Chapter: 5

Findings and Suggestions

“Success is not final, failure is not fatal: it is the courage to continue that counts.” Winston Churchill
5.1 Financial Services in India

Indian economy is currently going through a phase where our prime objective is to create a market driven, productive and competitive economy. In such a circumstance, it becomes essential for us to have an inherently strong and functionally diverse financial system which can display efficiency and flexibility. A mature financial system can support higher levels of investment and promotes growth in the economy with its depth and coverage. There is a high degree of positive correlation between economic growth and sound financial system. A well-regulated and well-developed financial sector is vital to achieving the most basic need of efficient allocation of scarce resources. The financial system in India consists of financial institutions, financial markets, financial intermediaries, financial instruments and financial services. Although, the concept of the financial services has been in existence in the west for last 100 years but the concept got attention in India only during the last 30-35 years. Financial services are the significant component of the financial system of any country. They have a significant role to play in the economic growth of a country. Though there is no straight forward definition of the term financial services, they are in general used to include banking, insurance, stock broking and investment services as well as side range of other business and professional services. The functioning of the financial system of any country depends on the range of financial services extended by their providers and their efficiency and effectiveness. Both Assets Management companies like leasing companies, mutual funds, merchant bankers as well as liability management companies like bill discounting houses and
discounting houses and acceptance house offer financial services. The revolution in the IT sector had a great impact on the financial services industry in India. Till recently, it was IT and Telecom sectors which was the major growth driver. but now the scenario is changing as financial services sector is going to be the next significant growth engine.

5.2 Economic Growth and Financial Services

At the centre of any economy, it is the process of financial intermediation and disintermediation that helps the economy to grow and expand. Financial system not only channels saving into the productive investment but also helps economic activities to take place. Financial services are essential to ensure the growth of the financial system. In a recently held ICICI Securities Investors Conference at New York, our Finance Minister P.Chidambaram expressed his intention to make financial services next growth engine. It is natural that when an economy becomes more open and trade intensity increases, financial flow would be bigger. Currently, India is a big purchaser of international financial services and so, there exists an opportunity to become provider of these services soon. As per a report, these services were valued at $13 billion a year and would rise to $48 billion by 2015. According to economic survey 2006-07, financial services sector experienced a growth of 11.1% in 2006-07. The Indian financial services sector is on an accelerated growth path which is being reflected by the robust growth in the stock markets. As a result of strong investor base(both domestic and foreign) interest, Indian stock markets has recorded expectedly high levels of growth, with
the popular Sensex crossing the 19,000-mark and Nifty crossing the 5,000-mark for the first time ever. Mutual fund assets have grown by 52.26 per cent during April-August 2007 over the corresponding period last year. The growth in Indian capital market has also attracted domestic investor to invest their money on India-dedicated offshore funds. During January-August 2007, India has been ranked at second place in capital market inflows in the Asia Pacific. As per an estimate, it was revealed that 121 Indian firms have mobilized US$ 23.96 billion during January-August 2007 as against US$ 16.1 billion mobilized in 2006. The total bank credit has increased by US$ 11.62 billion over the period between July 20 and September 14, compared with US$ 8.68 billion over the same period last year. Insurance sector has also recorded a 19.9 per cent growth in premium in dollar terms in the year 2006-07, whereas the world market growth rate was only 2.9 per cent. As a result of this, India has moved to be the 15th largest market from 19th in 2005. All these figures indicate the boom in the Indian financial services sector during recent years. The financial services sector plays a critical role in fulfilling the needs of the growing and increasingly diverse economy like ours by providing high quality services to the general public as well as the corporate world. The availability of sufficient financial services in any country is a key driver for business growth and sustained profitability. In India, we have world class financial institutions, which provide these services. The corporate India is currently shining as never before. The financial services sector is made up of financial institutions like banks, insurance companies, loan companies etc. These institutions provide a significant service of financial intermediation to the
corporate entities i.e. they channelize the saving of the common people into the investment in the corporate world. Banks and Insurance Company accept various kinds of deposits from the general public and lend them to the firms. Another significant trend in the Indian financial services sector has been the growth in consumer credit. As per an estimate in India almost 70% of the population is less than 35 years of age and so it is natural to have a greater demand for consumption. Although banks and other financial institutions are providing these services, yet there is huge untapped potential. In India, we need a greater financial inclusion i.e. more and more people are yet to be brought under the banking system. Hence, the scope for providing credit services and other banking services is huge and this sector is sure to register tremendous growth in time to come. The international market is another area which will be providing major growth opportunity in future. In International arena, we are witnessing various developments like companies establishing manufacturing bases overseas, building distribution network, acquiring right to natural resources and last but very significant large number of cross border mergers and acquisitions. In these area also, the potential for services sector is huge. Another significant role of financial services sector in the Indian economy would be its significant contribution in terms of employment generation. As an economy grows, more and more employment opportunities would come from services sector. This is a natural phenomenon. Like the other booming segment of services sectors like IT and Telecom sector, the financial services sector would be generating huge employment opportunities in the Indian economy.
5.3 Mutual Funds as a Financial service

