoted schemes to NAVs widened. Investors’ confidence suffered and their perception became poor [99]. Besides legality and ethics, profitability as well as performance of mutual funds started eroding. On sight inspections and close monitoring of mutual funds by SEBI brought to light several abuses, common violations of regulations and unhealthy business relations and thus, the regulations promulgated in 1993 proved to be ineffective. Responding to these concerns, SEBI undertook the mutual fund 2000 study to develop mutual funds into vibrant and effective investment vehicle. The study made far reaching recommendations and SEBI came out with new regulations i.e., the SEBI Regulations 1996 to replace the regulations of 1993 [10].

SEBI (Mutual Fund) Regulations, 1996 were issued under S.O. No. 865 (E) dated December 6, 1996 published in the Gazette of India, Part II, Section 3 (II), dated December 9 1996. These regulations were further amended from time to time and set uniform standards for all funds. Similarly, Union Government budget of 1999 took a big step in exempting all mutual fund dividends from income tax in the hands of investors. Both the SEBI Regulations 1996 and the Union Budget of 1999 had a far reaching impact on mutual funds industry and
its investors\(^6\). Also, year 1999 marked the beginning of a new phase in the history of mutual funds in India, a phase of significant growth in terms of both amounts mobilised by the investors and asset under management. Amount mobilised increased from Rs. 2,13,770 million in 1998-99 to Rs. 5,97,480 million in 1999-2000 and asset under management also had increased from Rs. 6,84,720 million in 1998-99 to Rs. 11,30,050 million in 1999-2000 (AMFI Mutual Fund Test Workbook, 2001). The number of mutual fund houses went on increasing, with many foreign mutual funds setting up funds in India. Industry has also witnessed several mergers and acquisitions in this time period. At the end of January 2003, there were 33 mutual funds with total assets of Rs. 1,21,8050 millions. The Unit Trust of India with Rs. 44,5410 millions of assets under management was still a way ahead of other mutual funds\(^7\).

**2.4.4. 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 was the Specified Undertaking of the Unit Trust of India with assets under management of Rs. 29,8350 millions as at the end of January 2003. The second was UTI Mutual Fund, sponsored by SBI, PNB, BOB and LIC. It has been registered with SEBI and functions under the Mutual Fund Regulations. With this, the current phase of consolidation and growth of Indian mutual fund industry had started. Indian mutual fund industry has witnessed impressive growth with their number of schemes increasing from 1 in 1964 to 1309 in 2012 (figure 2.3), with 44 players i.e., mutual fund companies in the market. The total assets under management had also increased from Rs. 250 million in March, 1965 to Rs. 66,47,920 million in March, 2012 (figure 2.4).

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\(^6\) Source: AMFI Mutual Fund Test Workbook, 2001  
Figure 2.3: Growth in No. of Schemes during four phases of Indian mutual fund industry

Source: AMFI Publications

Figure 2.4: Growth in Asset under Management during four phases of Indian mutual fund industry

Source: AMFI- History of Indian Mutual Fund Industry
The schemes of mutual funds have now become more diverse in nature and offer a wide array of choices to the investors. A number of innovative schemes launched by the mutual fund houses have given investors an option to choose funds, which suits their investment needs the best. Introduction of pioneering schemes like Exchange Traded Funds, Gold Exchange Traded Funds, Global Funds, Lifestyle funds, arbitrage funds, index funds, fund of fund and so on had galvanised the industry growth with 1,309 schemes (Table 2.1) which manages a total of Rs. 66,47,920 million as assets under management at the end of March 2012 (Table 2.2).

2.5 LEGAL AND REGULATORY ENVIRONMENT

The legal and regulatory framework governing mutual fund industry is broadly classified under two heads:

i. Regulatory Bodies/ Agencies involved in regulating various elements of the mutual fund industry

ii. The specific provisions that seek the protection of investor interests.

