Chapter: 3

Role of Mutual Funds

“Management is doing things right; leadership is doing the right things.” Peter F. Drucker
3.1 Mutual Funds: The Growth Driver

The success story of any economy can only be scripted on the basis of sound financial system of the country. Economic reform process of 1991 had a great impact on the financial system of the country leading to the overall development of the Indian economy. Today, India's financial system is considered to be sound and stable as compared to many other Asian countries where the financial market is facing many crises. During last one decade or so, role of Indian mutual funds industry as a significant financial service in financial market has really been noteworthy. In fact, Mutual funds have emerged as an important segment of financial market of India, especially as a result of the initiatives taken by the Govt. Of India for resolving problems relating to UTI's US-64 and to liberalize tax liabilities on the incomes earned by the mutual funds. They now play a very significant role in channelizing the saving of millions of individual into the investment in equity and debt instruments.

The economic and financial scenario of India prior to 1991 was pathetic. Indian economy at that time was suffering from low savings, low GDP, high inflation, high unemployment, high rates of interest, low forex reserve etc. When India approached IMF for financial assistance in 1991, we were imposed certain condition on which the financial assistance was sanctioned to India. These restrictions which we accepted under the pressure from IMF were actually the starting point of economic reforms popularly known as LPG process. The result of the LPG process of 1991 is more clearly visible now. India is now being ranked as one of the fastest growing economy of the world. As the 11th five year
planning is about to start, we are already targeting a GDP growth of 9%. The saving of the country is now around 29%. Foreign investors are finding Indian market with high potential. India’s forex reserve is around $175 billion. Inflation is also at 5% which is considered good for developing economies. So, Indian economy is really booming today. Some experts have opined that, the share of the US in world GDP is expected to fall (from 21 per cent to 18 per cent) and that of India to rise (from 6 per cent to 11 per cent in 2025), and hence India will emerge as the third pole in the global economy after the US and China. All these favorable things could have not been possible without the sound financial market. It is the financial market which finances economic development. It is the financial market which channelizes the saving of the people into the investment. Indian financial markets are getting more and more institutionalized. Foreign investors, local institutions and mutual funds are now playing a bigger role. This is the case in developed markets. Mutual Fund is an instrument of investing money. Nowadays, bank rates have fallen down below the inflation rate. Therefore, keeping large amounts of money in bank is not a wise option, as in real terms the value of money decreases over a period of time. One of the options available is to invest the money in stock market. But a common investor is not well informed and competent enough to understand the complexities involved in the price movement of shares in the stock market. This is where mutual funds come to rescue them. The role of mutual funds will increase in the Indian markets also. This means that retail investors will opt for mutual funds. In the US, 35 to 40 per cent of the investments currently come through mutual funds while in India
it is very negligible. With the stock markets reaching to newer heights in 2006, mutual funds could not be far behind. Total assets under management of 30 funds rose by Rs 125,296 crore, or 63 per cent, to Rs 323,601 crore during the calendar year 2006, according to the data published by the Association of Mutual Funds of India (AMFI). Mutual funds saw record resource mobilization as investors lined up to take advantage of the stock market boom. Reliance Mutual Fund — controlled by the Anil Ambani group — has toppled Prudential ICICI MF as the country’s largest private sector fund house, while UTI MF retained its leading position across both public and private sector funds in December. The paper aims at analyzing the significant role played by the Mutual funds in Indian financial market by channelizing the saving of the investors (mostly of retail investors) into the investment in corporate.

3.2 Financial System of India

In order to critically examine the role of mutual funds in Indian financial market, we should first of all have a good idea about the Indian financial system. The financial system in India comprises of financial institutions, financial markets, financial instruments and services. Financial market refers to those places where financial assets are created and traded. Financial assets represent a claim for the payment of principal amount some times in future date and for periodic payment of money in the form of interest or dividends. The Reserve Bank of India (RBI) as the main regulator of credit is the apex institution in the financial system. Other important financial institutions are the commercial banks.
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(in the public and private sector), cooperative banks, regional rural banks and development banks. Non-bank financial institutions include finance and leasing companies and other institutions like LIC, GIC, UTI, Mutual funds, Provident Funds, Post Office Banks etc. The banking system is, by far, the most dominant segment of the financial sector accounting for over 80 per cent of the funds flowing through the financial sector. The Indian financial sector reforms aim at improving the productivity and efficiency of the economy. It remained stable, even when other markets in the Asian region were facing a crisis. The opening of the Indian financial market to foreign and private Indian players has resulted in increased competition and better product offerings to consumers. The main function of all these financial institution is financial intermediation i.e. facilitating the flow of saving from common man to industrial houses. In the initial stages, the role of the intermediary was mostly related to ensure transfer of funds from the lender to the borrower. This service was offered by banks, FIs, brokers, and dealers. However, as the financial system widened along with the developments taking place in the financial markets, the scope of its operations also widened. Some of the important intermediaries operating in the financial markets include; investment bankers, underwriters, stock exchanges, registrars, depositories, custodians, portfolio managers, mutual funds, financial advertisers financial consultants, primary dealers, satellite dealers, self regulatory organizations, etc.

Financial Markets are mainly classified as Money Market and Capital Market. The term money market is used to denote the financial institutions which deal with the short term borrowing and lending of money. The term capital
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market is used to mean the institutes which deals with the lending and borrowing of long-term money. Resource mobilization by mutual funds is an important activity in the capital markets. India’s mutual fund and stock market has witnessed phenomenal growth over the last few years. According to a study, mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, giving positive results. As India is targeting a GDP growth rate of 9% in the 11th Plan Period, the role of financial sector as well as the role of mutual funds industry in India as an important segment of financial market for resource mobilization in capital market is going to be very significant. The consistency in the performance of mutual funds has been a major factor that has attracted many investors. The mutual fund industry growth is estimated at about 50 per cent, far higher than that of bank fixed deposits which are growing at about 20 per cent.