According to the global asset management 2006 report from Boston Consulting Group, India-managed assets will exceed more than $1 trillion by 2015. This means an annual growth rate of 21% for the next nine years. The Indian mutual funds industry has been growing at a healthy pace of 16.68 per cent for the past eight years and the trend will move further as has been emphasized by the report. With the entrance of new fund houses and the introduction of new funds into the market, investors are now being presented with a broad array of Mutual Fund choices. The total Asset under management of Mutual Fund industry rose by 9.45% from Rs.309953.04 Crores to 339232.46 Crores in November, 2006 as published by AMFI. In 1987, its size was Rs.1,000 crores, which went up to Rs. 4,100 crores in 1991 and subsequently touched a figure of Rs.72,000 crores in 1998. Since then this figure has kept increasing tremendously and thus revealing the efficiency of growth in the mutual fund industry. It has generally been observed that as the GDP of a country starts moving up, the share of AUM as a percentage of household financials assets start to increase. At present, India has a GDP of around $3,000 on a per capita basis and the AUM as a percentage of household financial assets is under 4%. This is undoubtedly very low as compared to other countries. As India’s GDP is expected to maintain its growth rate, households will surely be holding more assets through mutual fund than ever before.

The tremendous growth of Indian Mutual funds industry is an indicator of the efficient financial market we are currently having and the trust which
investors have on the regulatory Environment. Mutual Funds are essentially investment vehicles where people with similar investment objective come together to pool their money and then invest accordingly. Each unit of any scheme represents the proportion of pool owned by the unit holder (investor). Appreciation or reduction in value of investments is reflected in net asset value (NAV) of the concerned scheme, which is declared by the fund from time to time. Mutual fund schemes are managed by respective Asset Management Companies (AMC). Different business groups/ financial institutions/ banks have sponsored these AMCs, either alone or in collaboration with reputed international firms. Several international funds like Alliance and Templeton are also operating independently in India. Many more international Mutual Fund giants are expected to come into Indian markets in the near future.

Mutual funds invest according to the underlying investment objective as specified at the time of launching a scheme. So, we have equity funds, debt funds, gilt funds and many others that cater to the different needs of the investor. The availability of these options makes them a good option. While equity funds can be as risky as the stock markets themselves, debt funds offer the kind of security that is aimed for at the time of making investments. Money market funds offer the liquidity that is desired by big investors who wish to park surplus funds for very short-term periods. Balance Funds cater to the need of investors having an appetite for risk greater than the debt funds but less than the equity funds. The only pertinent factor here is that the fund has to be selected keeping the risk profile of the investor in mind because the products listed above have different
risks associated with them. So, while equity funds are a good bet for a long term, they may not find favour with corporates or High Networth Individuals (HNIs) who have short-term needs.

