INTRODUCTION

This chapter discusses the investment environment, wide range of investment avenues available to saver. It includes concept of mutual funds the role of mutual funds in financial market development as well.

Finally, the chapter converses investor’s behavior in the context of behavioral finance. The chapter finishes off with statement of problem, objectives and scope of the study.

Investment environment contains the market which provides various investment vehicles to investors and places for transaction with these investment vehicles. Every investment vehicle differs with each other on the basis of risk and return. The choice of investment option depends on our goal, budget, risk tolerance capacity, etc. Thus, investment decision is a part of our economic life. Everybody contract such decisions in different context at different time. Somebody earn more profit and some lose their money through investment but everybody invests for his future interests in the form of time, money and so on.

The fund for investment comes from assets already owned, savings, etc. invested in different investment avenues so that by earning return from
these investments we can enhance our future consumption possibilities like, education fee, marriage, health issues, etc. because, at the time of these responsibilities generally, we become not as much able to work and generate more fund. We do not invest only for return and capital appreciation but it is for better wealth management as well, in order to protecting our assets from inflation, taxes and other factors. Our present investment decisions affect our future wealth and it makes common sense to utilize a plan to guide our decisions. Financial planning helps in our investment decisions for example, which investment avenue or scheme will suit us can be decided with the help of financial planning.

The term *speculation* and *investment* together used simultaneously but these two terms differ on the basis of planning horizon, risk disposition, and return expectation, basis for decisions and leverage. Speculation is a financial action that does not promise for safety along with the return on principal sum. It is usually short term tendency. If a person purchases real productive asset, he is an investor while if he purchase financial asset from secondary market he is speculating his future cash flows or capital appreciation. In comparison to investors, speculators seek to make abnormally high return and for that they bear high risk. If a person buys a stock because of it goes high that means he is speculating. Speculation is not wrong thing but investor should realize that he is
speculating. Speculation is very complex task and it demands more maintenance, more time and proper strategy of investment.

“An investment operation is one which, upon thorough analysis, promises safety of principal and an adequate return. Operations not meeting these requirements are speculative.” — Ben Graham.

The following key factors considered by investors before making investment decisions:

**Return** – The expected rate of return plays a very important role in investment decision. It guides to investor where he should invest. The investor can decide according to his expectation whether he should invest in financial instrument or non financial instrument and how much amount should invest in financial instrument and how much in non-financial instrument.

**Risk Profile** – Risk means the volatility of portfolio’s value. The risk tolerance ability differs from person to person so investor should choose the investment option based on his risk profile. Risk profile depends on investor’s financial condition, personality, environment etc. So, understanding own risk bearing capacity is a crucial factor in investment decision like, a low risk investor should not invest into equities.
He should look for the safe investment option. Risky asset class causes a loss of principal.

**Liquidity** – Liquidity is also an important criterion for selection of investment avenue. It is the ability to convert asset into cash immediately. More liquid funds have less risk and the price of this safety is low return in compare to other investment options. For example, if the need of money is arising in 3 – 4 years time frame then an investor should not invest into PPF, because PPF has minimum lock up to 5 years.

**Taxation** – Tax liability plays an important role in selection of investment avenues. The investor belong to high tax bracket will prefer to invest in the option which offer higher return.

### 1.1 INVESTMENT AVENUES AT A GLANCE:

There are various investment avenues available in India. Brief descriptions of the investment avenues are given below:

Investment avenues can be classified into four groups:

a) Marketable Investments,

b) Non-marketable Investments,

c) Mutual Fund Schemes,
a) **Marketable Investments:** Marketable investments include equity shares, preference shares, convertible debentures, non-convertibles debenture, bonds of public sector units, savings certificates, Government securities etc. Equity shares and public sector bonds are the most common investment avenues among the marketable investments for the common man.

b) **Non-marketable Investments:** Non-marketable investments include bank deposits, provident and pension funds, life insurance, post-office saving deposits and fixed deposits like National Saving Certificates (NSC), Kisan Vikas Patra (KVC), private company’s shares, etc. The post-office and savings banks deposits, recurring deposits and fixed deposits are most common and important among the non-marketable investments.

Deposits in post offices and nationalized commercial banks are regarded as the less risky investment avenues. However, the rates of return in those investment avenues are comparatively less. The rate of return of fixed deposit in banks was high as 13% in the year 1991-92 and 1995-96 which has come down to 7- 9% in the year 2013-2014.
Table 1.1: Post Office Saving Schemes in India