3.3 Mutual Funds for Retail investors

Pure equity new fund offerings (NFOs) raked in a whopping Rs 32.309 crore in 2006, almost 33% more than the money raised by Indian corporates through initial and follow-on issues. This is a clear indication that retail investors are increasingly tapping the stock market through the mutual fund route. The mutual fund (MF), as a capital market intermediary, has emerged as new avenue for capital resources. It bridges the gap between retail investors and capital markets. According to Value Research data, the top five equity NFOs were Reliance Equity (Rs 5,790 crore), SBI Bluechip (Rs 2,850 crore), Reliance Long...
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Term Equity (Rs 2,100 crore), UTI Leadership Equity (Rs 2,080 crore) and Templeton India Equity Income (Rs 2,030 crore). Close to 40 NFOs were made in 2006 with average collections of Rs 950 crore. The top five IPOs of 2006 were made by the following companies — Cairn India (Rs 5,260 crore), Reliance Petroleum (Rs 2,700 crore), Bank of Baroda (Rs 1,633 crore), Parsvnath Developers (Rs 1,089 crore) and Lanco Infratech (Rs 1,067 crore). So, it is clearly evident that MF is providing more opportunities for the corporates to raise more funds. It is offering several options in structured forms. The industry is going to a major role model in the capital markets. According to a study conducted by the Associated Chambers of Commerce and Industry of India, the size of the mutual funds industry is expected to be worth Rs. 4 lakh crores by 2010. Mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, giving positive results. The consistency in the performance of mutual funds has been a major factor that has attracted many retail investors. 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. According a study, it has been found out that almost 54% of people invest for security and certainty while 38% of the people invest for current spending. Some 53% of the people prefer long term investment whereas 23% people each prefer medium term and small term investment. All these studies relate to retail investors. Actually, it is the consistence performance of mutual funds which is attracting retail investors towards it. Today, MF equity portfolio is worth around $32 billion, while individual investors own $88 billion. It is the Retail investors
who have been heavily investing in equities through MFs over the past couple of years. This observation can be made from the fact that close to $17 billion of NFO collections made in the last four years from equity funds. Eventually, money collected on these have made their way to equity market. On an average, MF net investments into equity markets remained around 50% of that by FIIs in the past three to four years. As Retail investor’s investments are typically long-term oriented, they are therefore important for maintaining stability in any equity market. Another very significant development for retail investors in the field of mutual funds is the entry of mutual funds in real estates. For the last three years the real estate sector has been growing at a fast pace of 30-40 %, especially in the metros. But for retail investors, participating in this growth was not easy. By opening the real estates investment for mutual funds, retail investors, who cannot invest directly in real estates which needs huge investments to start with, are actually allowed to investment in real estates through mutual funds. Retail investors are expected to account for 60% of the industry’s AUM. But this can be possible only if mutual funds in the country manage to enter into non-urban cities. This becomes more important because this is where saving deposits account for 49% of the total assets. These small towns account for only 30% of their holdings in mutual funds. So, one thing can be said for sure that retail investors are going to participate more and more in mutual funds in the times to come and thereby a lot of financial resources are going to be mobilized to financial market of India.
3.4 Money Market Mutual Funds

A money market fund is a mutual fund that invests solely in money market instruments. Money market instruments are forms of debt that mature in less than one year and are very liquid. Treasury bills make up the bulk of the money market instruments. Securities in the money market are relatively risk-free. Money market funds are generally the safest and most secure of mutual fund investments. The goal of a money-market fund is to preserve principal while yielding a modest return. Money-market mutual fund is similar to a high-yield bank account but can not be said to be entirely risk free. When investing in a money-market fund, one should be more attentive to the interest rate that is being offered. Money market mutual funds are very significant financial resource mobilizer for short term period.

During last few years, India’s position as a market with potential for long-term growth has really been noteworthy as the Indian economy is being ranked among the top 10 globally (in terms of GDP), and as the fourth-largest in terms of purchasing power parity (PPP). Another good thing to note about Indian mutual funds industry is that it has grown at a rapid pace of 16.4% during last 8 years as compared to global growth rate of 13% during the same period. However, when it comes to assets under management (AUM) of the global mutual fund (MF) industry, India’s ranks is 25th which is not very satisfactory, rather dismissal. With assets of around $76.5 billion (Rs 3.41 lakh crore) as per AMFI figures at the end of November ’06, India forms just 0.4% of the world’s global MF AUMs. MF assets worldwide stood at $19.41 trillion at the end of the second quarter of
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2006. US with $12.4 trillion of MF assets is the topper, followed by Luxembourg ($1.9 trillion), France ($1.6 trillion) and Australia ($723 billion). Another important criterion which is used by the analysts as parameter to judge the majority of a country's mutual fund industry is MF assets to GDP (PPP basis) ratio. According to available data, the ratio was 75.2% for US and 34.9% for UK. Even in the emerging economies' list, India's numbers were far from encouraging. The figure was 23.1% for Brazil, 26% for Russia, as compared to 1.3% for India. There are few other threats which Indian mutual fund is currently facing. Mutual funds must realize that there are some small saving schemes like NSC and PPF which are still offering high return than debt and income funds. Too much focus is being given to equity and any downswing in equity market would severely dent investor's confidence. Again, there is a lack of investor education which results in risk-return mismatch for investors investing in mutual funds. However, it can be said, in coming years, mutual fund industry is going to take off to newer heights. The Indian equity market has seen unbelievable rise in the last couple of years. From an index level of 5,590 as at March 31, 2004 to 14,000 during December, 2006, the markets have moved in top gear, at breathtaking speed, tumbling records after records in this unrelenting journey. The prices of gold and real estate have reached to sky high levels not only in India but also throughout the world. And both these traditional investment avenues have been extremely popular with Indian investors. Regulations have also favored these two classes of investments with the Securities and Exchange Board of India introducing norms for gold traded funds and the government relaxing...
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norms for foreign direct investments in real estate ventures. Retail investors have largely participated through mutual funds and this is clearly evident from the number of equity funds that have been launched in the last couple of years and the record collections they have witnessed. The Reserve Bank of India has relaxed norms for overseas investments thereby opening up more investment avenues. In recent years, SEBI has taken several steps to consolidate the Indian MF industry. There are some changes in guidelines that include standardization of the Funds Portfolios and disclosure of the balance sheet of the fund. Among other changes that are scheduled is reduction in the time taken by AMCs to complete formalities from 90 to 42 days. Also proposed is the use of unclaimed money for investor education. The present structure of funds is likely to change from the three-tier framework. This is expected to streamline the operations of the funds and will give them more flexibility. Finally, though mutual funds are primarily composed of stocks, there is a slight difference between these two which makes mutual funds more advantageous to the common investors. Diversification is the biggest advantage associated with mutual funds. Diversification is the idea of investing money across many different types of investment avenues. When one investment is not doing well other might be yielding good profit. Diversification reduces risk significantly. In addition to this, by purchasing mutual funds, one is actually hiring a professional manager at an especially inexpensive price. Now-a-days, a higher portion of investors' savings is now invested in market-linked avenues like mutual funds as compared to earlier times. However, if we compare proportion of people investing in mutual funds in India with that in U.S, then we find that in
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U.S more than 50% people invest in mutual funds whereas in India the proportion is less than 10%. This gives the indication that there is much more untapped potential for growth in this industry in India which must be explored in the coming time. In conclusion, it can be said that despite few problems, the recent changes in the mutual funds industry in India has really favored its amazing growth and in conclusion it can be said that in times to come mutual funds will continue to be a significant resource mobilizer in the Indian financial market.

3.5 Real Estate Mutual Funds: How Effective would it be

Financial reforms had great impact not only on Indian financial system but also on the Indian economy as a whole. Three sector of Indian financial system that have been greatly influenced and achieved substantial growth are Banking, Insurance and Mutual Funds. During the last one decade we have seen various positive developments in the field of mutual fund. Real estate which was till now out of the reach for common investors has been made available to small investor by SEBI. This has been made possible by allowing the entry of mutual fund players into the real estate. Though, it is said to be a very positive move yet it is to be seen how much positives will be there for investors in the time to come.