5.4 Challenges Before the Financial Services Sector

India is undoubtedly the late starter in the field of financial service and almost lagged behind by about 100 years. The Indian financial sector now operates in more competitive manner than ever before and intermediates relatively large volume of international flow. But of late, the technological developments have thrown up new challenges and as a result some new problems have started cropping up. In this increasingly complex environment, where changes are taking place everyday, banks and other financial institution providing these services are facing the challenges of revamping their organizational structure so that they can face the challenges arising from rapidly changing scenario. Appropriate organization structure has become a must for them. Another issue relates to the training of employees. The need to train and retrain staff on a continuous basis that matches with the fast track changes in IT sector has become a major challenge for the financial services sector. Another big challenge for these financial institutions is not only the competition which they are facing from international level but also the competition at the domestic level from the institutions operating in India. The other issue is related with the development of effective customer relationship management system and brand identification. As financial services are vital to the growth of the economy as well as that of the financial system, they must be regulated properly. Since, there is time lag
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between the purchase and actual effect of financial services, there is a chance of cheating and frauds which will not only affect the financial system of the country, rather entire economic activities would be affected. This has become more significant after the recent financial crisis in the east-Asian countries. However, in conclusion, it can be said that financial services industry provides a great value addition and is currently growing at a very high rate which is many times of what has been achieved by agriculture and industry in India. This time is not far away when the financial services sector would become the next significant growth engine for the Indian economy.

5.5 Mutual Funds: Universal appeal

"Savings form an important part of the economy of any nation. With savings invested in various options available to the people, the money acts as the driver for growth of the country. Indian financial scene too presents multiple avenues to the investors. Though certainly not the best or deepest of markets in the world, it has ignited the growth rate in mutual fund industry to provide reasonable options for an ordinary man to invest his savings. Investment goals vary from person to person. While somebody wants security, others might give more weightage to returns alone. Somebody else might want to plan for his child’s education while somebody might be saving for the proverbial rainy day or even life after retirement. With objectives defying any range, it is obvious that the products required will vary as well.

Though still at a nascent stage, Indian MF industry offers a plethora of schemes and serves broadly all type of investors. The range of products includes
equity funds, debt, liquid, gilt and balanced funds. There are also funds meant exclusively for young and old, small and large investors. Moreover, the setup of a legal structure, which has enough teeth to safeguard investors' interest, ensures that the investors are not cheated out of their hard-earned money. All in all, benefits provided by them cut across the boundaries of investor category and thus create for them, a universal appeal. Investors of all categories could choose to invest on their own in multiple options but opt for mutual funds for the sole reason that all benefits come in a package. Let us see how.

An investor normally prioritizes his investment needs before undertaking an investment. So different goals will be allocated different proportions of the total disposable amount. Investments for specific goals normally find their way into the debt market as risk reduction is of prime importance. This is the area for the risk-averse investors and here, mutual funds are generally the best option. The reasons are not difficult to see. One can avail of the benefits of better returns with added benefits of anytime liquidity by investing in open-ended debt funds at lower risk. Many people have burnt their fingers by investing in fixed deposits of companies who were assuring high returns but have gone bust in course of time leading to distraught investors as well as pending cases in the Company Law Board.

This risk of default by any company that one has chosen to invest in, can be minimized by investing in mutual funds as the fund managers analyze the companies' financials more minutely than an individual can do as they have the expertise to do so. They can manage the maturity of their portfolio by investing in
instruments of varied maturity profiles. Since there is no penalty on pre-mature withdrawal, as in the cases of fixed deposits, debt funds provide enough liquidity. Moreover, mutual funds are better placed to absorb the fluctuations in the prices of the securities as a result of interest rate variation and one can benefit from any such price movement.