<table>
<thead>
<tr>
<th>Schemes</th>
<th>Interest Rates</th>
<th>Tenure</th>
<th>Investment Limit</th>
<th>Tax Rebate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Post Office Savings</td>
<td>4% p.a.</td>
<td>No fix tenure</td>
<td>Minimum INR 20/- and Maximum RS. 100,000</td>
<td>Interest is tax free u/s 80L</td>
</tr>
<tr>
<td>Post Office Recurring</td>
<td>8.4% p.a.</td>
<td>5 years, can be renewed for another 5 years</td>
<td>Min. INR 10/- per month or multiple of INR 5/- and Max. No Limit</td>
<td>No tax rebate</td>
</tr>
<tr>
<td>Post Office Time Deposit</td>
<td>8.40%</td>
<td>1 Year</td>
<td>Min. INR 200/- or its multiple and Max. no limit</td>
<td>Investment qualifies for deduction u/s 80C and interest is tax free u/s 80L</td>
</tr>
<tr>
<td>Post Office Monthly</td>
<td>8.40%</td>
<td>2 Years</td>
<td>Min. INR 1500/- per month or multiples of it and Max. INR 4.5 lakhs for individual and INR 9 lakhs for joint account</td>
<td>Interest is tax free u/s80L</td>
</tr>
<tr>
<td>Post Office Monthly</td>
<td>8.40%</td>
<td>3 Years</td>
<td>Min. INR 1500/- per month or multiples of it and Max. INR 4.5 lakhs for individual and INR 9 lakhs for joint account</td>
<td>Interest is tax free u/s80L</td>
</tr>
<tr>
<td>Post Office Monthly</td>
<td>8.40%</td>
<td>5 Years</td>
<td>Min. INR 1500/- per month or multiples of it and Max. INR 4.5 lakhs for individual and INR 9 lakhs for joint account</td>
<td>Interest is tax free u/s80L</td>
</tr>
<tr>
<td>Post Office Monthly</td>
<td>8.70% p.a.</td>
<td>15 years</td>
<td>Min. INR 500/- and</td>
<td>Investment</td>
</tr>
<tr>
<td>Schemes</td>
<td>Interest Rates</td>
<td>Tenure</td>
<td>Investment Limit</td>
<td>Tax Rebate</td>
</tr>
<tr>
<td>----------------------------------</td>
<td>-------------------------</td>
<td>---------</td>
<td>---------------------------</td>
<td>------------------------------------------------------</td>
</tr>
<tr>
<td>Public Provident Fund Account</td>
<td>compounded yearly</td>
<td></td>
<td>Max. INR 100,000/-</td>
<td>qualifies for deduction u/s 80C and interest is tax free u/s 80L</td>
</tr>
<tr>
<td>5 - years National Saving Certificate (VIII issue)</td>
<td>8.5% p.a. compounded half yearly but payable after maturity.</td>
<td>5 years</td>
<td>Min INR 100/- and Max. no limit</td>
<td>Investment and interest deemed to be reinvested qualifies u/s 80C</td>
</tr>
<tr>
<td>10 - years National Saving Certificate (IX issue)</td>
<td>8.80% p.a. compounded half yearly but payable after maturity.</td>
<td>10 years</td>
<td>Min INR 100/- and Max. no limit</td>
<td>Investment and interest deemed to be reinvested qualifies u/s 80C</td>
</tr>
<tr>
<td>Senior Citizen Saving Schemes</td>
<td>9.20% p.a.</td>
<td>5 years</td>
<td>Only one deposit allowed in multiple of INR 1000/- and max. INR 15 lakhs</td>
<td>Investment qualifies for deduction u/s 80C</td>
</tr>
</tbody>
</table>

**c) Mutual Funds Schemes:** Instead of directly buying financial securities, one can invest in mutual funds. Mutual funds provide an opportunity to diversify the risk of investor by investing in different securities. Mutual funds managed by professional fund managers, who
decide where to invest, when to invest, how much to invest and when to disinvest so that the mutual funds scheme would be able to give a profit to its investors.

d) **Physical Assets:** Physical assets include house, car, building, land, flats, gold, silver etc. For the bulk of the investors the most important asset in their portfolio is a residential house. Generally physical assets are purchased to satisfy basic needs, like if an investor purchase a land or home then he and his family would be living there. He buys a car for travelling comfortably.

### Table 1.2: Evaluation of Various Investment Avenues

<table>
<thead>
<tr>
<th></th>
<th>Rate of Return (Annual Income)</th>
<th>Rate of Return (Capital Gain)</th>
<th>Risk Profile</th>
<th>Liquidity</th>
<th>Tax Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Marketable Investment</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity</td>
<td>Low</td>
<td>High</td>
<td>High</td>
<td>High</td>
<td>Yes</td>
</tr>
<tr>
<td>Non-convertible Debentures</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
<td>Average</td>
<td>No</td>
</tr>
<tr>
<td><strong>Nonmarketable Investments</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank Deposit</td>
<td>Low</td>
<td>Nil</td>
<td>Low</td>
<td>High</td>
<td>Yes</td>
</tr>
<tr>
<td>Life Insurance</td>
<td>Nil</td>
<td>High</td>
<td>Nil</td>
<td>Average</td>
<td>Yes</td>
</tr>
<tr>
<td>Provident Fund</td>
<td>Nil</td>
<td>High</td>
<td>Nil</td>
<td>Average</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Mutual Fund Schemes</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Growth/Equity</td>
<td>Low</td>
<td>High</td>
<td>High</td>
<td>High</td>
<td>Yes</td>
</tr>
<tr>
<td>Income/Debt</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
<td>High</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Physical Assets</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real Estate</td>
<td>Low</td>
<td>High</td>
<td>Low</td>
<td>Limited</td>
<td>Average</td>
</tr>
<tr>
<td>Precious Metal</td>
<td>Nil</td>
<td>Average</td>
<td>Average</td>
<td>Nil</td>
<td>Average</td>
</tr>
</tbody>
</table>
1.1.1 Household Saving:

Economic outlook conducted a study that concluded that in the last two years the financial savings accounted for less than a third of the household savings. The households started showing a serious aversion towards investing their money in financial instruments since 2010-11. The financial savings dropped from 12% of GDP in 2009-10 to 9.9% in 2010-11. It dropped further to 7% in 2011-12 and remained low at 7.1% in 2012-13. Because of decrease in financial saving and no increase in savings in physical assets, overall household sector saving rate also declined. There was a progressive shift in allocation of household savings towards financial assets from physical assets since independence (Table 1.3).

Table 1.3: Distribution of Household Saving Between Financial and Physical Assets (As Percentage to GDP at Current Market Prices)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Household Sector Saving</td>
<td>23.0</td>
<td>23.6</td>
<td>25.2</td>
<td>23.1</td>
<td>22.8</td>
<td>21.9</td>
</tr>
<tr>
<td>Financial Saving</td>
<td>11.6</td>
<td>10.1</td>
<td>12.0</td>
<td>9.9</td>
<td>7.0</td>
<td>7.1</td>
</tr>
<tr>
<td>Saving in Physical Assets</td>
<td>11.4</td>
<td>13.5</td>
<td>13.2</td>
<td>13.2</td>
<td>15.8</td>
<td>14.8</td>
</tr>
</tbody>
</table>

Source: rbi.org - Table 11.3 gross domestic saving – sector wise

Because of negative returns on financial savings and easy availability of personal loans, the households have shown a clear preference for physical assets over financial assets in the recent times. The
financial savings yielded either marginal or negative real returns during the last three years because of high inflation (Fig 1.1).