Table 2.1: Number of Mutual Fund Schemes as on 31st March 2012

<table>
<thead>
<tr>
<th>Mutual Fund Scheme</th>
<th>Open End</th>
<th></th>
<th>Close End</th>
<th></th>
<th>TOTAL</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No. of Schemes</td>
<td>Amount (Rs. Millions)</td>
<td>No. of Schemes</td>
<td>Amount (Rs. Millions)</td>
<td>No. of Schemes</td>
<td>Amount (Rs. Millions)</td>
</tr>
<tr>
<td>Income</td>
<td>229</td>
<td>5,32,470</td>
<td>512</td>
<td>4,14,130</td>
<td>775</td>
<td>9,67,240</td>
</tr>
<tr>
<td>Income (Interval Funds)</td>
<td></td>
<td>34</td>
<td></td>
<td>20,640</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity</td>
<td>299</td>
<td>43,370</td>
<td>4</td>
<td>-</td>
<td>303</td>
<td>43,370</td>
</tr>
<tr>
<td>Balanced</td>
<td>29</td>
<td>5,900</td>
<td>1</td>
<td>-</td>
<td>30</td>
<td>5,900</td>
</tr>
<tr>
<td>Liquid/Money Market</td>
<td>55</td>
<td>55,69,760</td>
<td>-</td>
<td>-</td>
<td>55</td>
<td>55,69,760</td>
</tr>
<tr>
<td>Gilt</td>
<td>42</td>
<td>7,150</td>
<td>-</td>
<td>-</td>
<td>42</td>
<td>7,150</td>
</tr>
<tr>
<td>ELSS -Equity</td>
<td>36</td>
<td>5,880</td>
<td>13</td>
<td>260</td>
<td>49</td>
<td>6,140</td>
</tr>
<tr>
<td>Gold ETF</td>
<td>14</td>
<td>2,920</td>
<td>-</td>
<td>-</td>
<td>14</td>
<td>2,920</td>
</tr>
<tr>
<td>Other ETFs</td>
<td>21</td>
<td>1,470</td>
<td>-</td>
<td>-</td>
<td>21</td>
<td>1,470</td>
</tr>
<tr>
<td>Fund of funds investing Overseas</td>
<td>20</td>
<td>1,010</td>
<td>-</td>
<td>-</td>
<td>20</td>
<td>1,010</td>
</tr>
<tr>
<td>Total</td>
<td>745</td>
<td>61,69,930</td>
<td>530</td>
<td>4,14,390</td>
<td>1,309</td>
<td>66,04,960</td>
</tr>
</tbody>
</table>

Source: AMFI Monthly, March, 2012
Table 2.2: Asset under Management (AUM) as on March 2012