During the last one decade or so, the Indian economy has really broken the label of “constant and low growth economy”. This label was tagged with Indian economy for so many years. A lot of factors are responsible for this change. Undoubtedly, the financial reforms are the most vital reasons for this shift from
the traditional economy to new dynamic economy. The LPG process which started in India in 1991 has really given a boost to the growth rate of Indian economy which was for many years stagnant at around 3.5%. The three important areas of Indian Financial system which had most significant effect due to financial reforms are the Banking sector, the Insurance sector and the Mutual fund industry. In India, the mutual fund started with the formation of UTI in 1993-64. Then with the passage of time, many public sector, private sector and foreign sector players entered into the industry. Till 1999, U.T.I had the virtual monopoly in the mutual fund industry and controlled around 80% of all mutual fund assets. But now, it holds only something around 12% of mutual fund assets. Mutual Fund industry today, with about 34 players and more than five hundred schemes, is one of the most preferred investment avenues in India. The mutual fund industry reported a net inflow of Rs 11235 crore for the month of August as per AMFI data. However it had witnessed a net inflow of Rs 20302 crore in the month of July. Growth funds registered a net outflow of Rs 650 crore as against net outflow of Rs 209 crore in July 2006, while income and liquid funds saw a net inflow of Rs 7826 crore and Rs 3950 crore as against net inflow of Rs 5114 crore and Rs 15517 crore respectively in the previous month indicating the investor’s increasing preference for income funds as yields softened. Balanced Funds and ELSS also saw a net inflow of Rs 105 crore and Rs 98 crore respectively. The total assets under management of the mutual fund industry rose by 6.9% from Rs.287088 crore to Rs 307106 crore as on 3rd September, 2006.
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In a significant development, the SEBI (Security and Exchange Board of India) has recently permitted real estate mutual funds to invest directly in the immovable properties, mortgage-backed securities or in equity shares or bonds or debentures of listed or unlisted companies, which deal or undertake property development. In this context, it would be interesting to analyze what impact this new development is going to bring to already booming mutual fund industry and the financial market which is really showing signs of excellence in recent times. It is significant to note that the annual composite rate of growth in mutual fund industry is expected to be 13.4% during the rest of the decade and the global real-estate consulting group Knight Frank has ranked India 5th in the list of 30 emerging retail markets and predicted an impressive 20 per cent growth rate for the organized retail segment by 2010. With the liberalization of the economy and the consequent increase in business opportunities, India’s real estate sector has assumed growing importance. Indian real estate has huge potential demand in almost every sector, but especially commercial, residential, retail, industrial, hospitality, healthcare etc. For the last three years the real estate sector has been growing at a fast pace of 30-40 %, especially in the metros. But for retail investors, participating in this growth was not easy.

So far the only funds that were available were real estate venture funds, such as those launched by ICICI, HDFC, Pantaloon and Anand Rathi. These funds are affordable by only high net worth individuals, since the minimum amount of investment required is very high. The only securities available to the small investor are real estate stocks, but these tend to be volatile. For the small
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Investor to participate in the growth of the real estate market, he has to buy a property. Again, here the amount of investment required is very high at least Rs 15-20 lakh even if one wants to invest in a small apartment today. In addition to this, investment in properties is always subject to huge risk. Again, one has to ensure that the property which he is buying is free from legal litigation.

3.5.1 Current Scenario

Today, the Indian economy is growing at a faster and the real estate sector is growing even faster. As a result, in our economy, more and more money is chasing a limited quantity of high-quality property. This makes real estate investment potentially one of the best investment opportunities available. But it is the high price and high transaction cost which causes difficulty for a small investor to take part in this booming sector. Fortunately, a new investment product known as real estate mutual fund is being developed which will make it easier for the average investor to invest his or her hard-earned money in real estate. In order to be called Real Estate Mutual Funds (REMF), these MFs will invest directly or indirectly in real estate property and shall be governed by the provisions and guidelines under SEBI (mutual funds) regulations. In other words, this new category of mutual funds can buy real estate as well as purchase shares of real estate companies. Real estate development across the country has been estimated at US$15 billion and growing at the rate of 30 per cent every year. The cumulative impact of liberalized FDI (Foreign Direct Investment) norms and the recent SEBI’s decision to permit real estate mutual funds are expected to take...
the realty sector to a new high of US$102 billion in the next 10 years. A research by Indian Venture Capital Journal reveals that the corporate fund size of 21 real estate funds operating in India is US$4.7 billion. Till now, as the real estate investment needs huge money, it was beyond the capacity of retail investors. By opening up this sector to the mutual funds industry, retail investors have been given a unique opportunity to enter into the high profit making zone. Property prices in India are rising fast, and not just in the biggest cities. As the tech boom spreads across the country, as more Indians by virtue of growth of their income buy homes, and as the economy grows at faster than 8% a year, real estate is and will be attracting more investors, even many of them from abroad. India is said to be the most exciting real estate market in Asia. This improvement is a matter of worries for some. Concerns about an asset-price bubble have led the Reserve Bank of India to raise the risk weightage on real estate loans extended by banks, and mortgage rates have gone up from 7.5% to about 9.5% as a result. That's still well below the 15% rates that most Indians were used to, but it's enough to raise questions about whether the speculation of the past year and a half, which has driven land prices up by 30% to 100% and real estate stocks up as much as 2,000%, may be coming to an end.

According to a report on real estate trends by Merrill Lynch the number of malls in Mumbai, Bangalore, New Delhi, Hyderabad and Pune would grow to about 250 by 2010 as against 40 now. Again, in term of total area, there was 12.40 million square feet (mnsqft) of mall space available in these cities. As the competition in the market is intense, builders are going out of their way to be
different. Specialized malls have become the order of the day. Gurgaon, on the suburbs of New Delhi will soon have an auto mall, while Bangalore is about to get an exclusive furniture mall. Gurgaon is set to get the biggest mall of the world — a large US$ 89.78 sq ft sprawling property that is being developed by DLF Universal. It will be known as Mall of India. Similarly in the home segment, which is driven by the availability of easy home finance, most builders are trying to woo investors with interesting features, each more tempting than the other.

The main aim of the article is to critically analyze the impact of mutual funds entering into real estates on the overall financial scenario and growth. It becomes very relevant to analyze how the mutual funds are going to take the advantage of the booming real estate market in India. The real estate market in the country currently stands at $12 billion in terms of revenues and may reach $50 billion by '10. The domestic real estate market is among the high-yielding markets globally. Yields from prime grade A office space are 9-12% here, compared to 4-7% in the US and Europe. Over the past few years, real estate has emerged as an investment alternative option. However, until recent times, participation in the realty sector was limited to direct investment in individual properties.