Inflation rose sharply at the wholesale as well as the consumer level during 2010-2013. The Wholesale Price Index (WPI) rose at a compounded annual rate of growth (GARG) of 8.6 per cent between 2009-10 and 2012-13. The rise in the Consumer Price Index (CPI) was even steeper at 9.8%. As inflation rate is increased saving rate has tended to pull down, household attempt to maintain their current consumption level. The households preferred bank deposit for parking their money over the equity markets, as the real value of their money got eroded less in these. The term deposits of more than one year maturity yielded annual average returns of 9.25% during 2010-13. This is on the higher end of the deposit rates. On the lower end, the returns were 7.75%. When discounted for inflation, the bank deposits too yielded negative or marginally positive returns between 2009-10 and 2012-13. But, the real value of the savings parked in deposits eroded less than that parked in shares. Hence, share of deposits in total financial savings went up from 28.8% in 2009-10 to 37.7% in 2010-11 and further up to 50.2% in 2011-12.

Similar case was of provident & pension funds. Their share in total financial savings of households went up from 16.6% in 2009-10 to 21.6% in 2012-13.
Fig 1.1: Distribution of Financial and Physical Savings
This only explains the choice households made between different financial assets. Their overall preference was clearly for the physical assets. The share of physical assets in total household savings shot up from 52.5% in 2009-10 to 69.2% in 2011-12 and then remained high at 67.6% in 2012-13. The savings in physical assets include of households’ investments in construction and machinery and change in stock. The property prices rose substantially during the last three years, making investments in real estate attractive. This explains the shift in household savings towards physical assets from financial assets.

The rising availability of banking credit to finance purchases of physical assets also contributed to the shift of savings away from the financial assets. As per the Reserve Bank of India (RBI) data, the scheduled commercial banks (SCBs) disbursed net loans of INR 3.2 trillion during April 2010-March 2013. This is a big jump from the INR 638.3 billion loans disbursed in the preceding two years. A major chunk of this was for housing purposes (INR 1.6 trillion). Net personal loans disbursed for purchases of vehicles were also substantial at INR 733 billion. More importantly, there was a sharp jump in loan disbursement for these purposes in the last three years.
Thus, the easy availability of loans and positive real returns on investments in real estate has prompted households to shift their savings into physical assets from financial assets in the last few years.

1.2 MUTUAL FUNDS IN INDIA:

Indian mutual fund industry is growing on great speed. A large number of schemes available in market but still it is not attracting to investors in India. Because of low literacy level, customers are not aware with those different schemes of mutual funds. There are various mutual fund companies distributing mutual fund. Now mutual fund industry has included various distribution channels like national and regional distributors, banks, independent financial advisor and direct selling. Apart from these channels AMCs are also reaching to Post Office which has large contacts of investors and more number of branches in various cities. The remarkable presence of India post has significant potential of sales of mutual funds.

1.2.1 History of Mutual Fund Industry:

The mutual fund industry in India began in 1963 with the formation of Unit Trust of India. At that time the primary objective of mutual fund was to attract small investors and it was achieved through collective efforts 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.

First Phase – 1964-87 (Establishment and growth of unit trust of India)

The mutual fund concept was introduced in India with the setting up of UTI in 1963. The Unit Trust of India (UTI) was the first mutual fund setup under the UTI Act, 1963. At that time it was only entity offering mutual fund in India so it enjoyed monopoly. It was set up by the Reserve Bank of India and controlled 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 entire control in place of RBI. The first scheme launched by UTI was Unit Scheme 1964 (US-1964), the first open ended scheme and the most popular scheme which attracted the largest number of investors in any single investment scheme over the years. UTI’s investible funds, at market value grew from INR 49 crore in 1965 to INR 6700 crore by the end of 1988. Its investor base had also grown to about two million investors. It launched innovative schemes during this phase.

Second Phase – 1987-1993 (Entry of Public Sector Funds)

The second phase witnessed 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). In June
1987, SBI Mutual Fund became the first non-UTI Mutual Fund followed by Canbank Mutual Fund (December 1987), Punjab National Bank Mutual Fund (August 1989), Indian Bank Mutual Fund (November 1989), Bank of India (June 1990), Bank of Baroda Mutual Fund (October 1992) under the Indian trust Act, 1882. LIC established its mutual fund in June 1989 while GIC had set up its mutual fund in December 1990. The assured return types of schemes floated by the mutual funds during this phase were perceived to be another banking product offered by the arms of sponsor banks. With the entry of public sector funds, there was a tremendous growth in size of the mutual fund industry with investible funds, at a market value, increasing to INR 47,004 crores.

<table>
<thead>
<tr>
<th>1992-93</th>
<th>Amount Mobilized</th>
<th>Assets under Management</th>
<th>Mobilization as % of Gross Domestic Savings</th>
</tr>
</thead>
<tbody>
<tr>
<td>UTI</td>
<td>11,057</td>
<td>38,247</td>
<td>5.2%</td>
</tr>
<tr>
<td>Public Sector</td>
<td>1,964</td>
<td>8,757</td>
<td>0.9%</td>
</tr>
<tr>
<td>Total</td>
<td>13,021</td>
<td>47,004</td>
<td>6.1%</td>
</tr>
</tbody>
</table>

Source: www.indianmirror.com

Third Phase – 1993-2003 (Emergence of Private Sector Funds)

The year 1993 marked as a turning point in the history of mutual funds in India. Private sector funds and foreign players were allowed in
1993 in the Indian mutual fund industry, giving the Indian investors a wider choice of fund families. Also, 1993 was the year in which the Security and Exchange Board of India (SEBI) issued the first Mutual Fund Regulations. Under which all mutual funds, except UTI were to be registered and governed. Private funds introduced innovative products, investment techniques and investor-servicing technology. By 1994-95, about 11 private sector funds had launched their schemes. The Kothari Pioneer (now merged with Franklin Templeton) set up the first private sector mutual fund in July 1993. Kothari pioneer introduced the first open-ended fund Prima in 1993. Several other private sector mutual funds were setup during this phase.