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Name of the Asset Management Company</th>
<th>AUM (Rs. Millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A</strong></td>
<td><strong>BANK SPONSORED</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Joint Ventures - Predominantly Indian</strong></td>
<td></td>
</tr>
<tr>
<td>i</td>
<td>1. Canara Robeco Asset Management Co. Ltd.</td>
<td>76,630</td>
</tr>
<tr>
<td></td>
<td>2. SBI Funds Management Private Ltd.</td>
<td>420,420</td>
</tr>
<tr>
<td></td>
<td>3. Union KBC Asset Management Company Pvt. Ltd.</td>
<td>13,770</td>
</tr>
<tr>
<td></td>
<td><strong>Total A (i)</strong></td>
<td><strong>5,10,820</strong></td>
</tr>
<tr>
<td>ii</td>
<td><strong>Joint Ventures - Predominantly Foreign</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. Baroda Pioneer Asset Management Company Limited</td>
<td>41,910</td>
</tr>
<tr>
<td></td>
<td><strong>Total A (ii)</strong></td>
<td><strong>41,910</strong></td>
</tr>
<tr>
<td>iii</td>
<td><strong>Others</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. IDBI Asset Management Ltd.</td>
<td>54,820</td>
</tr>
<tr>
<td></td>
<td>2. UTI Asset Management Company Ltd</td>
<td>5,89,220</td>
</tr>
<tr>
<td></td>
<td><strong>Total A (iii)</strong></td>
<td><strong>6,44,040</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Total A (i+ii+iii)</strong></td>
<td><strong>11,96,770</strong></td>
</tr>
<tr>
<td><strong>B</strong></td>
<td><strong>INSTITUTIONS - JOINT VENTURES - PREDOMINANTLY INDIAN</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. LIC NOMURA Mutual Fund Asset Management Co. Ltd.</td>
<td>57,990</td>
</tr>
<tr>
<td></td>
<td><strong>Total B</strong></td>
<td><strong>57,990</strong></td>
</tr>
<tr>
<td><strong>C</strong></td>
<td><strong>PRIVATE SECTOR</strong></td>
<td></td>
</tr>
<tr>
<td>i</td>
<td><strong>Indian</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. Axis Asset Management Company Ltd.</td>
<td>88,150</td>
</tr>
<tr>
<td></td>
<td>2. Deutsche Asset Management (India) Private Ltd.</td>
<td>1,21,450</td>
</tr>
<tr>
<td></td>
<td>3. Edelweiss Asset Management Limited</td>
<td>3,730</td>
</tr>
<tr>
<td></td>
<td>4. Escorts Asset Management Ltd.</td>
<td>2,130</td>
</tr>
<tr>
<td></td>
<td>5. India Infoline Asset Management Co. Ltd.</td>
<td>720</td>
</tr>
<tr>
<td></td>
<td>6. Indiabulls Asset Management Company Ltd.</td>
<td>19,380</td>
</tr>
<tr>
<td></td>
<td>7. J.M. Financial Asset Management Private Ltd.</td>
<td>58,850</td>
</tr>
<tr>
<td></td>
<td>8. Kotak Mahindra Asset Management Co. Ltd.</td>
<td>2,57,380</td>
</tr>
<tr>
<td></td>
<td>9. L&amp;T Investment Management Limited</td>
<td>38,980</td>
</tr>
<tr>
<td></td>
<td>10. Motilal Oswal Asset Management Co. Ltd.</td>
<td>3,670</td>
</tr>
<tr>
<td></td>
<td>11. Peerless Funds Management Co. Ltd.</td>
<td>38,010</td>
</tr>
<tr>
<td></td>
<td>12. Quantum Asset Management Co. Private Ltd.</td>
<td>1,910</td>
</tr>
<tr>
<td></td>
<td>13. Reliance Capital Asset Management Ltd.</td>
<td>7,81,120</td>
</tr>
<tr>
<td></td>
<td>14. Religare Asset Management Company Private Limited</td>
<td>1,04,650</td>
</tr>
<tr>
<td></td>
<td>15. Sahara Asset Management Co. Private Ltd.</td>
<td>9,100</td>
</tr>
<tr>
<td></td>
<td>16. Sundaram Asset Management Company Ltd.</td>
<td>1,40,990</td>
</tr>
<tr>
<td></td>
<td>17. Tata Asset Management Ltd.</td>
<td>1,98,180</td>
</tr>
<tr>
<td></td>
<td>18. Taurus Asset Management Co. Ltd.</td>
<td>37,440</td>
</tr>
<tr>
<td>S.No.</td>
<td>Name of the Asset Management Company</td>
<td>AUM (Rs. Millions)</td>
</tr>
<tr>
<td>-------</td>
<td>--------------------------------------</td>
<td>-------------------</td>
</tr>
<tr>
<td></td>
<td>Total C (i)</td>
<td>19,05,840</td>
</tr>
<tr>
<td>ii</td>
<td>Foreign</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. AIG Global Asset Management Company (India) Private Ltd.</td>
<td>6,790</td>
</tr>
<tr>
<td></td>
<td>2. BNP Paribas Asset Management India Private Limited</td>
<td>44,210</td>
</tr>
<tr>
<td></td>
<td>3. Daiwa Asset Management (India) Private Limited</td>
<td>7,970</td>
</tr>
<tr>
<td></td>
<td>4. FIL Fund Management Private Ltd.</td>
<td>86,880</td>
</tr>
<tr>
<td></td>
<td>5. Franklin Templeton Asset Management (India) Private Ltd.</td>
<td>3,44,930</td>
</tr>
<tr>
<td></td>
<td>6. Goldman Sachs Asset Management (India) Private Limited</td>
<td>4,264</td>
</tr>
<tr>
<td></td>
<td>7. Mirae Asset Global Investments (India) Private Ltd.</td>
<td>4,440</td>
</tr>
<tr>
<td></td>
<td>8. Morgan Stanley Investment Management Private Ltd.</td>
<td>20,530</td>
</tr>
<tr>
<td></td>
<td>9. Pramerica Asset Managers Private Limited</td>
<td>18,540</td>
</tr>
<tr>
<td></td>
<td>Total C (ii)</td>
<td>5,76,930</td>
</tr>
<tr>
<td>iii</td>
<td>Joint Ventures - Predominantly Indian</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. Birla Sun Life Asset Management Co. Ltd.</td>
<td>6,11,420</td>
</tr>
<tr>
<td></td>
<td>2. DSP Black Rock Investment Managers Private Ltd.</td>
<td>2,92,980</td>
</tr>
<tr>
<td></td>
<td>3. HDFC Asset Management Co. Ltd.</td>
<td>8,98,790</td>
</tr>
<tr>
<td></td>
<td>4. ICICI Prudential Asset Management Co. Ltd.</td>
<td>6,87,180</td>
</tr>
<tr>
<td></td>
<td>5. IDFC Asset Management Company Private Limited</td>
<td>2,54,500</td>
</tr>
<tr>
<td></td>
<td>Total C (iii)</td>
<td>27,44,870</td>
</tr>
<tr>
<td>iv</td>
<td>Joint Ventures - Predominantly Foreign</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. Bharti AXA Investment Managers Private Limited</td>
<td>1,520</td>
</tr>
<tr>
<td></td>
<td>2. HSBC Asset Management (India) Private Ltd.</td>
<td>48,590</td>
</tr>
<tr>
<td></td>
<td>3. ING Investment Management (India) Private Ltd.</td>
<td>10,460</td>
</tr>
<tr>
<td></td>
<td>4. JPMorgan Asset Management (India) Private Ltd.</td>
<td>63,690</td>
</tr>
<tr>
<td></td>
<td>5. Principal Pnb Asset Management Co. Private Ltd</td>
<td>41,260</td>
</tr>
<tr>
<td></td>
<td>Total C (iv)</td>
<td>1,65,520</td>
</tr>
<tr>
<td></td>
<td>Total C (i+ii+iii+iv)</td>
<td>53,93,160</td>
</tr>
<tr>
<td></td>
<td>A+B+C</td>
<td>66,47,920</td>
</tr>
</tbody>
</table>