Apart from liquidity, these funds have also provided very good post-tax returns on year to year basis. Even historically, we find that some of the debt funds have generated superior returns at relatively low level of risks. On an average debt funds have posted returns over 10 percent over one-year horizon. The best performing funds have given returns of around 14 percent in the last one-year period. In nutshell we can say that these funds have delivered more than what one expects of debt avenues such as post office schemes or bank fixed deposits. Though they are charged with a dividend distribution tax on dividend payout at 10 percent (plus a surcharge of 10 percent), the net income received is still tax free in the hands of investor and is generally much more than all other avenues, on a post tax basis.

Moving up in the risk spectrum, we have people who would like to take some risk and invest in equity funds/capital market. However, since their appetite for risk is also limited, they would rather have some exposure to debt as well. For these investors, balanced funds provide an easy route of investment. Armed with the expertise of investment techniques, they can invest in equity as well as good quality debt thereby reducing risks and providing the investor with better returns than he could otherwise manage. Since they can reshuffle their portfolio as per
market conditions, they are likely to generate moderate returns even in pessimistic market conditions. Next come the risk takers. Risk takers by their very nature, would not be averse to investing in high-risk avenues. Capital markets find their fancy more often than not, because they have historically generated better returns than any other avenue, provided, the money was judiciously invested. Though the risk associated is generally on the higher side of the spectrum, the return-potential compensates for the risk attached.

Capital markets interest people, albeit not all for there are several problems associated. First issue is that of expertise. While investing directly into capital market one has to be analytical enough to judge the valuation of the stock and understand the complex undertones of the stock. One needs to judge the right valuation for exiting the stock too. It is very difficult for a small investor to keep track of the movements of the market. Entrusting the job to experts, who watch the trends of the market and analyze the valuations of the stocks will solve this problem for an investor. Mutual funds specialize in identification of stocks through dedicated experts in the field and this enables them to pick stocks at the right moment. Sector funds provide an edge and generate good returns if the particular sector is doing well.

Next problem is that of funds/money. A single person can't invest in multiple high-priced stocks for the sole reason that his pockets are not likely to be deep enough. This limits him from diversifying his portfolio as well as benefiting from multiple investments. Here again, investing through MF route enables an investor to invest in many good stocks and reap benefits even through a small
Investment. This not only diversifies the portfolio and helps in generating returns from a number of sectors but reduces the risk as well. Though identification of the right fund might not be an easy task, availability of good investment consultants and counselors will help investors take informed decision.

**Risk Return Grid**

<table>
<thead>
<tr>
<th>Risk Tolerance / Return Expected</th>
<th>Focus</th>
<th>Suitable Products</th>
<th>Benefits offered by MFs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>Debt</td>
<td>Bank/ Company FD, Debt based Funds</td>
<td>Liquidity, Better Post-Tax returns</td>
</tr>
<tr>
<td>Medium</td>
<td>Partially Debt, Partially Equity</td>
<td>Balanced Funds, Some Diversified Equity Funds and some debt Funds, Mix of shares and Fixed Deposits</td>
<td>Liquidity, Better Post-Tax returns, Better Management, Diversification</td>
</tr>
<tr>
<td>High</td>
<td>Equity</td>
<td>Capital Market, Equity Funds (Diversified as well as Sector)</td>
<td>Diversification, Expertise in stock picking, Liquidity, Tax free dividends</td>
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Their appeal is not just limited to these categories of investors. Specific goals like career planning for children and retirement plans are also catered to by mutual funds. Children funds have found their way in a big way with many of the fund houses already having launched a children fund. Essentially debt oriented, these schemes invite investments, which are locked till the child attains majority and requires money for higher education. You can invest today and assure financial support to your child when he/she requires them. The schemes have given very good returns of around 14 percent in the last one-year period. These schemes are also designed to provide tax efficiency. The returns generated by these funds come under capital gains and attract tax at concessional rates.