At the end of January 2003, there were 33 mutual funds with total assets of INR 121,805 crores. The Unit Trust of India with INR 44,541 crores of assets under management was way ahead of other mutual funds.

*Fourth Phase – since February 2003 (Growth and SEBI Regulation)*

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 INR 29,835 crores as at the end of January 2003, representing broadly, the assets of US 64 scheme, assured return and certain other schemes. The
specified undertaking of Unit Trust of India, functioning under an administrator and under the rules framed by Government of India and does not come under the purview of the Mutual Fund Regulations.

The second is the UTI Mutual Fund, sponsored by SBI, PNB, BOB and LIC. It is registered with SEBI and functions under the Mutual Fund Regulations. With the bifurcation of the erstwhile UTI which had in March 2000 more than INR 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.

Presently, Unit Trust of India operates under the name of UTI Mutual Fund and its past schemes (like US-64, Assured Return Schemes) are being gradually wound up. In 1999, there was a significant growth in mobilization of funds from investors and assets under management which is supported by the table 1.5.

Fifth Phase - Growth and Consolidation - 2004 Onwards

The industry has also witnessed several mergers and acquisitions recently, examples of which are acquisition of schemes of Alliance Mutual Fund by Birla Sun Life, Sun F&C Mutual Fund and PNB Mutual Fund by
Principal Mutual Fund. Simultaneously, more international mutual fund players have entered India like Fidelity, Franklin Templeton Mutual Fund etc. There were 29 funds as at the end of March 2006. This is a continuing phase of growth of the industry through consolidation and entry of new international and private sector players. The graph in fig 1.2 indicates the growth of assets over the years.

### Table 1.5: Gross Fund Mobilizations (INR crores)

<table>
<thead>
<tr>
<th>From</th>
<th>To</th>
<th>UTI</th>
<th>Public Sector</th>
<th>Private Sector</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>01/04/1998</td>
<td>31/03/1999</td>
<td>11,679</td>
<td>1,732</td>
<td>7,966</td>
<td>21,377</td>
</tr>
<tr>
<td>01/04/1999</td>
<td>31/03/2000</td>
<td>13,536</td>
<td>4,039</td>
<td>42,173</td>
<td>59,748</td>
</tr>
<tr>
<td>01/04/2000</td>
<td>31/03/2001</td>
<td>12,413</td>
<td>6,192</td>
<td>74,352</td>
<td>92,957</td>
</tr>
<tr>
<td>01/04/2001</td>
<td>31/03/2002</td>
<td>4,643</td>
<td>13,613</td>
<td>1,46,267</td>
<td>1,64,523</td>
</tr>
<tr>
<td>01/04/2002</td>
<td>31/01/2003</td>
<td>5,505</td>
<td>22,923</td>
<td>2,20,551</td>
<td>2,48,979</td>
</tr>
<tr>
<td>01/02/2003</td>
<td>31/03/2003</td>
<td>-</td>
<td>7,259</td>
<td>58,435</td>
<td>65,694</td>
</tr>
<tr>
<td>01/04/2003</td>
<td>31/03/2004</td>
<td>-</td>
<td>68,558</td>
<td>5,21,632</td>
<td>5,90,190</td>
</tr>
<tr>
<td>01/04/2004</td>
<td>31/03/2005</td>
<td>-</td>
<td>1,03,246</td>
<td>7,36,416</td>
<td>8,39,662</td>
</tr>
<tr>
<td>01/04/2005</td>
<td>31/03/2006</td>
<td>-</td>
<td>1,83,446</td>
<td>9,14,712</td>
<td>10,98,158</td>
</tr>
<tr>
<td>01/04/2006</td>
<td>31/03/2007</td>
<td>142280</td>
<td>196340</td>
<td>1599873</td>
<td>1938493</td>
</tr>
<tr>
<td>01/04/2007</td>
<td>31/03/2008</td>
<td>337498</td>
<td>346126</td>
<td>3780753</td>
<td>4464376</td>
</tr>
<tr>
<td>01/04/2008</td>
<td>31/03/2009</td>
<td>423131</td>
<td>710472</td>
<td>4292751</td>
<td>5426354</td>
</tr>
</tbody>
</table>

Source: SEBI
Fig 1.2: Growth in Assets under Management

Source: AMFI
1.2.2 Types of Mutual Fund Schemes:

Mutual Fund schemes may be classified on the basis of its structure and investment objective.

Based on Maturity Period:

(a) **Open - Ended Schemes:**

An open-ended scheme is one in which investor is free to join any time through the year. It can be redeemed on a continuous basis. These do not have a fixed maturity. Investor can withdraw from the fund at any time after an initial lock-in period. The key feature of open-end schemes is liquidity. UTI is best example of open ended scheme. These types of mutual fund disclose NAV on daily basis.

(b) **Close - Ended Schemes:**

The units of a close ended scheme are open for subscription only when it is launched known as the New Fund Offer. This type of mutual funds is not issued or repurchase or redeemed on periodic basis. Period of maturity of scheme is specified. These cannot be redeemed before termination of maturity period. AMC collects money during the initial offer i.e., NFO which remains open for few days. Investor who wants to sell the unit will sell it in the stock exchange where the units are listed and
stock exchange will sell it to buyer who wants to purchase it so it lacks liquidity. These types of mutual funds disclose NAV on weekly basis.

(c) **Interval Schemes:**

Interval Schemes are that scheme, which combines the features of open-ended and close ended schemes. These schemes are close ended but open for sale or redemption during pre specified intervals at NAV related prices. For example in monthly interval fund scheme investor can buy or sell units every month on the specified dates.

