Chapter 5

Conclusions, Findings and Suggestions

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5.1 Introduction

This chapter brings out major findings including problems and prospects of mutual funds industry in India. The suggestions along with the strategies for overcoming the existing problem, coping with challenges have also been offered for further promotion of mutual funds industry in India.

5.2 Findings

➤ The concept of mutual funds is not new. It was started in 1822 as an investment trust called ‘Societe General de Belgique’ in Belgium. This trust used diversification as means to minimize risk. The modern day mutual funds are based on this concept. They mobilize resources from small and big investors and invest on their behalf thus offering benefit of professional management and diversification. It was due to this very advantage that mutual funds operation was started in India by the enactment of the Unit Trust of India (UTI) Act in 1963. The first scheme to be launched in India was US-64. The objective of launching this scheme was to provide an opportunity of investment to small and marginal investor who themselves could not invest in stock market.

➤ Mutual funds entered the Indian capital market in 1964 with a view to provide the retail investors the benefit of diversification of risk, assured returns, professional management. Since then they have grown phenomenally in terms of number, size of operations, investor base and scope. With the ushering in of economic reforms in the early 1990s, the Government of India opened the way for the
entry of private sector and foreign players into this industry. Consequently, this has emerged as a highly competitive financial service industry today. In India, the mutual fund industry came into being with the establishment of Unit Trust of India in 1964. Public sector banks and financial institutions began to establish mutual funds in 1987. The private sector and foreign institutions were allowed to set up mutual funds in 1993

➢ Today three different types of players are operating in the Indian Market that includes UTI, non-UTI public sector mutual funds and private sector mutual funds (including foreign mutual funds).

➢ Entry of private sector mutual funds adversely affected the prospects of banks sponsored and other public sector mutual funds. As the share net resource mobilization of these institution supported mutual funds has gone down gradually since the inception of private sector mutual funds.

➢ Association of mutual funds industry (AMFI) represents the AMCs in India. It was established as non-profit organization on 22 August, 1995. It is dedicated to developing the Indian mutual fund industry on professional, healthy and ethical lines and to enhance and maintain standards in all areas with a view to protecting the interests of the mutual fund and their unit holders.

➢ The asset under management in India is 10% of GDP that is quite low compared to 74% in US 100% percent in Australia and 45% in Brazil
There are 180 million households in India, of which only 11.8 million, i.e., 6.7%, invest in mutual funds. In urban areas, 13.7% of the households invest in mutual funds and in rural areas it is just about 3.8%. Thus, the Indian small investors do not prefer to invest in mutual funds.

The industry comprises of 37 AMCs, 956 schemes that has crossed 36 million folios. The majority of the funds in India, approximately 96% are open-ended type and the remaining 4% are close-ended type. The MF industry is growing at an average rate of 16-17% because of the entry of commercial banks and the private players coupled with the rapid growth of the Indian capital market. Even then India ranks 25th in the AUM of the global MF industry.

The Indian MF industry is mostly concentrated in urban areas and among High Net worth Individuals (HNWIs). Irrespective of the many players, the MFs today have neither gathered a large investor base nor garnered huge AUMs. The urban investors are playing a major role in the industry and it should be diversified into rural and suburban areas, where there is a vast potential market. High costs, low awareness and low penetration remain the biggest bugbears in the MF industry. And they are also competing with insurance companies that have launched a range of products with a similar structure, for the same set of investors. The Securities and Exchange Board of India (SEBI) bars MFs from getting celebrities to advertise their schemes and this has two effects—one, on the positive side, it will reduce the costs of MFs and two, on the negative side, it restricts the creation of awareness.
The consistency in the performance of MFs has been a major factor that has attracted many investors. The MFs are declaring double-digit dividends. This is one of the reasons why people are now opting for mutual funds investment.

Though India enjoys a good saving rate, the mutual fund industry gets a very little share out of those savings. To match the international markets like the US and Australia etc., these savings need to be channelized through mutual funds. One of the major reasons that Indian mutual fund industry is not matching the likes of the markets of these developed countries is lack of deeper distribution networks and channels in India. This has been a major concern for the mutual funds industry in India, which has not been able to penetrate deeper into the rural parts of the country and major focus has been on the metro cities and `A' class cities. The rural markets and `B' and `C' class cities, which also hold a lot of potential, should be addressed properly by the players in the industry.

Lack of awareness about the mutual funds products among investor is another reason for the low penetration of mutual funds products.

Political instability is another factor often becomes reason for the poor performance of mutual funds. This has become more evident due to coalition politics.