Besides this, if the objective was to save taxes, the industry offers equity linked savings schemes as well. Equity-based funds, they can take long-term call
on stocks and market conditions without having to worry about redemption pressure as the money is locked in for three years and provide good returns. Some of the ELSS have been exceptional performers in past and cater to equity investor with good performances. The industry offered tax benefits under various sections of the IT Act. For e.g. dividend income is free in the hands of the investor while capital gains are taxed after providing for cost inflation indexation. Hitherto, the benefits under section 54 EA/EB were available to take benefits of the tax provisions for capital gains but have now been removed. The benefits listed so far have essentially been for the small retail investor but the industry can attract investments from institutional and big investors as well. Liquid funds offer liquidity as well as better returns than banks and so attract investors. Many funds provide anytime withdrawal enabling a big investor to take maximum benefits. In other developed countries, mutual funds attract much more investments as compared to the banking sector but in India the case is reverse. We lack awareness about the benefits that are offered by these schemes. It is time that investors irrespective of their risk capacities, made intelligent decisions to generate better returns and mutual funds are definitely one of the ways to go about it.

5.6 10 commandments

Moses gave to his followers 10 commandments that were to be followed till eternity. The world of investments too has several ground rules meant for investors who are novices in their own right and wish to enter the myriad world of
investments. These come in handy for there is every possibility of losing what one has if due care is not taken.

1. Assess yourself: Self-assessment of one’s needs; expectations and risk profile is of prime importance failing which; one will make more mistakes in putting money in right places than otherwise. One should identify the degree of risk bearing capacity one has and also clearly state the expectations from the investments. Irrational expectations will only bring pain.

2. Try to understand where the money is going: It is important to identify the nature of investment and to know if one is compatible with the investment. One can lose substantially if one picks the wrong kind of mutual fund. In order to avoid any confusion it is better to go through the literature such as offer document and fact sheets that mutual fund companies provide on their funds.

3. Don't rush in picking funds, think first: one first has to decide what he wants the money for and it is this investment goal that should be the guiding light for all investments done. It is thus important to know the risks associated with the fund and align it with the quantum of risk one is willing to take. One should take a look at the portfolio of the funds for the purpose. Excessive exposure to any specific sector should be avoided, as it will only add to the risk of the entire portfolio. Mutual funds invest with a certain ideology such as the "Value Principle" or "Growth Philosophy". Both have their share of critics but both philosophies work for investors of different kinds. Identifying the proposed investment philosophy of the fund will give an insight into the kind of risks that it shall be taking in future.
4. Invest. Don't speculate: A common investor is limited in the degree of risk that he is willing to take. It is thus of key importance that there is thought given to the process of investment and to the time horizon of the intended investment. One should abstain from speculating which in other words would mean getting out of one fund and investing in another with the intention of making quick money. One would do well to remember that nobody can perfectly time the market so staying invested is the best option unless there are compelling reasons to exit.

5. Don't put all the eggs in one basket: This old age adage is of utmost importance. No matter what the risk profile of a person is, it is always advisable to diversify the risks associated. So putting one's money in different asset classes is generally the best option as it averages the risks in each category. Thus, even investors of equity should be judicious and invest some portion of the investment in debt. Diversification even in any particular asset class (such as equity, debt) is good. Not all fund managers have the same acumen of fund management and with identification of the best man being a tough task, it is good to place money in the hands of several fund managers. This might reduce the maximum return possible, but will also reduce the risks.

6. Be regular: Investing should be a habit and not an exercise undertaken at one's wishes, if one has to really benefit from them. As we said earlier, since it is extremely difficult to know when to enter or exit the market, it is important to beat the market by being systematic. The basic philosophy of Rupee cost averaging would suggest that if one invests regularly through the ups and downs of the market, he would stand a better chance of generating more returns than the
market for the entire duration. The SIPs (Systematic Investment Plans) offered by all funds helps in being systematic. All that one needs to do is to give post-dated cheques to the fund and thereafter one will not be harried later. The Automatic investment Plans offered by some funds goes a step further, as the amount can be directly/electronically transferred from the account of the investor.