**Exchange Traded Funds:**

Exchange Traded Funds (ETF) are hybrid of open-ended index funds and close ended index fund. However, trading at the stock exchange does not affect their portfolio. The investors who want to invest in equity with long term goal and do not want to take more risk; ETF is best option for them. According to Association of Mutual Funds in India, average assets under management in retail ETF category has raised from INR 59 crore in March 2009 to INR 394 crore in March 2012. An ETF invest in stock that comprises in index. ETFs are basically passively managed funds that track a particular index such as S & P CNX Nifty. Since they are open–ended and listed on stock exchanges, it is possible to buy and sell them throughout the day and their price is determined by the demand – supply
forces in the market. In practice, they trade in a small range around the value of the assets (NAV) held by them.

ETFs offer several distinct advantages:

1. **Low Cost:** Since there is only one transaction per trade, commissions are lower on an ETF as opposed to an index, which requires a basket of stocks and multiple trades. Also, there are no load fees, and managing fees on a regular basis. Moreover, ETFs don’t employ teams of analysts tasked with finding superior stocks. This means increased savings for ETF investors. Whereas the average mutual fund charges fees of 1.4%.

2. **Tax efficiency:** ETFs are more tax efficient than traditional mutual funds because most of the tax on capital gains are realized when the assets are sold and completely up to the investors. When a gain is realized in a daily mutual fund trade or even within an index trade, capital gain taxes are incurred immediately. Therefore ETFs are a "tax friendly" investment.

3. **Diversification:** One ETF can incorporate a group of equities, market segments or styles. In comparison to a stock, the ETF can track a broader range of stocks, or even attempt to copy the returns of a country or a group of countries. Mutual funds can be diversified as well, but the ETF has lower fees and trades more like an equity investment.

4. **Derivatives:** Many ETFs catalog options and futures contracts, which are grand tools for risk-managing of the portfolio. So whether investor
wants to hedge our ETFs with calls and puts or trade ETF volatility with option straddles, some funds will have that flexibility.

5. Flexibility: Speaking of flexibility, like equity, most ETFs can be traded on market price throughout market hours. ETFs can be sold short or on margin if investors anticipate a downward movement in a particular index or commodity, and prices are continuously updated during the trading day. In other words, ETFs trade just like equities on the stock market.

6. Accountability: The company sponsor/designer/creator of the ETF publishes the list of assets in the fund on a daily basis. Most mutual funds publish the constituents on an infrequent basis and are not known for their transparency. However, this is the opposite case with ETFs.

7. Passive Management: ETFs are meant to follow a particular index, not break it. Therefore, only minor adjustments are required for the ETF, as opposed to an aggressively managed fund, which is looking for a higher return than its core asset. Thus it lowers risk and management fees for ETFs as well.

8. Immediate Dividends: The dividends of most of the companies in open-ended ETF are reinvested immediately back into the fund. The time frames can vary in the case of traditional funds. However, while ETFs are tax friendly, one must not ignore the taxes on ETF dividends either.

9. Simplicity: ETFs are simple in structure and easy to understand. If we are looking to invest in a certain industry or want to emulate the ROI on a
particular index or underlying asset, we are only a trade away from getting started with ETFs.

**Based on Investment Objective:**

(a) **Equity / Growth Funds:**

These funds invest a major part of it in stocks. The aim of growth funds is to meet investor’s need for capital appreciation over medium to long- term, high risk bearing capacity and ability to defer liquidity. Equity funds invest minimum 65% of its corpus in equity shares with significant growth potential and they offer higher return to investors in long term. They assume the risk associated with equity investments. There is no guarantee or assurance of returns. These funds may invest in a wide range of industries or focus on one or more industry sectors. These types of schemes are usually close- ended and listed on stock exchange.

(b) **Sectoral Funds:**

These funds invest in specific core sectors like energy, telecommunications, information technology, construction, financial services, and transportation. Some of these newly opened up sectors offers good investment potential.
(c) **Equity Linked Saving Schemes (ELSS):**

ELSS is an open ended, diversified schemes investing in share of blue chip companies. Returns of these schemes are determined by return of stock market. For encouraging investors to invest in the equity market, the government has given tax concessions through special schemes. Investment in these schemes entitles the investor to claim for income tax rebate, but these schemes carry a lock-in period of three years before the end of which funds cannot be withdrawn. Investor can claim up to INR 1 lakh of his ELSS investment as a deduction from his gross total income in a financial year under Sec 80C of the Income Tax Act 1961.

*Features of ELSS Funds:*

1. Tax-saving,
2. Three-year lock-in period,
3. Can be held even after the completion of three years,
4. It have both dividend and growth options, and
5. Tax Saving instrument.

*Tax Treatment of ELSS Funds:*

The returns from an ELSS fund are tax free in our hands. The long term capital gains from an ELSS are tax free as well. This is because no
tax is levied on equities that are held for more than a year. As per section 80C of Income Tax Act 1961, investor can claim up to INR 1,00,000 from their investment as a deduction from their gross total income.

**ELSS treatment after the introduction of Direct Tax Code (DTC):**

ELSS was excluded as a tax saving instrument as per the last draft of the DTC. So investment in ELSS will not get investor a deduction from his income under Sec 66 (which is a replacement of Sec 80C under DTC). Any fresh investment in ELSS after April 2012 will be treated as equity mutual fund, but only the draft version of the DTC has been released. So it remains to be seen if the mutual fund industry can get the Government to include ELSS as a tax saving instrument in the final version of the DTC.

**Advantages of ELSS over other tax saving schemes:**

- **i. Lower Lock-in Period:** As compared to traditional tax saving instruments like Fixed Deposit for five years, NSC for six years; an ELSS has a very short lock-in period of only three years. PPF investments have the highest lock-in period of 15 years.

- **ii. Long Term Capital Gains:** Since an ELSS fund invests in equities, and is dynamically managed by a professional fund manager; it has the potential to provide long term capital gains compared to other passively managed asset classes.
iii. **Systematic Savings:** There is no need to worry about making fast last-minute lump-sum investments for saving tax. One can plan effectively and invest in ELSS through the SIP (Systematic Investments Plans) route.

iv. **Challenges:** One needs to bear in mind that the returns of the ELSS schemes are determined by the performance of the equity market.