3.5.2 Looking Ahead

Like mutual funds, real estate funds (or Real Estate Investment Trusts – REITs as they are commonly referred to in the US) are founded by a group of real estate professionals/experts to 'manage' property/real estate for the investor. The real estate mutual fund industry in the US has evolved into a concept called the
REIT, the Real Estate Investment Trust. It is a publicly listed entity, which basically passes on at least 90% of its profits to investors. REITs typically own large commercial office spaces, hotels and rely mainly on rental incomes. However, there are some that are more focused on capital appreciation as well. REITs buy, develop and sell property and share profits with investors/unitholders from any capital appreciation on the sale of property. Apart from sale of property, real estate funds also make money from rentals on property owned by them. Some real estate funds may not actually own property as that may involve above-average risk from volatility in property prices. Instead such funds invest in bonds/instruments that are secured by property. The coupon rate that they receive on these bonds/instruments is then distributed to investors/unit holders as dividends. While real estate funds have just announced their arrival in the country, real estate as an asset class has been around for some time. Whenever a 'new' sector comes on the screen, there is an interest, in general. Real Estate, though an old asset class, is for the first time being opened up to retail Indian and foreign participation. The fact that the last few years has seen rise in prices and volumes has helped the cause.

The objectives behind the setting up of REMFs are to provide the property market with an investor base and investors with an attractive investment option so that both can be benefited simultaneously. Real Estate is emerging as a new asset class and is expected to fight for its share of the cake with traditional asset classes like equities and debt. Real-estate mutual funds have already made a mark in several countries and are raring to enter the mutual fund arena in India.
Role of Mutual Funds soon. The first step towards REMFs in India was initiated by the capital market regulator, Securities and Exchange Board of India, by issuing the norms for REMFs. But, this asset class would get a shot in the arm only after setting up of real estate investment trusts (REITs), as is the practice internationally. They infuse confidence among investors, because they also serve as custodians of title deeds. REITs pool various real estate assets, including warehouses, buildings, industrial estates and parks, malls, commercial and residential premises and get listed on the stock exchange to enable investors to buy and sell. They afford an opportunity to diversify the portfolio within that limited sense as well. The only way, so far, for ordinary individuals to invest in property was to buy one. This has several disadvantages, primary one being the huge outlay required to put up even the large upfront amount. Things are, however, set to change. SEBI has cleared the formation of real estate mutual funds. This is a landmark step and will have huge implications not only for investors wanting to invest in real estate but also for the property market itself.

The mode of operation of REMFs is just like that of any mutual fund. While existing mutual funds invest in stocks, debt and money market instruments, REMFs will also be able to invest in physical property. Like any mutual fund, it will pool the contributions from a number of subscribers and invest that money. As per news reports, Sebi guidelines are likely to permit such funds to invest not only in shares of companies associated with the real estate market but also in mortgage backed securities and physical property. These reports also say that these funds are initially likely to be close ended and will be compulsorily listed on
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the stock exchanges. A close ended structure -- in which subscription and redemption is not open on an ongoing basis -- will be ideal for such funds. Investment in property is a long term game and a close ended structure will ensure that the fund has a stable corpus to play around with. Liquidity for investors will be available on the stock exchanges where the units of such a fund will be listed. The guidelines also are likely to mandate daily declaration of fund NAV. Such funds can record gains and income through various sources. While appreciation in shares of companies it invests in is one source, such a fund also earns capital gains through appreciation in the properties it invests in. Income comes from dividends, interest on the securities it invests in. Globally, such funds also earn significant amount of income from rental income of developed properties it buys up. The primary advantage of these funds will be that it will make investment in the real estate asset class accessible to a lot more people. Real estate, like debt, equity, gold etc. is also an asset class. Till now, ordinary investors could only in real estate asset class by putting up a huge amount of money upfront. In the case of a real estate mutual fund the minimum investment amount is likely to be a few thousand rupees. This will enable even small investors to take exposure to real estate and diversify their portfolio.

Whenever a 'new' sector comes on the screen, there is an interest, in general. Real Estate, though an old asset class, is for the first time being opened up to retail Indian and foreign participation. One thing is for sure that the regulator (SEBI) has set the ball rolling for real estate funds. But, it will be some time before retail investors can begin investing in real estate funds and making
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profit. As of now, the real estate window is open only to high net worth individuals (HNIs), institutional investors and global investors. From small investors point of view, REMF provide the following advantages:

1. Affordable: Small investors will be able to begin investing in real estate mutual funds with as little as Rs 1,000 as is the case with debt and equity mutual funds.

2. Mitigate risks: Many of the risks involved in investing in real estate will be taken care of by the fund manager looking after the fund. These professionals will have the capability to ensure that the project is free of legal encumbrances. They will also be able to carry out due diligence and determine whether the developer’s project is worth investing in.

3. Sound advice: When general people invest in equity fund, this is simply because they do not have sufficient time and experience to select right equity shares themselves. Similarly, making the right real estate investment is not easy for the lay investor. By investing in the fund, he gets the right advice. Hence the choice of the fund becomes very important.

4. Liquidity: Real estate mutual funds are likely to be launched as close ended funds which will trade on the stock exchange. Investors can realize their investments by selling them at the exchange. This will be far easier than exiting from an investment in a property, where the process is very cumbersome. Also, it will be easier to sell off a part of your real estate mutual fund investments.

3.5.3 DIFFICULTIES TO ENCOUNTER

But, there are difficulties: Real estate funds have the same risks that are associated with equity/debt mutual funds. For instance i.e. one could make the
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wrong choice while selecting a real estate fund in which case one has to lose money as it could be in any other cases as equity or debt fund. If with equities three years is the minimum investment time frame, then with real estate investments one has to be even more patient. Buying property, developing it and then renting it out or selling it, is a high gestation activity. It could take some time before real estate mutual fund actually starts making money. The major risk involved in investing in REMFs is that they are sector specific funds. The real estate sector may be booming now, but there will be long term problems when this sector will be going through difficult phases. A typical property market cycle tends to be much longer than a business cycle. Returns from real estate mutual funds are bound to get affected during the period when the property market is depressed. The road to real estate mutual fund investing is not smooth. It is well known that the Indian real estate and property market is opaque and disorganized. Payment in 'black' in order to evade capital gains and stamp duties is common. Thus, these funds will have a huge problem in acquiring or investing in clean properties. Many buildings in India also do not conform to building guidelines that is an additional risk the funds will have to take on. Even a basic task such as calculation of net asset value (NAV) is fraught with difficulties. The guidelines are likely to mandate daily declaration of NAV. However, since there is no exchange or any other means by which the value of physical properties are discovered everyday, it is not yet clear how physical properties held by a mutual fund will be valued for the purposes of NAV calculation. If a person is investing in property; he has to pay registration cost. In developed markets in the west, the
registration cost does not exceed 3-5% of the cost of property. But in India some states have lowered it to 6-8%, while others continue to demand as much as 14-16%. This adds further to the cost of investing in property.