By offering tailored made products for the various categories of investors open-ended mutual funds scheme has become a big boon in India. This evident from the fact that 592 open-ended schemes were in operation as on march 2008. However the popularity of close-ended scheme has decreased in India since 1991. As during
1990-91, 18 scheme were launched out of which 15(83%) were close-ended and 3 (17%) were open-ended. But in 2008 out of 956 schemes, 364(38%) were close-ended and 592(62%) were open-ended

- The investments of mutual funds are permitted only in transferable securities that include money market and capital market instruments or debt. These holdings shall not exceed 10 percent with respect to growth funds and 40 percent in case of income funds. It is mandatory that the debt instruments are rated by approved credit rating agencies if this is not so then the approval of the board of AMC is required. Beside this mutual funds cannot invest more than 5 percent of their amount through any of their schemes in one single company or own more than 5 percent of any company's paid up capital containing voting rights

- The investors participating in the mutual funds investment have no proper knowledge of its working mechanism. In the absence of proper knowledge they some time become prey to luring advertisement offering higher rate of return. When they fail to earn the required rate of return offered in the advertisement they get dissuaded from investing in mutual funds.

- The share of mutual funds savings in total financial savings of the household sector savings has declined over the years.

- The impact of liberalization on the net resource mobilization of mutual funds industry in India is responsible for 56.2 percent of the funds mobilized. This implies that there are many other macro economic factors which have indirectly affected of quantum of net
resource mobilization by mutual funds in India. Further the impact of time on the net resource mobilization is insignificant but the impact of policy and policy and time is significant on the net resource mobilization.

- There are 4.33 crore investor accounts holding units of Rs. 50,766.99 crore. Out of this total number of investor accounts, 4.20 crore are individual investors accounts and contribute Rs. 18,746.3.98 crore which is 36.93 percent of the total net assets. While corporate and institutions who form only 1.16 percent of the total number of investors account in the mutual funds, contribute a sizable amount of Rs. 28,710.01 crore which is 56.55 percent of the total net assets in the mutual funds industry. NRIs and FIIs constitute a very small percentage of investors accounts (1.98%) and contribute Rs. 3,309.01 crore (6.52%) of the net assets.

- The total share of equity in HDFC Balanced Fund is 68.59. The reliance industries limited has maximum of 6.99 percent followed by Coramandal Fertilizers Ltd. ICICI Bank Ltd. has the least share of 3.45 percent. The debt and money market instruments together constitute a share of 28 percent.

- The maxim investment of 8.97 percent of the HDFC equity scheme is in ICICI Bank Ltd. The total share of equity and equity related holding is 99.3 percent while investments in other assets is 0.69 percent.

- The maximum investment of HFC Growth fund is made in ITC Ltd. (6.88%). This is followed by SBI (6.43%). The total equity and equity
related a holding is 90.13 percent while the investment in other avenue other than equity is 9.47 percent.

- The maximum investment of HDFC TaxSaver is in ITC Ltd. followed by Larsen and Turbo Ltd. with a share of 6.46 and 5.43 percent respectively. The total equity and equity related holding is 94.64 percent while 5.36 percent in invested in other class of assets.

- The total investment of HDFC Top 200 schemes in equity and equity related holdings is 95.95 percent while the remaining 4.05 percent is invested in other current assets.

- Of the five funds chosen for the study all funds except balanced funds earned higher than the market return. This implies that 80 percent of the selected funds have superior performance than the market. The balanced fund (20%) however generated lower return than the market.

- The average return earned by the sample funds is 2.5 percent per month whereas the average return of the market is 1.8 percent. This implies that the sample funds on an average performed better than the market as well as the risk-free assets.

- The average risk of the sample fund is 7.5 percent per month whereas for the market it is 7 percent per month. This implies that fund has taken slightly higher risk than the market.

- The sample funds chosen for the study is not adequately diversified as reflected by their coefficient of determination values, $R^2$, the average diversification is only 69 percent.
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- The Sharpe ratio of 80 percent of the schemes is better than the relevant benchmark.
- On the basis of the Treynor ratio, it was found that eighty percent of the fund has performed better than the relevant benchmark.
- Results of Jensen measure indicate that out of five schemes chosen for study, 4 schemes (80%) have positive alpha values indicating superior performance, which means that these funds have generated returns in excess of equilibrium returns. This indicates that four-fifth of the fund manager are able to earn superior returns.
- On the basis of the Sharpe differential return for the sample schemes, it was found that out of five schemes four schemes have positive differential return thereby indicating superior performance. These schemes are HDFC balanced fund, HDFC equity, HDFC tax saver and HDFC top-200 schemes. These are the returns earned by the selection of undervalued securities and diversifying the portfolio by the fund manager.

5.3 Suggestions

- HDFC mutual funds in order to become number one asset management company should continue to provide better return and after sale service to its customer.
- HDFC mutual funds should organize regular refresher course for agents and broker. This will improve their skill and more money will be channelized for investment.
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- HDFC should expedite grievance redressal mechanism as at the end of 31 March 2008, 5604 complaints were received out of which 5572 complaints were redressed. This means that 98 complaints were pending. The delay causes dissatisfaction amongst the clients.

- HDFC mutual funds should focus on generating better performance than the market. To yield better return it become imperative that fund manager of various scheme are better trained to reap better investment irrespective of the prevailing market conditions.