   The CRISIL-AMFI Mutual fund performance index seeks to track the performance of Equity Linked Saving Schemes (Fig: 1.3).

(d) **Debt/ Income Funds:**

   The aim of income funds is to provide safety of investment and regular income to investors. Such schemes invest predominantly in fixed income securities like bonds, corporate debentures, commercial paper and Government securities. Income Funds are ideal for safety of capital and regular income. The returns as well as the risk are lower in income funds as compared to growth funds. These funds tend to be less volatile than equity funds and produce regular income.
Fig 1.3: ELSS Fund Performance Index

Source: www.crisil.com
Hybrid Funds:

Funds also referred to as balanced schemes, divide their investment in both equities and fixed interest bearing instrument in such a proportion indicated in their offer documents for balancing the portfolio. The aim of hybrid funds is to provide both capital appreciation and regular income. The portfolio generally comprises 60% Equity and 40% Debt instruments. Their exposure to risk is moderate and they offer reasonable rate of return. In a rising stock market, the NAV of these schemes are likely to be less volatile compared to pure equity funds. These are ideal for investors looking for a combination of income and moderate growth.

New mutual funds are better

According to the study released by Lubos Pastor, Charles P. McQuaid Professor of Finance at the Booth School of Business, The University of Chicago, mutual funds launched before a couple of years are beating market more than the old mutual funds launched around for a decade or more. It doesn’t mean that investor should not include old fund while those previously have been found useful. It means that if two funds are having equal weightage, investor should select younger one. The study didn’t find the age of old and younger fund. “Even relatively small return differences should be of interest to investors in today's low-rate
environment,"

1.2.3 Indian Mutual Fund Industry: Opportunity and Challenges:

As mutual fund play a very important role in financial market but till now it is new to Indian investors. Given the lack of longer-term investment options in emerging markets such as India, it was expected that mutual funds will become popular once made available. Yet, that has not happened. Real estate, precious objects and saving account in bank are preferred choice for Indian investors over mutual funds. Indian investors did not pay attention to mutual funds.

Sankaran Naren, CIO of Equities from ICICI Prudential Mutual Fund, observed that though the mutual fund industry has grown significantly since 2004, it is relatively small (for e.g., the Indian equity mutual funds account for only 3% of the total market capitalisation while the US equity funds account for 30%.) despite the investor-friendly taxation and regulatory framework in the country. He attributed this to the tendency of Indians to trade short-term in equities rather than invest in mutual funds with a long term view, and the fact that two other asset classes, gold and real estate, have managed to give much better returns with much lower volatility. However, despite the short-term uncertainty, he felt that with better awareness and investor education, investment in
equity mutual funds was going to increase significantly over the next 10 – 20 years.

1.2.4 Role of Mutual Fund in Financial Market Development:

According to Dr. Subir Gokarn, Deputy Governor, Reserve Bank of India, four attributes efficiency, stability, transparency, and inclusion are four critical attributes of financial system; those can be developed by financial market. From this perspective, mutual funds play an important role in the development of the financial system. First, they pool the resources of small investors together, increasing their participation in financial markets, which helps both inclusion and the efficient functioning of markets themselves, as a result of larger volumes. Second, mutual funds, being institutional investors, can invest in market analysis generally not available or accessible to individual investors, thereby providing services based on informed decisions to small investors. The Reserve Bank of India regulates three categories of financial markets; money markets, government securities markets and foreign exchange markets. Mutual Funds have a presence in the first two and the Reserve Bank is therefore interested in the role that they play in developing them.

Mutual funds have contributed significantly in broadening and deepening of different segments of the Money Market and, to some extent,
the Government Securities market. Money Market Mutual Funds (MMMFs) were introduced in India in April 1991 to provide an additional short term investment avenue to investors and to bring money market instruments within the reach of individuals.

In order to promote retail holding in government securities and broaden the investor base, mutual funds which invest exclusively in government securities, Gilt Funds, were introduced. The first Gilt Fund in India was set up in December 1998. However, Gilt Funds have registered moderate growth. As on May 31, 2011, the total assets under management of the Gilt Funds were placed at INR 3,336 crore, 0.5% of the aggregate assets under management of the mutual funds.

Mutual funds occupy a large share of the primary market of Certificates of Deposit (CDs) and CPs. As on June 10, 2011, the total holdings of Mutual Funds in CDs and CPs remained at INR 2,95,164 crore (66% of the aggregate outstanding) and INR 82,951 crore (65% of the aggregate outstanding) respectively. Mutual Funds have also provided substantial liquidity to the secondary market segments of CPs and CDs. Their increased activity in the secondary market corresponds to their growing portfolio of money market investments. During the last six months, Mutual funds share in the daily turnover the secondary market of CDs and CPs stood at around 41% and 46% respectively.
The overnight segment of the money market has also benefitted from the participation of mutual funds. Their reliance on the collateralized segment of the overnight markets, viz. market repo and Collateralized Borrowing and Lending Operations (CBLO), for placement of their daily surplus liquidity enhanced the depth of the markets.

By contrast, in the Government Securities market, the participation of Mutual Funds has not been very encouraging. Out of the outstanding Government of India dated securities or G-Sec, the mutual funds held 0.9% as at end December 2010, which dropped to 0.2% as at end March 2011. The average holding of government securities by the mutual funds during the last two years remained at 0.6% as against 38.7% by the banks, 22.4% by insurance companies, 8.9% by PDs, 6.7% by PFs, 3.1% by corporate entities. During the current calendar year till the end of May, the average share of mutual funds in the secondary G-Sec market remained at 5.8% of the total traded volume. One possible reason for the lower level of participation of mutual funds in the G-Sec market is lack of investor interest in the gilt-oriented mutual funds due to significant interest rate risks.

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.

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%. 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.