On the positive side, though the entry of such mutual funds is likely to force the hand of the various people involved in property trade and construction to get their act together. Such funds will be a valuable source of capital and those wanting to access it will have to change the way they function. The government too will need to initiate reform and lower stamp duties, which encourage evasion in the first place. On the whole this development needs to be welcomed. The prospects for the real estate sector indeed are bright; a substantial amount of gains in prices has already taken place. Investors would benefit from taking part in the real estate story.

However, the real estate sector has many components - residential, office, retail (malls), hospitality (hotels, resorts). The fund manager will usually diversify across these sub-sectors to reduce risk, since not all these sub-sectors move in tandem. Thus, the launch of real estate mutual funds is one of the most important pieces of news to have emerged out of the real estate sector this year. But, investors has to be very careful while choosing the right avenue in mutual funds to invest in real estate. Otherwise, they may end up losing their money in this booming sector too. The entry of mutual fund is not only good news for investors in mutual funds but also for the real estate sector as more funds will be available. And if domestic funds are available, builders will not have to depend on FDI, where there are restrictions regarding the minimum size of investment of 50,000
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sq m in commercial developments or 25 acres in residential developments. There are indications that less bank funds might be available to developers for acquiring land banks. Earlier banks used to give loan to builders at easier terms and condition for acquiring properties. As a result of this lot of money was chasing the available land and the prices of properties started rising. The resulted in hiking the risk weightage by RBI to this sector. So, now the mutual funds can fill the need gap by providing necessary fund to developers. One thing which can be surely said at this point of time is that from a longer term perspective, entry of mutual funds in real estates is undoubtedly a positive move. It will give us a new class of asset to invest. One would be able to get in and get out and put small sums of money, which retail investors could not put in the real estate. In terms of the market opportunity, this development is a right step in right direction.

3.6 Mutual Funds Investment: A Long Term Saving Vehicle

The booming Indian financial market has lot to do with the booming Indian economy. It is the financial market which finances economic activities of any country. Capital market provides long term finance whereas money market provides short term finance. One of the important functions of the financial market is to mobilize the saving of the people into the investments in corporate. Mutual funds have emerged as an important segment of financial market of India, especially as a result of the initiatives taken by the Govt. Of India for resolving problems relating to UTI’s US-64 and to liberalize tax liabilities on the incomes earned by the mutual funds. Indian mutual funds industry has matched in steps with the country’s booming capital market. In the recent years, mutual funds
Role of Mutual Funds

have emerged as long term saving vehicle for retail investors. People are benefiting more by investing in mutual funds for a longer period of time unlike earlier time when people used to use mutual funds investment as very short investment vehicle. This article attempts to study this new dimension of the mutual funds industry in India.

Indian economy is the undoubtedly on the path of high GDP growth and this growth rate of over 8% is also expected to continue. The main factors which are responsible for this growth are consumer's preference for current consumption, capital expenditure/infrastructure creation and the booming financial market of the country. The stock market is also reflecting the underlying fundamental growth and hence over the next few years, one can be bullish on the Indian economy as well as markets. In recent times, the stock market has broken all time records. From investment's point of view, many sectors are looking promising at this point in time. Most of the mutual fund companies are focusing on the sectors like IT, infrastructure (engineering, capital goods, and construction), banking, telecom and automobiles as they are booming. The continued robust growth has increased the reliability to raise resources from the capital market and hence the year 2007 is expected to be one of the biggest years for the Indian entrepreneurship. It is expected that the market capitalization of the Indian stock market would cross the magic figure of one trillion US dollars ($1,000 billion) in 2007-08. The current market capitalization of National Stock Exchange (NSE)-listed companies is $834 billion which is 91.5 per cent of the gross domestic products. In term of market capitalization, India is at the fourth
position in the world only after the US $17,400 billion, Japan $4,800 billion and China $1,000 billion. In the year 2006, we have also witnessed the emergence of a strong and vibrant mutual funds industry. This is a clear indication of the fact that the Indian investors are now investing in the capital market through the institutional route. It has been estimated that the net mobilization of funds by the mutual funds industry has increased by four times to Rs 104,950 crore in 2006 as against Rs 25,454 crore in 2005. Buoyant inflows were seen in both debt and equity funds, which has taken the total mutual fund industry size to Rs 323.593 crore. The inflows which were negative in 2004 turned out to be positive for the public sector mutual funds in 2005 and accelerated further in 2006. The scenario for the mutual funds industry probably was never ever as better as today, so far as the entry of individual or retail investors is concerned. It is for the first time ever that the individual investor is set to account for half the assets under management (AUM). The retails investors are now investing billions of dollars into funds. The share of corporate investors, on the other hand, has been dropping, which indicate that more retail investors see mutual funds as a preferred avenue for investing in the markets. In March 2004, the share of individual investors was 33% of AUM, while corporates were 65%. Non-resident Indians (NRIs) were at 1% and FIIs at 0.5%. The shares changed dramatically by March 2006, with the individual investor taking 43%, corporates 51%, NRIs 5% and FIIs 1%. The AUM was Rs 2,07,979 crore in January 2006, which stood at Rs 2,31,862 crore by March last year.
In developed markets, mutual funds have proved to be the ideal vehicle for retail investors to take advantage of the excellent long-term growth of stock markets. In fact, in terms of assets under management, the mutual fund industry in the US has overtaken the banking industry. In India, the mutual fund industry is relatively not as developed, both as regards the number of players and products on offer. But the things which is noteworthy is that Indian mutual funds industry has not been able to maintain a pace with our booming capital market step by step but has also maintained a better risk profile for retails investors. This article aims to critically analyze the significance of mutual funds investment by the retail investors as a long term investment avenue.

Financial Markets are mainly classified as Money Market and Capital Market. The term money market is used to denote the financial institutions which deal with the short term borrowing and lending of money. The term capital market is used to mean the institutes which deals with the lending and borrowing of long-term money. Resource mobilization by mutual funds is an important activity in the capital markets. India’s mutual fund and stock market has witnessed phenomenal growth over the last few years. According to a study, mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, giving positive results. As India is targeting a GDP growth rate of 9% in the 11th Plan Period, the role of financial sector as well the role of mutual funds industry in India as an important segment of financial market for resource mobilization in capital market is going to be very significant. The consistency in the performance of mutual funds has been a major
factor that has attracted many investors. In developed financial markets, like the United States, Mutual Funds have almost overtaken bank deposits and total assets of insurance funds. As of date, in the US alone there are over 5,000 Mutual Funds with total assets of over US $ 3 trillion (Rs. 100 lakh crores). In India, the Mutual Fund industry started with the setting up 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. This fast growing industry is regulated by the Securities and Exchange Board of India (SEBI). The mutual fund industry growth is estimated at about 50 per cent, far higher than that of bank fixed deposits which are growing at about 20 per cent.