Source: AMFI Monthly, March, 2012

### 2.5.1. REGULATORY BODIES/ AGENCIES

**i. Securities and Exchange Board of India (SEBI)**

Securities and Exchange Board of India (SEBI) is entrusted with the role of regulating and supervising mutual funds in India. It has been set up by an Act of Parliament namely the SEBI Act, 1992 and is supervised by the Ministry of Finance. As the regulator of Indian capital market, SEBI came out with its first mutual fund regulations in 1993 that were revised
and enlarged subsequently in 1996. Apart from sharply focused normative standards, the regulatory mechanism laid huge emphasis on market discipline through enhanced transparency and disclosure requirements. These regulations have been amended from time to time. With SEBI regulations, all mutual funds have been brought under a common regulatory framework to ensure greater degree of transparency in their operations and adherence to a common structure. This act spells out several requirements and restrictions designed to protect the interests of investors and ensure that each mutual fund scheme is managed and operated in the best interest of its unit holders.

To begin with, SEBI (Mutual Fund) Regulations, define a mutual fund as a fund established in the form of a trust by a sponsor, to raise capital by the trustees, through the sale of units to the public under one or more schemes for investing in securities in accordance with these regulations. This entails three limitations on a mutual fund. First, it allows mutual fund to raise capital through sale of units to the public. Second, it permits the mutual fund to invest only in securities prescribed in SEBI (Mutual Fund) Regulations.

Third, it requires the mutual fund to be set up in the form of a trust under the Indian Trust Act. In a trust structure, the beneficial owner has no power to challenge the bona fide actions of the trustee. SEBI Regulations provides stringent qualifications for the appointment of trustees. The regulation had also spelled out the rights and obligations of the trustees, the disqualification from being appointed as trustees etc, to ensure that they carry out their fiduciary responsibilities in the best interest of their unit holders. Also, a code of conduct to be abided by the trustees has been delineated in the act.

All mutual funds are required to register with the Securities and Exchange Board of India. Registration is intended to provide adequate and accurate disclosure of material facts concerning the mutual funds. Mutual funds are allowed to launch schemes only with the prior approval of SEBI. Also the mutual funds are required to disclose to SEBI regular, comprehensive disclosures of their operations. Mutual funds must adhere to specific rules laid down by SEBI regarding their sale, distribution and advertising. According to it, the advertisement for each scheme shall disclose investment objective for each scheme. The offer document and advertisement materials shall not be misleading or contain any statement or opinion that is incorrect or false.