7. Do your homework:

It is important for all investors to research the avenues available to them irrespective of the investor category they belong to. This is important because an informed investor is in a better decision to make right decisions. Having identified the risks associated with the investment is important and so one should try to know all aspects associated with it. Asking the intermediaries is one of the ways to take care of the problem.

8. Find the right funds

Finding funds that do not charge much fees is of importance, as the fee charged ultimately goes from the pocket of the investor. This is even more important for debt funds as the returns from these funds are not much. Funds that charge more will reduce the yield to the investor. Finding the right funds is important and one should also use these funds for tax efficiency. Investors of equity should keep in mind that all dividends are currently tax-free in India and so their tax liabilities can be reduced if the dividend payout option is used. Investors of debt will be charged a tax on dividend distribution and so can easily avoid the payout options.

9. Keep track of your investments
Finding the right fund is important but even more important is to keep track of the way they are performing in the market. If the market is beginning to enter a bearish phase, then investors of equity too will benefit by switching to debt funds as the losses can be minimized. One can always switch back to equity if the equity market starts to show some buoyancy.

10. Know when to sell your mutual funds: Knowing when to exit a fund too is of utmost importance. One should book profits immediately when enough has been earned i.e. the initial expectation from the fund has been met with. Other factors like non-performance, hike in fee charged and change in any basic attribute of the fund etc. are some of the reasons for to exit. For more on it, read "When to say goodbye to your mutual fund."

5.7 INVESTMENT OPTIONS: MUTUAL FUNDS STAND OUT

Investments in mutual funds too are not risk-free and so investments warrant some caution and careful attention of the investor. Investing in mutual funds can be a dicey business for people who do not remember to follow these rules diligently, as people are likely to commit mistakes by being ignorant or adventurous enough to take risks more than what they can absorb. This is the reason why people would do well to remember these rules before they set out to invest their hard-earned money.

Savings form an important part of the economy of any nation. With the savings invested in various options available to the people, the money acts as the driver for growth of the country. Indian financial scene too presents a plethora of avenues to the investors. Though certainly not the best or deepest of markets in
the world, it has reasonable options for an ordinary man to invest his savings. Let us examine several of them:

5.7.1 Banks

Considered as the safest of all options, banks have been the roots of the financial systems in India. Promoted as the means to social development, banks in India have indeed played an important role in the rural upliftment. For an ordinary person though, they have acted as the safest investment avenue wherein a person deposits money and earns interest on it. The two main modes of investment in banks, savings accounts and Fixed deposits have been effectively used by one and all. However, today the interest rate structure in the country is headed southwards, keeping in line with global trends. With the banks offering little above 9 percent in their fixed deposits for one year, the yields have come down substantially in recent times. Add to this, the inflationary pressures in economy and you have a position where the savings are not earning. The inflation is creeping up, to almost 8 percent at times, and this means that the value of money saved goes down instead of going up. This effectively mars any chance of gaining from the investments in banks.

5.7.2 Post Office schemes

Just like banks, post offices in India have a wide network. Spread across the nation, they offer financial assistance as well as serving the basic requirements of communication. Among all saving options, Post office schemes have been offering the highest rates. Added to it is the fact that the investments are safe with the department being a Government of India entity. So the two basic and most
sought for features, those of return safety and quantum of returns were being handsomely taken care of. Though certainly not the most efficient systems in terms of service standards and liquidity, these have still managed to attract the attention of small, retail investors. However, with the government announcing its intention of reducing the interest rates in small savings options, this avenue is expected to lose some of the investors. Public Provident Funds act as options to save for the post retirement period for most people and have been considered good option largely due to the fact that returns were higher than most other options and also helped people gain from tax benefits under various sections. This option too is likely to lose some of its sheen on account of reduction in the rates offered.