3.6.1 Mutual Funds: A Better Option for Retail Investors

In the year 2006, Pure equity new fund offerings (NFOs) raised huge amount of Rs 32,309 crore in 2006, almost 33% more than the money raised by Indian corporates through initial and follow-on issues. This is a clear indication that retail investors are increasingly tapping the stock market through the mutual fund route. The mutual fund (MF), as a capital market intermediary, has emerged as new avenue for capital resources. It bridges the gap between retail investors and capital markets. According to Value Research data, Reliance Equity (Rs 5,790 crore), SBI Bluechip (Rs 2,850 crore), Reliance Long Term Equity (Rs 2,100 crore), UTI Leadership Equity (Rs 2,080 crore) and Templeton India Equity Income (Rs 2,030 crore) were the top five equity NFOs. In year 2006, some 40
NFOs were made in with average collections of Rs 950 crore. Cairn India (Rs 5,260 crore), Reliance Petroleum (Rs 2,700 crore), Bank of Baroda (Rs 1,633 crore), Parsvnath Developers (Rs 1,089 crore) and Lanco Infratech (Rs 1,067 crore) respectively made the top five IPOs of 2006. So, it is clearly evident that MF is providing more opportunities for the corporates to raise more funds. It is offering several options in structured forms. The industry is going to be a major role model in the capital markets. According to a study conducted by the Associated Chambers of Commerce and Industry of India, the size of the mutual funds industry is expected to be worth Rs. 4 lakh crores by 2010. Mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, and thereby giving positive results. The consistency in the performance of mutual funds has been a major factor that has attracted many retail investors. 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. According a study, it has been found out that almost 54 % of people invest for security and certainty while 38 % of the people invest for current spending. Some 53 % of the people prefer long term investment whereas 23% people each prefer medium term and small term investment. All these studies relate to retail investors. Actually, it is the consistence performance of mutual funds which is attracting retail investors towards it. Today, MF equity portfolio is worth around $32 billion, while individual investors own $88 billion. It is the Retail investors who have been heavily investing in equities through MFs over the past couple of years. This observation can be made from the fact that close to $17 billion of
NFO collections made in the last four years from equity funds. Eventually, money collected on these have made their way to equity market. On an average, MF net investments into equity markets remained around 50% of that by FIIIs in the past three to four years. As Retail investor's investments are typically long-term oriented, they are therefore important for maintaining stability in any equity market. Another very significant development for retail investors in the field of mutual funds is the entry of mutual funds in real estates. For the last three years the real estate sector has been growing at a fast pace of 30-40 %, especially in the metros. But for retail investors, participating in this growth was not easy. By opening the real estates investment for mutual funds, retail investors, who cannot invest directly in real estates which needs huge investments to start with, are actually allowed to investment in real estates through mutual funds. Retail investors are expected to account for 60% of the industry's AUM. But this can be possible only if mutual funds in the country manage to enter into non-urban cities. This becomes more important because this is where saving deposits account for 49% of the total assets. These small towns account for only 30% of their holdings in mutual funds. So, one thing can be said for sure that retail investors are going to participate more and more in mutual funds in the times to come and thereby a lot of financial resources are going to be mobilized to financial market of India.

3.6.2 Mutual funds as a long term investment option

Mutual funds have become a significant source of investment in both government and corporate securities. Earlier, Investing for the long term (3-5
Role of Mutual Funds

Yrs) was a problem for mutual fund investors as they were not willing to hold the funds for such a long period of time. Even if investors believe that equities work best over the long-term, there aren’t a whole of mutual funds that cater to them. In the recent past we have seen some mutual funds correct this anomaly by walking the talk as far as long-term investing is concerned. One of the options available mutual fund investors is to consider investing in tax-saving funds. Tax-saving funds have a 3-Yr lock-in, which affords the fund manager the luxury to make long-term investment calls. It is heartening to note that recently fund houses have identified the problem of lack of long-term investment opportunities and have tried to resolve the problem in two ways. One of the ways which has been adopted by the fund managers is by promoting long-term investments in mutual funds through different measures like waiver of entry loads on systematic investment plans (SIPs). To discourage investors from exiting SIP investments prematurely, redemptions within 12 months are charged with an exit load. Some fund houses are getting more proactive and telling investors upfront the ideal investment time frame for a particular scheme. At least one fund house’s fact sheet mentions very clearly the ideal investment horizon for each of its scheme; equity schemes of the fund house have a time frame of 5 years. The following table will give an idea about the long term growth:-
Role of Mutual Funds

Long-term investing delivers

<table>
<thead>
<tr>
<th>Equity funds</th>
<th>NAV (Rs)</th>
<th>6-Mth</th>
<th>1-Yr</th>
<th>3-Yr</th>
</tr>
</thead>
<tbody>
<tr>
<td>RELIANCE GROWTH G</td>
<td>103.83</td>
<td>52.98%</td>
<td>43.47%</td>
<td>71.71%</td>
</tr>
<tr>
<td>RELIANCE VISION G</td>
<td>76.86</td>
<td>40.46%</td>
<td>23.32%</td>
<td>70.09%</td>
</tr>
<tr>
<td>FRANKLIN INDIA PRIMA FUND G</td>
<td>101.2</td>
<td>46.94%</td>
<td>37.81%</td>
<td>69.21%</td>
</tr>
<tr>
<td>HDFC LONG TERM ADV. G</td>
<td>45.58</td>
<td>51.16%</td>
<td>47.57%</td>
<td>66.17%</td>
</tr>
<tr>
<td>UTI MASTER VALUE</td>
<td>28.42</td>
<td>41.89%</td>
<td>26.00%</td>
<td>54.75%</td>
</tr>
<tr>
<td>TATA EQUITY OPPORTUNITY A</td>
<td>25.95</td>
<td>40.80%</td>
<td>28.78%</td>
<td>54.56%</td>
</tr>
<tr>
<td>HDFC CAPITAL BLD. G</td>
<td>32.77</td>
<td>51.35%</td>
<td>46.60%</td>
<td>51.96%</td>
</tr>
<tr>
<td>HDFC TOP 200 G</td>
<td>48.56</td>
<td>37.53%</td>
<td>32.28%</td>
<td>51.05%</td>
</tr>
<tr>
<td>HDFC TAX SAVER G</td>
<td>58.56</td>
<td>57.58%</td>
<td>50.59%</td>
<td>50.94%</td>
</tr>
<tr>
<td>DSP ML OPP G</td>
<td>24.24</td>
<td>38.04%</td>
<td>33.66%</td>
<td>50.93%</td>
</tr>
</tbody>
</table>

(Source: Credence Analytics. NAV data as on Dec 3, 2004. Growth over 1-Yr is compounded annualised)