SEBI has prescribed a detailed code of conduct for all mutual fund intermediaries i.e. agents and distributors. For the purpose of implementing this code of conduct effectively,
AMFI certification examination has been made mandatory for all the distributors and agents of mutual funds. Mutual funds need to specify certain information about their scheme in the offer document as the name of directors of Asset Management Company, trustees and the contact person whom unit holders may approach in case of any query, complaints or grievances. Investors can also approach SEBI for rectifying their complaints after which, SEBI takes up the matter with the concerned mutual fund and follows up with them till the matter is resolved.

ii. Reserve Bank of India (RBI)

RBI is the regulatory authority of banks in India. Banks can function as sponsors, custodians and distributors of mutual funds. For performing these functions, they are subject to regulations stipulated by RBI from time to time. RBI is the regulator of the government securities and money markets in India. Since mutual funds may invest in these securities, they are required to abide by the RBI Regulations as may be applicable.

iii. Stock Exchanges

It is mandatory for close-ended funds to be listed on a stock exchange. Mutual funds also offer exchange traded funds (ETF) that can be bought and sold on a stock exchange. For these funds, the mutual fund will enter into a listing agreement with stock exchange and subject itself to the necessary regulatory and disclosure requirements.

iv. Association of Mutual Funds in India (AMFI)

AMFI is the apex body of all the registered asset management companies (AMC). It was incorporated on August 22, 1995 as a non profit organization. All the AMCs that have launched mutual fund schemes are its members. The objective of AMFI is to promote investor’s interest by defining and maintaining high ethical and professional standards in the mutual fund industry. It recommends the best business practices and code of conduct for its members. AMFI represents the mutual fund industry regarding its various matters to regulators and policy makers as SEBI, RBI and Government of India. It also conducts various awareness programmes to promote the understanding of mutual funds and disseminates information on mutual fund industry.
It is mandatory for intermediaries to register themselves with AMFI after completing the certification exam and obtain AMFI Registration Number (ARN). A distributor, whether individual or corporate will be empanelled by an AMC only after obtaining an ARN. The AMFI code of ethics (ACE) set out the standards of good practices to be followed by the asset management companies in their operations and dealings with investors, intermediaries and the public. AMFI has also framed a set of guidelines and code of conduct as AMFI Guidelines and Norms for Intermediaries (AGNI), for intermediaries who sell and distribute mutual fund products. According to SEBI it is mandatory for all distributors to follow this code of conduct. If it is violated by any distributor, AMFI is authorised by SEBI to seek explanation, issue warnings or cancel the registration of that intermediary.

2.5.2. INVESTORS’ RIGHTS AND SERVICE STANDARD

The rights of investors or unit holders in mutual funds are concerned with the information disclosure they are entitled to, the standard of services provided to them and the management of their funds. These are discussed below in detail.

i. Information Disclosure

Investors have rights for receiving information that is relevant to their investment decisions. They also have right for information revelation regarding mutual fund scheme’s Net Asset Value (NAV), portfolio and key documents.

- **Net Asset Value (NAV):** NAV of a mutual fund schemes, along with their sale and repurchase price, should be published every business day on the website of AMFI by 9 PM. A fund of funds (FoFs) can publish its NAV only after the underlying funds have published their NAV and therefore, these funds have to publish it by 10 AM of the next day following the business day. NAV should also be published in at least two newspapers.

- **Portfolio Disclosure:** Mutual funds have to publish the investment portfolio of all their schemes, every six months, in the format prescribed by SEBI. The mutual fund companies has to make this portfolio to be published in one English national daily and one regional language newspaper, published from the location of the mutual fund’s head office. This disclosure has to be made within one month from the close of the half-year. Scheme-wise Annual Report or an abridged summary has to be mailed to all unit holders within four months from the close of financial year.
• **Key Documents:** Investors have the rights to inspect key documents such as the Trust Deed, R&T Agent Agreement, Custodial Service Agreement, Investment Management Agreement and Memorandum of Articles of Association of the AMC. Investors have the right to receive information about the fund and the scheme in the Key Information Memorandum (KIM), a mandatory part of the mutual fund application form.

ii. **Service Standards**

Regulations have stipulated the time period within which routine investor transactions have to be completed. The number of pending complaints regarding these transactions has to be mandatorily published by the mutual funds. Table 2.3 provides the summary of service standards imposed on mutual funds by SEBI [143].