Mutual funds are also allowed by Securities Exchange Board of India (SEBI) to trade on Interest Rate Futures (IRF). IRF contracts on 10-year notional coupon bonds were launched on National Stock Exchange (NSE) in August 2009. The product witnessed significant activity during the initial period, but liquidity tapered off subsequently. Reserve Bank of India (RBI) has already issued guidelines for futures contracts on 91-days T-Bills, which are expected to be introduced shortly. RBI is also considering introduction of IRF contracts on 2- years and 5-years 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.

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.

A significant feature of MMMFs or liquid mutual funds in India is that they have been mainly catering to the short-term investment needs of institutional investors such as corporate and banks whose redemption requirements are large and simultaneous. As on March 31, 2011, the investor profile of liquid funds was dominated by corporate (76.5%) followed by Banks/FIs (17.1%), HNIs (5.3%). As a consequence, when the banking sector faces liquidity shortfall and withdraws its investment from liquid mutual funds, they collectively come under stress. This may lead to a sharp fall in banks’ fresh investment in liquid funds which, in turn, could intensify the pressure on those entities that receive investments from the liquid funds.
It may be recalled that during October-November, 2008, RBI had to provide a special dispensation in the form of Term Repo facility of Rs. 60,000 crores, under which banks could avail central bank funds to address the liquidity stress faced by mutual funds, NBFCs, HFCs. banks were given an SLR exemption up to 1.5% of NDTL to address this problem.

A related issue is the circularity of funds between the banking system and mutual funds. Banks invest in mutual funds and the mutual funds put large volume of funds back to the banking system through investments in CDs, lending in CBLO and Market Repos. Such circular flow of funds between banks and mutual funds has the potential for creating systemic instability in times of stress/liquidity crunch. Thus, banks could potentially face a large liquidity risk. In this connection, RBI had announced in the monetary policy on May 3, 2011 that the bank’s investment in debt oriented mutual funds to be capped at 10% of net-worth as on March 31 of the previous year and banks would be given a period of six months to achieve this limit.

From a prudential perspective, there is the possibility of banks’ investments in the mutual funds getting channelized to sensitive sectors such as real estate and stocks. This may lead to banks’ exposure to such sensitive sectors going beyond the prescribed prudential limits.
The role of mutual funds in promoting savings continues to be insignificant in India. Despite a long history, assets of mutual funds in India constitute less than 10 per cent of GDP. A cross-country comparison suggests that mutual funds are very popular all over the world. However, assets under them in India are relatively low as compared with other emerging market economies. One of the major reasons for relatively low activity of mutual funds in India is that penetration, especially in the rural areas remains small. This is an important issue from the perspective of financial inclusion of low-income households in the formal financial system. It is generally perceived that mutual funds are popular mainly with the middle and high-income groups and have not been found to be an attractive investment avenue for the low-income groups. Thus, if the sector has to grow fast, it needs to devise appropriate schemes to attract the saving of low-income groups, especially in rural areas. This is the only way to ensure participation of all categories of investors in the financial markets, which is crucial for sustained development, both of the financial sector and the economy as a whole.

1.3 INVESTOR BEHAVIOR:

Individual investor behavior is affected by variety of psychological heuristic and biases. Investors are rational so they can take rational decisions but they are irrational in financial market. Correct and rational
behavior is necessary for success in stock market. The decision process is complex and demonstrates the limitation of viewing his behavior as just the act of putting money therefore in order to understand investors adequately. We should focus that in addition of physical activities, mental decision is also the part of their behavior that take place over the time. Somewhere it may be for a short time and in some cases it may be for a long time, i.e. one year or more. Investor behavior in actual is a subset of human behavior, so factors influence their daily activities of their life also affect their investment activities. Economic expectations and constrains affect them. A discipline called as behavioral finance has studied investor’s behavior for some time. The field of modern financial economics assumes that people behave with extreme rationality, but they do not. Furthermore, people’s deviations from rationality are often systematic. Examination of individual investor behavior is important for stock market. What affect an investor behavior and how he will react on market movements are important issues of stock market. Companies also make their policies on the basis of investor’s behavior. Government also need to make stock market more investor friendly, so for that there should be more legislation for participation of retail investors in stock market.

**Behavioral Finance** is new approach in financial market that has emerged in response of problems faced by the traditional finance.
Traditional finance is unable to address that what mistakes not to do in investment and what type of strategies should make in financial markets for earning supernormal return. There is no area in real words where behavior finance is not applied. Generally, people overestimate risk and return of any security. The behavior of an individual is organized into a coherent pattern. Although a person’s behavior changes with the situation but he behave in a consistent manner in various situation. This view emphasizes the totality of an investor’s market rather than focusing on specific actions that he will take in a particular instance.

Attitudes are the central issue of investor’s behavior. In fact, attitude has become an important subject of study in the field of investor behavior. Attitude research forms the basis for developing new investment products, repositioning existing products, creating advertising campaigns, and predicting brand preferences as well as general investment behavior. Arguments in favour of behavioral finance are realistic, psychological foundation, explanatory power of financial models; solve the puzzles of traditional finance and new approach to traditional finance.

Investors do not invest with understanding theories rather prefer Holistic Decision Making Model (HDMM) which involves reasoning and intuition in their decision making process. The HDMM is authorized by
Dr. Harsh Purohit (2013) from an extension of WISDOM equation (Reason + Intuition = Wisdom).

1.4 STATEMENT OF RESEARCH PROBLEM:

For intensifying economic development of our country, it is not sufficient to increase the rate of savings but also to do better the holding pattern of such savings. Savings held in the form of currency or physical assets either remain idle or kept non-productive or unused. The Government intervention in financial savings is one of the major contributions for the rapid economic development. As investment in equity shares are too risky, mutual funds are a vehicle to mobilize money from investors, to invest in different markets and securities.

While mutual funds are major players in most established financial markets, they are relatively new to Indian investors. The challenge for the mutual fund industry has to face is low investor awareness and financial literacy in the semi-urban and rural areas. The reason for this low mutual fund awareness is there is never a genuine or trusted forum for retail investors to clear their doubts. In this context, the need of this study has been aroused in order to see the preference, awareness and the investors’ perception regarding the mutual funds in retail investors.