A fund that permits the fund manager to make long-term investment decisions not only stands a better chance of meeting the investment objective of long-term capital appreciation but is also likely to do this at lower turbulence in performance. For a long time, mutual funds have been perceived as an investment avenue for investors in the higher tax bracket, with nothing in it for investors in the lower bracket. However, that perception is changing gradually. Generally, mutual funds take a backseat to investment avenues like bank deposits and company fixed deposits, which are considered more 'safe'. Safety apart, mutual funds are deemed as the preferred investment option for investors in the higher tax bracket, with nothing in it for investors in the lower bracket. Basically, there is a rationale for investing in mutual funds even without the tax benefit. A mutual fund (income fund) is able to invest in many securities that are not available as investment options to the individual investor. Examples of these are Government Securities, Preference Shares, Treasury Bills etc. These investment alternatives enable mutual funds to earn returns that are in excess of those available to retail...
investors. Add to it the fact that returns are tax-free in the hands of the investors, the funds are professionally managed and the investment is far more liquid. Moreover, investors get a chance to see their portfolios and know where their money is going. Due to these reasons, mutual funds are not only attractive to investors in the higher tax bracket, but are also viable investment avenues for all investors irrespective of the tax considerations. According to a report, the mutual fund industry has grown about four-times to $65 billion in terms of their total asset size since 1993, while the industry’s contribution to the country’s GDP has also grown in the past decade to nearly 10 per cent. With rising per-capita income, awareness of capital market investing and pension fund reforms would make mutual fund investing a viable long-term investment vehicle. There are different new schemes that include — assured return, balanced, floating rate, fund of funds, gilt, growth, income, liquid and money market funds. It has been estimated that Mutual funds have added over 18.5 lakh investors in the third quarter of current fiscal taking the total investor base to 2.67 crore.

3.6.3 Future prospects of the Mutual funds industry

Undoubtedly the start of the mutual funds industry in India was slow but steady. But what is heartening to note is that after such a slow start, the industry has picked up and is presently going phase which can be described as interesting one. The last few years have really been noteworthy for the industry. Today, mutual funds have become popular among the customers and have gained wide acceptability as a savings vehicle among the investors. The performance of many
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funds has been good, a strong distribution network has been established, products are in line with customer preference and requirements and the industry on the whole is on a growth path.

During last few years, India’s position as a market with potential for long-term growth has really been noteworthy as the Indian economy is being ranked among the top 10 globally (in terms of GDP), and as the fourth-largest in terms of purchasing power parity (PPP). Another good thing to note about Indian mutual funds industry is that it has grown at a rapid pace of 16.4% during last 8 years as compared to global growth rate of 13% during the same period. However, when it comes to assets under management (AUM) of the global mutual fund (MF) industry, India’s ranks is 25th which is not very satisfactory, rather dismissal. With assets of around $76.5 billion (Rs 3.41 lakh crore) as per AMFI figures at the end of November '06, India forms just 0.4% of the world’s global MF AUMs. MF assets worldwide stood at $19.41 trillion at the end of the second quarter of 2006. US with $12.4 trillion of MF assets is the topper, followed by Luxembourg ($1.9 trillion), France ($1.6 trillion) and Australia ($723 billion).

Another important criterion which is used by the analysts as parameter to judge the majority of a country’s mutual fund industry is MF assets to GDP (PPP basis) ratio. According to available data, the ratio was 75.2% for US and 34.9% for U.K. Even in the emerging economies’ list, India’s numbers were far from encouraging. The figure was 23.1% for Brazil, 26% for Russia, as compared to 1.3% for India. There are few other threats which Indian mutual fund is currently facing. Mutual funds must realize that there are some small saving schemes like
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NSC and PPF which are still offering high return than debt and income funds. Too much focus is being given to equity and any downswing in equity market would severely dent investor's confidence. However there are certain issues which must be addressed soon. The Indian mutual funds industry has to further strengthen its distribution network so that a wider base can be tapped. This issue must be given immediate attention. Education of both investors and distributors is needed. The second issue is related with the fixed rate of interest which people have got used to with Banking and other system. Peoples have not yet been able to understand the risk-return trade-off fully. Thirdly, investor expectations are very high. It must be understood that mutual funds cannot turn out magic - investors must expect only reasonable returns. Another important issue is related with pension funds. This must be opened up - professional fund managers must be allowed to manage pension funds.

3.7 MFs Industry in India: A SWOT Analysis

Financial reforms had great impact not only on Indian financial system but also on the Indian economy as a whole. The booming Indian financial market has lot to do with the booming Indian economy. It is the financial market which finances economic activities of any country. Indian economy is projected to grow at over 9 % during the 11th the plan. To support such a growth, we need very sound financial market. During last one decade or so, the MF industry has not only registered a very fast growth rate, we have also seen various positive developments in the field of mutual fund. The tremendous growth of Indian
Role of Mutual Funds

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. So, our financial market as well as mutual funds industry is attaining maturity. In this context, it would be very interesting to make a SWOT analysis of the MF industry in India and watch out for the future trends in the Indian MF industry.

On the eve of 11th planning Indian economy is in a very comfortable position. We never started our any five year planning with such a favorable position. India has achieved a growth rate of over 8% for the third consecutive year. The infrastructure related problems as a threat to country’s economic development is being solved to some extent through public, private, domestic and foreign investments. The productivity scenario of India’s economy is growing at a faster rate today. This can be indicated by that fact that both the savings and investment rates in the country are growing very rapidly. As far as the current data is concerned, India’s saving rate is 32 percent of the total GDP and investment is of 34 percent. Both these indicators are expected to rise even faster in the years to come. The result of the LPG process of 1991 is more clearly visible now. India is now being ranked as one of the fastest growing economy of the world. As the 11th five year planning has started, we are already targeting a GDP growth of 9%. The saving of the country is now around 29%. Foreign investors are finding Indian market with high potential. India’s forex reserve is around $175 billion. Inflation is also at 6% which is slightly above the desired
level. However, this is not a very matter of big concern right now. So, one thing that is for sure is that our economy is booming as never before.

The mutual fund industry in India came into being in 1963 with the setting up of the Unit Trust of India (UTI). In 1987, Public Sector Banks and Insurance Companies opened their own mutual funds, thus starting the second phase in the growth of the mutual funds industry. By the end of 1988, the industry's total assets under management (AUM) reached Rs. 67 billion. The industry registered a major milestone in 1993 when the first private sector player, the erstwhile Kothari Pioneer Mutual Fund (now merged with Franklin Templeton), was set up. Since then, several international players have also entered the fray. The industry has also witnessed a spate of mergers and acquisitions, the most recent ones being the acquisition of Alliance Mutual by Birla Sun Life, GIC Mutual by Canbank Mutual, and Sun F&C by Principal Mutual. Mutual fund (MF) industry in India has finally come of age. Asset management companies are increasingly getting their act more organized. Unlike the traditional yesteryears, MF houses are now looking at brand building. The size of mutual fund industry is expected to be worth Rs 4000bn by 2010 from its current level of over Rs2000bn as this industry will keep growing at a CAGR of around 17%, according to a Study conducted by The Associated Chambers of Commerce and Industry of India (ASSOCHAM) on 'Mutual Fund : Future's Wealth Creator and Wealth Saviour'. Presently, the domestic mutual fund industry is about Rs 3.39 lakh crore managed collectively by some 30 odd AMCs. The good news is that the total assets being managed by the mutual funds industry in India has risen by 63.1% in the last one year. But, the
assets under management (AUM) are still concentrated with the big boys of the industry. While the top 5 fund houses accounted for 47.9% of the total AUM of Rs 2.18 lakh crore in February 2006, they continued to account for approximately the same proportion in February 2007 (49.95% of the total AUM of Rs 3.56 lakh crore). It picture doesn’t get any better if one were to take the top 10 funds - they account for 72.83% of the total AUM as compared with 73.41% a year ago. Though the growth rates of AUM in some of the smaller houses has been phenomenal, they haven’t been able to do anything significant to topple the dominance of the big league. Industry analysts say that the top 5 fund houses - UTI, Reliance, Prudential ICICI, HDFC and Franklin Templeton - are household names in India. As a result, these brands tend to collect more money in their schemes, becoming more profitable and, hence, are able to spend more on advertising and distribution expenses. As the cycle completes itself, they tend to collect more money. The penetration of mutual funds in rural areas is relatively low with 13.7 per cent of urban households owning mutual funds against only 3.8 per cent of rural households”.