- HDFC mutual funds can improve its customer base by adopting aggressive marketing strategy. It can tap the potential of the rural and semi urban area by opening its branches in these areas.

- HDFC mutual funds should launch new and innovative schemes at regular intervals to attract investors.

- The mutual funds industry should focus on managing investor money and other function such as accounting and other allied services can be outsourced. This will save both money and energy to concentrate in other profitable ventures.

- The rate of attrition is very high amongst the fund manager of various schemes as they are frequently changing their job to get higher package. This is cause of major concern as it is impacting the profitability and long term objectives of the schemes.
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- Mutual funds industry at present having minuscule share of household savings as majority of people still prefer to park their savings in banks and other safer avenue of investments. To overcome this customer education programme should be undertaken by AMFI in collaboration with other fund houses.

- To increase the pace of growth of the industry use of information technology should be promoted at a larger scale. This will reduce the time of transaction.

- The broker often engages in unethical practices of false projection about funds performance in order to generate brokerage on mobilised investment. This create negative image about the mutual funds industry and dissuade investors from investments.

- The distribution net work of the Indian mutual funds industry is very poor. It is mainly concentrated in big cities. The small towns and rural areas do not have distribution net work. To increase the penetration level of mutual funds in this semi urban and rural areas distribution channel should be open in these areas.

- Mutual funds can be offered online to the investors through the stock exchange. This can in one hand lower the cost of servicing the fund holder and on the other increase the penetration of mutual funds.

- The investors should have through knowledge about the funds before they make any investment. Therefore investment should be
preceded by tracking the performance of the funds over a period of time and different business cycles.

➤ The Indian mutual funds industry should develop product separately for the institutional and retail investors. This would prevent undesirable practices and protects the interest of the retail investors.

➤ The tax benefit should be made available only to retail investors and necessary regulations should be framed in this context.

➤ The institutional investors at present have share of 55 percent of the corpus this should be gradually reduced and the share of retail investors increased gradually.

➤ The net worth of the asset management company’s (AMC) should be gradually raised from Rs 10 crore to Rs 50 crore.

➤ The existence of variety of schemes and their different variant confuses the investors. This should be controlled and reduced gradually. The number of schemes launched should be directly proportional to the net owned funds.

➤ The inter-schemes transfer of funds should be gradually reduced and in no case permitted over the prescribed limits. As this will give undue advantage to one scheme at the cost of another.

➤ The Trustee of the company and the AMC should have separate identity. Though Trustee has the fiduciary responsibility but the
fee paid to it is too meager. The SEBI should frame necessary guidelines to compensate the Trustee for its valuable service. The other area of concern pertaining to the Trustee is that one Trustee is not allowed to be a member of another AMC this need to reviewed. The trustee should be allowed to play more active role in order to improve governance in mutual funds.

- The grievance redressal system in mutual funds is not matured as different mutual funds follow its own system of dealing with customer problems. Therefore there is an urgent need that a uniform system is developed by the SEBI to address the grievances of the client.

- To give relief to mutual funds investors suffering due to delay in grievance redressal SEBI can appoint MF Ombudsmen. This can bring relief to customer and instill confidence in them to invest in mutual funds.

- The SEBI should frame a code of conduct for the Indian mutual funds industry wherein a minimum service standard can be prescribed for each mutual funds operating in India. If any mutual funds are found violating these codes certain fine can be imposed.

- To bring about change in the present unit holding pattern where there is dominance of institutional investors. The awareness and educating programme can be carried out in small town and rural areas about advantages and disadvantages of investing in mutual
funds. This can help in attracting retail investment in mutual funds.

- The existing regulatory framework can be strengthened. Norms regarding valuations and disclosures should be formed.

- Mutual funds can be allowed to launch new products like pension funds. This will give boost to existing business.

- The entry and exit load should be abolished to ease the burden on investors. This will increase the participation of retail investors who find this cost too high to bear.

- To make investment in mutual funds more attractive a transparent fund utilization mechanism should be developed whereby investors are informed where their money will be invested.

- High operational cost and slow expansion of distribution network is another major challenge for the Indian Mutual funds industry. The lease rentals and staff costs contribute to the bulk of operational costs. The industry therefore should try to overcome this and bring efficiency in operation by adopting better technology and trained manpower.

5.4 Scope for Further Research

The present study is an empirical work based on secondary sources of information. The work is related to assess the impact of liberalization on the Indian mutual fund industry. The study also takes into account the performance of HDFC mutual funds. However it was not possible to
undertake all relevant issues of the subject matter in this single study. During the present study the researcher felt the need of further research.

Following directions are suggested:

- The performance evaluation of private and public sector mutual funds since liberalisation.
- The performance of different categories of schemes since liberalisation.
- The role of mutual funds in the mobilization of the household sector savings since liberalization.
- The problems and prospects of marketing strategy of the Indian mutual funds industry.