5.7.3 Company Fixed Deposits

Another oft-used route to invest has been the fixed deposit schemes floated by companies. Companies have used fixed deposit schemes as a means of mobilizing funds for their operations and have paid interest on them. The safer a company is rated, the lesser the return offered has been the thumb rule. However, there are several potential roadblocks in these. First of all, the danger of financial position of the company not being understood by the investor lurks. The investors rely on intermediaries who more often than not, don't reveal the entire truth. Secondly, liquidity is a major problem with the amount being received months after the due dates. Premature redemption is generally not entertained without cuts in the returns offered and though they present a reasonable option to counter interest rate risk (especially when the economy is headed for a low interest regime), the safety
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of principal amount has been found lacking. Many cases like the Kuber Group and DCM Group fiascoes have resulted in low confidence in this

5.7.4 Option.

The options are essentially for the risk-averse, people who think of safety and then quantum of return, in that order. For the brave, it is dabbling in the stock market. Stock markets provide an option to invest in a high risk, high return game. While the potential return is much more than 10-11 percent any of the options discussed above can generally generate, the risk is undoubtedly of the highest order. But then, the general principle of encountering greater risks and uncertainty when one seeks higher returns holds true. However, as enticing as it might appear, people generally are clueless as to how the stock market functions and in the process can endanger the hard-earned money.

For those who are not adept at understanding the stock market, the task of generating superior returns at similar levels of risk is arduous to say the least. This is where Mutual

5.7.4 Funds come into picture.

Mutual Funds are essentially investment vehicles where people with similar investment objective come together to pool their money and then invest accordingly. Each unit of any scheme represents the proportion of pool owned by the unit holder (investor). Appreciation or reduction in value of investments is reflected in net asset value (NAV) of the concerned scheme, which is declared by the fund from time to time. Mutual fund schemes are managed by respective Asset Management Companies (AMC). Different business groups/ financial
institutions/ banks have sponsored these AMCs, either alone or in collaboration with reputed international firms. Several international funds like Alliance and Templeton are also operating independently in India. Many more international Mutual Fund giants are expected to come into Indian markets in the near future. The benefits on offer are many with good post-tax returns and reasonable safety being the hallmark that we normally associate with them. Some of the other major benefits of investing in them are:

5.8 Number of available options

Mutual funds invest according to the underlying investment objective as specified at the time of launching a scheme. So, we have equity funds, debt funds, gilt funds and many others that cater to the different needs of the investor. The availability of these options makes them a good option. While equity funds can be as risky as the stock markets themselves, debt funds offer the kind of security that is aimed for at the time of making investments. Money market funds offer the liquidity that is desired by big investors who wish to park surplus funds for very short-term periods. Balance Funds cater to the investors having an appetite for risk greater than the debt funds but less than the equity funds. The only pertinent factor here is that the fund has to be selected keeping the risk profile of the investor in mind because the products listed above have different risks associated with them. So, while equity funds are a good bet for a long term, they may not find favour with corporates or High Networth Individuals (HNIs) who have short-term needs.

5.8.1 Diversification
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Investments are spread across a wide cross-section of industries and sectors and so the risk is reduced. Diversification reduces the risk because all stocks don't move in the same direction at the same time. One can achieve this diversification through a Mutual Fund with far less money than one can on his own.

5.8.2 Professional Management

Mutual Funds employ the services of skilled professionals who have years of experience to back them up. They use intensive research techniques to analyze each investment option for the potential of returns along with their risk levels to come up with the figures for performance that determine the suitability of any potential investment.

5.8.3 Potential of Returns

Returns in the mutual funds are generally better than any other option in any other avenue over a reasonable period of time. People can pick their investment horizon and stay put in the chosen fund for the duration. Equity funds can outperform most other investments over long periods by placing long-term calls on fundamentally good stocks. The debt funds too will outperform other options such as banks. Though they are affected by the interest rate risk in general, the returns generated are more as they pick securities with different duration that have different yields and so are able to increase the overall returns from the portfolio.