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Turnaround Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Allotment of units in a New Fund Offer (NFO)-Other than ELSS</td>
<td>Five days from NFO closing date</td>
</tr>
<tr>
<td>Allotment of units in a NFO for ELSS</td>
<td>30 days from NFO closing date</td>
</tr>
<tr>
<td>Dispatch of Statement of Account that is ongoing</td>
<td>10 working days from the request</td>
</tr>
<tr>
<td>Dispatch of Statement of Account for systematic transactions</td>
<td>10 days from end of calendar quarter</td>
</tr>
<tr>
<td>Dispatch of redemption proceeds</td>
<td>10 working days from transaction request</td>
</tr>
<tr>
<td>Dispatch of dividend warrants</td>
<td>30 days from date of dividend declaration</td>
</tr>
</tbody>
</table>

If there is a delay in dispatching dividends warrants or redemption proceeds, the unit holders will be paid an interest at the rate of 15 percent per annum that has to be borne by Asset Management Company and cannot be charged to the scheme.

iii. **Management of Fund**

If mutual funds make a change in any fundamental attribute of a scheme as converting close-ended fund to an open-ended fund, or a sector fund into a diversified fund, then mutual funds have to send a written communication to all its unit holders about the proposed change. Also, the proposed change and unit holder’s right in that event have to be published in two newspapers, one national and one regional. Before the implementation of changes in the
fundamental attributes, investors are given an option to redeem their units without an exit load. A merger or consolidation is considered as a change in fundamental attribute of both the merging scheme and the surviving scheme, until and unless two conditions are met. First, there are no other changes in the attributes of the surviving scheme. Second, the mutual funds are able to demonstrate that the interests of unit holders of the surviving scheme have not been affected.

Unit holders can terminate the AMC of a mutual fund. This is done by passing a resolution duly signed by the 75 percent of the unit holders of the schemes. They can also ask for winding up the scheme. If trustees want to wind up or redeem a scheme prematurely, they need to seek the consent of their unit holders. In case of any change in the sponsor or AMC of the scheme, unit holders have to be notified and they can redeem their units without any load within a stipulated time of at least 30 days. Three tier structure of AMC, trustee and custodian protect the rights of investors.

2.6 VALUATION AND COST OF INVESTING IN MUTUAL FUNDS

2.6.1 NET ASSET VALUE (NAV)

Net Asset Value is the market value of assets of the scheme minus its liabilities. Per unit NAV is the net asset value of the scheme divided by the number of units outstanding on the Valuation Date. For calculating the mutual fund's NAV, value of the total assets of the mutual fund is subtracted by its liabilities, and then this amount is divided by the total number of units in the mutual fund. i.e.,

\[
\text{Mutual Fund’s NAV} = \frac{\text{Total Assets} - \text{Liabilities}}{\text{Total number of units}}
\]

The assets of a mutual fund would consist of its investments and cash whereas its liabilities include operating expenses. NAV for all mutual funds is calculated every business day called the valuation day. Valuing the mutual fund portfolio employing the current market prices of the securities held by it is called marking to market. The net assets of the schemes are represented at current market value, and therefore, NAV is the current value of each unit of the scheme.

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8 Source: AMFI- Concept of mutual funds; http://www.amfiindia.com/showhtml.aspx?page=mfconcept#E
Net assets of a scheme go up when there is a realised income or appreciation in the market value of the scheme’s assets. It goes down in cases of realised loss or depreciation in the value of scheme’s assets. NAV of all mutual fund schemes have to be posted on the website of AMFI every business day till 9 PM. Its value is rounded off to two decimal places for all schemes except for liquid, debt and index funds for which its value is rounded off to four decimal places.

2.6.2. EXPENSES AND COST OF INVESTING IN MUTUAL FUNDS

The charges that investors pay to buy or sell a mutual fund and ongoing fund operating expenses impact their rate of return. This is due to the fact that fees are deducted from their investment returns. Many people wrongly assume that the only expense incurred in mutual fund investment is the load fee. With various advantages offered by mutual funds as liquidity, diversification, and professional management, one additional huge advantage is the complete disclosure of all the fees. Apart from the load fees and other charges, mutual fund costs are classified into the operation expenses, paid out of the fund's earnings, and sales charges, that are directly deducted from the capital which investors invest.

i. SCHEME EXPENSES:

Expenses incurred in managing a mutual fund are borne by its investors and are deducted from the market value of investments to arrive at the net assets value of scheme. SEBI regulates the heads of expenses that can be charged to mutual fund scheme and their maximum value that can be so charged. Any expense that is not chargeable, or is higher than the regulatory limits, has to be borne by the AMC itself. There are two broad types of expenses incurred by the mutual fund schemes. First are the initial issue expenses and second are fund running expenses.

a. Initial Issue Expenses:

Initial issue expenses are incurred at the time of launch of a scheme to meet expenses on advertisement and commission. These are the expenses at the time of new fund offer (NFO) and cannot be charged to the investors as these have to be borne by the AMC itself.

b. Fund Running Expenses:

Fund running expenses are incurred to manage the money mobilised from the investors. SEBI (Mutual Fund) Regulations have specified the heads of the expenses that can
be charged to the schemes and the maximum expense chargeable (Expense Ratio), as percentage of net assets.

Only certain types of expenses incurred to manage the mutual fund, called as direct expenses can be charged to its schemes. These expenses are charged on the mutual fund scheme on accrual basis and are reduced from the assets of the scheme before computing their NAV. The costs are deducted from the income earned by the fund, and are called ‘expense ratio.’ It is an annual fee that is charged to a mutual fund to pay for such expenses as: Investment management fees, marketing and selling expenses including commission, fees of registrar and transfer agent, trustee fees, custodian fees, audit fees, costs related to investor communication and costs of statutory disclosures and advertisements.

An annual expense is expressed as a percentage of the fund's average daily or weekly net assets and its break-up is reported in the scheme's offer document. The expense ratio is calculated after dividing operating expenses of a mutual fund scheme by its average net assets. Securities and Exchange Board of India (SEBI) Mutual Fund Regulations have specified the limits for expenses charged to the fund as per the following slabs:

<table>
<thead>
<tr>
<th>Net assets</th>
<th>Equity schemes</th>
<th>Debt schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>First Rs. 100 crore</td>
<td>2.50%</td>
<td>2.25%</td>
</tr>
<tr>
<td>Next Rs. 300 crore</td>
<td>2.25%</td>
<td>2.00%</td>
</tr>
<tr>
<td>Next Rs. 300 crore</td>
<td>2.00%</td>
<td>1.75%</td>
</tr>
<tr>
<td>On the balance of assets</td>
<td>1.75%</td>
<td>1.50%</td>
</tr>
</tbody>
</table>

ii. **ENTRY LOAD**

An entry load is a sales charge investors pay when they buy units of a mutual fund scheme. In other words, it is a charge collected by a scheme when it sells its units. This charge reduces the amount of their investment in fund. It is also called as Front-end load or Sales Load. Schemes that do not charge a load are called ‘No Load’ schemes.

iii. **EXIT LOAD**

Exit load is imposed on redemptions as this is the charge collected by a scheme when it buys back the units from its unit holders. Investors pay this charge when they sell mutual
fund units. This reduces the amount received by them at the time of redemption. It is also called as ‘Repurchase’ or ‘Back-end’ Load:

iv. CONTINGENT DEFERRED SALES CHARGE (CDSC)

A CDSC is a sales load that investors pay at the time of redeeming their mutual fund units. These are the variable exit load that decreases over time. As per the regulations laid down by SEBI, a no-load scheme can charge a CDSC. The asset management company is entitled to levy a CDSC not exceeding 4 percent of the redemption proceeds in the first four years after purchase, 3 percent during the second year, 2 percent in the third year and 1 percent in the fourth year.

The mutual funds have been restricted to charge entry and exit loads on investors with effect from August 1, 2009 as follows:

- Investors will not be charged any entry load. Therefore, the purchase price for investors i.e., the sales price for mutual funds should be same as the NAV of fund.
- Exit loads or CDSC charged to investors in excess of 1 percent is credited back to the scheme.
- Exit load does not vary on the basis of type of investor and is applied uniformly to all the investors in a scheme.

v. Sale Price

It is the price paid by investors at the time of investing in a scheme. Or in other words, it is the purchase price for investors and is also called as ‘Offer Price’. Sale price may also include a sales load.

vi. REPURCHASE PRICE

It is the price at which units under open-ended schemes are repurchased by the Mutual Fund. Such prices are NAV related.

vii. REDEMPTION PRICE

It is the price at which close-ended schemes redeem their units on maturity. Such prices are also NAV related.