According to the report announced by World Bank, India overtook
Japan as the third largest economy in terms of Purchasing Power Parity (PPP). India holds a 6.4% share of GDP on PPP basis. The United States remains at first place with 17.1% and China trails it at 14.9%. Japan holds a 4.8% share of global wealth. Many unhealthy practices prevailed in the primary market to attract retail investors. High pricing of new issues, difficulties in analyzing the prospects of a company, under pricing of shares in the market after listing have discouraged and aroused hesitation among many investors to enter into the stock market. The secondary market had become highly volatile and technical for small investors. Market of real estate, equity share, derivatives and other assets have become highly volatile. Investors have to understand the complexities of market, to keep track of market movements and to make scientific investment decisions for investing in corporate securities demands. The growing popularity of mutual funds show that it is an ideal investment vehicle for small investors having limited information and knowledge to enter the today’s complex and modern capital market. The domestic mutual fund industry has grown by 50% particularly through Systematic Investment Plan (SIP) from retail investors. But, only five percent of the households are investing in mutual fund schemes. Savings in deposits and small savings of individuals increased in the 2013-14, while saw a drop in mutual funds and currency. Households have been putting less money in financial savings recently. As stated above, the financial saving accounted
for less than a third of the households’ savings in the last two years. It started showing a serious aversion towards in investment in financial savings since 2010 – 11.

As investment limit under section 80C has been increased so investors can invest more in tax saving mutual funds schemes like Equity Linked Saving Scheme.

Mutual funds seek to serve those individuals, who have the inclination to invest but lack the background, expertise and sufficient resources to diversify their investment among various sectors. Even though mutual fund industry is growing, still there is a long way to go. The present work is an attempt to fill up the gap and help investors to make meaningful investments. Therefore, the present study attempts to bring out the attitude of mutual fund investors in Rajasthan especially for Equity Linked Saving Scheme, Exchange Traded Funds and Sectoral Funds.

The mutual fund industry has gained momentum in 1993 with the entry of private sector in the wake of liberalization and globalization. Further, the industry has gained a desired status after the implementation of the SEBI (Mutual Funds) Regulations, 1996. Out of the various categories of mutual fund schemes, ELSS, Sectoral mutual funds and ETF expected to offer the advantages of diversification, market timing and tax
saver. ELSS is an open ended, diversified schemes investing in share of blue chip companies. Returns of these schemes are determined by return of stock market. For encouraging investors to invest in the equity market, the Government has given tax concessions through special schemes. Investment in these schemes entitles the investor to claim for income tax rebate, but these schemes carry a lock-in period of three years before the end of which funds cannot be withdrawn. Sectoral fund invest in specific core sectors like energy, telecommunications, information technology, construction, financial services, transportation. Some of these newly opened up sectors offer good investment potential. When market advances some sectors are at forefront. If an investor is bullish in a particular sector can easily capitalize on his knowledge. ETF is also a best option of investing money as it has an advantage that it can be sold at real time prices rather than waiting of closing of day to get the price. Hence, the researcher intends to study the attitude of retail investors towards Equity Linked Saving Schemes, Sectoral Mutual Fund and Exchange Traded Fund.

In this contemporary world many financial institutions are mushrooming very fast and offer new products and services to the investors and encourage them to invest in their plan. Mutual funds come into this category. Mutual funds play a very crucial role in economic
development of a country. The recent trend in stock market has shown that investors are losing their money with the fall in the market. Investors have started to hire professional experts for investing on their behalf. However they are proved very costly to small investors. So mutual fund is safer and cheap option for small investors to enter in the market. Investor does not need to administer a huge sum of money to purchase stocks; with a small amount he can diversify his portfolio and risk. As stock market enter in to rough phase, values of units of mutual fund also go down. As a result mutual fund becomes available at attractive Net Asset Value (NAV). Once the stock market gets better, the NAV of mutual fund also increase.

Mutual funds industry has grown up by leaps and bounds, particularly during the last two decades of the 20th century. Moreover the entry of the private (since, 1993) has injected a sense of competition and the industry has been witnessing a structural transformation from a public sector monopoly to monopolistic industry. A proper evaluation measure will remove confusion and help the investors to decide about the level of investment in various mutual funds schemes, about their financial performance over a period of time and risk associated with their investment, so as to avoid loss and maximize the returns. It will also contribute in the performance of mutual funds.
1.5 OBJECTIVES OF THE STUDY:

The primary objective of this research work is to study the perception of retail investors towards equity linked saving schemes, sectoral mutual funds and exchange traded funds. The secondary objectives of the study are as follows:

(i) To determine the outlook of retail investors for different investment avenues.

(ii) To find out the association between the share of mutual fund in total investment of investor and his demographic profile like, age, gender marital status etc.

(iii) To study investment experience of investors in mutual fund and find out the association between investment experience and their demographic profile.

(iv) To exhibit the investor’s preferences towards different mutual fund products, equity linked saving scheme, exchange traded funds and sectoral mutual fund and association of preference with age, gender qualification, and occupation.

(v) To study the investment objectives and preferential feature of investment option considered by investors in Rajasthan.

(vi) To know opinion of investors about risk involved in mutual
fund.

(vii) To identify the features of mutual funds that attract the investors of Rajasthan.

(viii) To study the satisfaction level and problems encountered by the investors in the mutual fund market.

(ix) To study the purchasing behavior of investors and the correlation between their behavior and their demographic profile.

(x) To give suggestions to investors and mutual fund industry for making better decision and safeguarding investor’s decision respectively.

1.6 SCOPE OF THE STUDY:

The present study focuses on the investors’ perception towards mutual fund in Rajasthan. This includes various schemes of mutual fund, investment alternatives, factors influencing investment, investor’s expectation regarding the mutual fund and investors’ preference of different mutual fund schemes. It covers factors affecting investor’s attitude towards mutual fund investment. The geographical extent of the study covers investor’s residing in Rajasthan. Variables like income level, age and gender have been considered.