5.8.4 Liquidity

Fixed deposits with companies or in banks are usually not withdrawn premature because there is a penal clause attached to it. The investors can withdraw or redeem money at the Net Asset Value related prices in the open-end schemes. In
closed-end schemes, the units can be transacted at the prevailing market price on a stock exchange. Mutual funds also provide the facility of direct repurchase at NAV related prices. The market prices of these schemes are dependent on the NAVs of funds and may trade at more than NAV (known as Premium) or less than NAV (known as Discount) depending on the expected future trend of NAV which in turn is linked to general market conditions. Bullish market may result in schemes trading at Premium while in bearish markets the funds usually trade at Discount. This means that the money can be withdrawn anytime, without much reduction in yield. Besides these important features, mutual funds also offer several other key traits. Important among them are:

**5.8.5 Well Regulated**

Unlike the company fixed deposits, where there is little control with the investment being considered as unsecured debt from the legal point of view, the Mutual Fund industry is very well regulated. All investments have to be accounted for, decisions judiciously taken. SEBI acts as a true watchdog in this case and can impose penalties on the AMCs at fault. The regulations, designed to protect the investors’ interests are also implemented effectively.

**5.8.6 Transparency**

Being under a regulatory framework, mutual funds have to disclose their holdings, investment pattern and all the information that can be considered as material, before all investors. This means that the investment strategy, outlooks of
the market and scheme related details are disclosed with reasonable frequency to ensure that transparency exists in the system. This is unlike any other investment option in India where the investor knows nothing as nothing is disclosed.

5.9 Conclusion

Mutual Funds offer a relatively less expensive way to invest when compared to other avenues such as capital market operations. The fee in terms of brokerages, custodial fees and other management fees are substantially lower than other options and are directly linked to the performance of the scheme. Investment in mutual funds also offers a lot of flexibility with features such as regular investment plans, regular withdrawal plans and dividend reinvestment plans enabling systematic investment or withdrawal of funds. Even the investors, who could otherwise not enter stock markets with low investible funds, can benefit from a portfolio comprising of high-priced stocks because they are purchased from pooled funds.

Mutual funds offer several benefits that are unmatched by other investment options. Post liberalization, the industry has been growing at a rapid pace and has crossed Rs. 100000 crore size in terms of its assets under management. However, due to the low key investor awareness, the inflow under the industry is yet to overtake the inflows in banks. Rising inflation, falling interest rates and a volatile equity market make a deadly cocktail for the investor for whom mutual funds offer a route out of the impasse. The investments in mutual funds are not without risks because the same forces such as regulatory
frameworks, government policies, interest rate structures, performance of companies etc. that rattle the equity and debt markets, act on mutual funds too. But it is the skill of the managing risks that investment managers seek to implement in order to strive and generate superior returns than otherwise possible that makes them a better option than many others. The mutual fund sector would grow at compound annual rate of 30 per cent in next three years to become Rs 9,50,000 crore industry, industry body Assocham predicted from a survey on its growth. The industry has grown at 25 per cent between 1999 and 2007 to stand at Rs 4,67,000 crore and the trend would improve as MFs are becoming a preferred choice for both rural and urban retail investors. This would contribute to the growth of the MF industry, the chamber said in its survey on 'MF Growth Patterns'. The share of privately managed MF players in the total MF industry is expected to fall to 70 per cent from the current estimation of 82 per cent. The reduction would result from the alliance of the private sector with overseas partners, it said. The public sector share in the industry would go up nearly 20 per cent from 10 per cent now. Similarly, the share of joint sector would also rise to about 10 per cent from 8 per cent currently. The chamber said the country's MF industry is 100 times behind that of the US where the size of the industry is at staggering $12 trillion. In India, MF industry manages nearly 700 schemes against 12,000 schemes handled by the US MF industry. Assocham said market penetration in MF industry would more than double by 2010 from about 4 per cent now. This rate is, however, 49 per cent in the US and 20 per cent in the UK. MFs in India are now focussed on enhancing their reach to cities other than the
In conclusion, it can be said that Mutual funds Industry has really played a very significant role in the financial system as a very significant mobilizer of financial resources to the corporate securities and in the time to come, its role is going to significantly increase.