3.7.1 Strengths of the Industry

. Mutual Fund is an instrument of investing money. Nowadays, bank rates are just slightly higher than the inflation rate. Therefore, keeping large amounts of money in bank is not a wise option, as in real terms the value of money decreases over a period of time. One of the options available is to invest the money in stock market. But a common investor is not well informed and
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competent enough to understand the complexities involved in the price movement of shares in the stock market. This is where mutual funds come to rescue them. The role of mutual funds will increase in the Indian markets also. This means that retail investors will opt for mutual funds. In the US, 35 to 40 per cent of the investments currently come through mutual funds while in India it is very negligible. With the stock markets reaching to newer heights in 2006, mutual funds could not be far behind. Total assets under management of 30 funds rose by Rs 125,296 crore, or 63 per cent, to Rs 323,601 crore during the calendar year 2006, according to the data published by the Association of Mutual Funds of India (AMFI). Mutual funds saw record resource mobilization as investors lined up to take advantage of the stock market boom. Undoubtedly Mutual funds are one of the most sought after investment avenues for the investors. But what makes it so special. Indian economy is growing very fast and we are sure to attain the growth rate of around 9% in the 11th planning period. But this does not make stock market less volatile. Inflation is also rising very fast and bank rate of interest is not much higher than the current inflation rate. So, investing in stock market as well in bank is not attracting the common investor to the desired extent. In such volatile times, it is the mutual funds become the obvious choice for investors not only for the individual but also for the corporate. The assets under management for the mutual fund industry have nearly doubled in the past two years. At Rs 3,53,300 crore, the size of the industry is sure to grow further. It is forecasted by the Industry experts that its size would easily treble in the next five years and there would be significant additions to the 32 players currently operating in the
market place. In developed markets, mutual funds have proved to be the ideal vehicle for retail investors to take advantage of the excellent long-term growth of stock markets. In fact, in terms of assets under management, the banking industry is lagging behind the mutual funds industry. In India, the mutual fund industry is relatively not as developed, both as regards the number of players and products on offer. But the things which is noteworthy is that Indian mutual funds industry has not been able to maintain a pace with our booming capital market step by step but has also maintained a better risk profile for retails investors. Mutual funds as an investment avenue has the following strengths:

**Convenience:** An investor must keep track of investments, if he wants it to be profitable, which takes time and effort. But incase of mutual funds, the investor pass on this function to funds manager.

**Expertise:** Mutual funds employ experienced professionals to research investment options. This probably would be a very big task on part of an individual investor with a moderate knowledge of investment.

**Returns:** Mutual funds have the potential to provide favorable returns within the same risk category. The mutual fund industry in India has performed credibly over the past year. According to a study conducted by the Association of Mutual Funds in India, of the 118 equity schemes in the market, 91 outperformed the benchmark Bombay Stock Exchange Sensex.

**Lower expenses:** For investing directly in market, one has to bear several costs. These include brokerage, stamp duty and custodial charges, in addition to the expenses incurred in tracking your share portfolio. Mutual funds too have to bear
these costs, but economies of scale enable them to reduce procedural expenses like these.

**Risk Reduction:** An investor with a small amount of capital cannot maintain a much diversified portfolio. But mutual funds pool resources from many sources and invest in diversified portfolios so as to minimize risk and maximize return.

**Variety:** There are different strata’s of investors who wants to invest in varieties of schemes depending on their preference return and risk. For instance, there are growth schemes for investors who are willing to bear a greater risk, gilt schemes for investors who are risk-averse and retirement plans for those with an eye on the future.

**Liquidity:** In case of open-ended schemes, a majority of mutual funds provide investors easy entry and exit at prices related to the scheme’s net asset value (NAV). This ensures good liquidity positions for the investors in the mutual funds.

### 3.7.2 Weaknesses of the Industry

In March 2004, the share of individual investors was 33% of AUM, while corporates were 65%. Non-resident Indians (NRIs) were at 1% and FIIs at 0.5%. Though the shares changed dramatically by March 2006, with the individual investor taking 43%, corporates 51%, NRIs 5% and FIIs 1%, yet it the corporates which dominates. This proportion must change because corporate will take away profits frequently resulting in destruction in the compound growth of fund under management. In developed markets, mutual funds have proved to be the ideal vehicle for retail investors to take advantage of the excellent long-term growth of
Role of Mutual Funds

stock markets. In fact, in terms of assets under management, the mutual fund industry in the US has overtaken the banking industry. Another weakness of the mf industry in India is its distribution network is not very good. The Indian mutual funds industry has to further strengthen its distribution network so that a wider base can be tapped. This issue must be attended to promptly. Education of both investors and distributors is needed. Another important issue is concerned with the fixed rate of interest people have got used to. People have not been able to understand the risk-return trade-off fully. Further, investor expectations are very high. It must be understood that mutual funds cannot turn out magic - investors must harbour only reasonable expectations. The products offered by MF industry are not sufficient to cater to the entire life cycle of an investor. Mutual funds in developed countries like US offers diversified products ranging from purchase of car, house etc to admission in universities.

3.7.3 Opportunities of the Industry

In India only around 7 % of household holds mutual funds whereas in developed countries like US it is around 50% and in UK it is around 17%. Most of the people are not aware of mutual funds. The young people do not have interest in the MF industry and they rather show interest in the insurance policy. So, a huge untapped opportunity can be tapped if some sort of interest among young generation can be created for mutual funds. Interest that can be earned by putting money in bank fixed deposit is around 9% while the inflation rate is around 6 %. This simply implies a net earning of around 3 % only if money is
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invested in bank fixed deposit. Mutual funds in any way provide a better return than the fixed deposits. Further, the equity investor likes to have a higher return than a typically interest rate return. Though the interest rate scenario is better now, yet the investor can opt for the fixed maturity plan (FMP) of mutual funds instead of bank FDs. The mind set of the investors investing in capital market and bank FDs are certainly different. If an investor is looking for a capital safety, then he may prefer bank FDs. Instead of that, they may look for different capital protection schemes available with mutual funds. Another significant opportunity that MF industry provides to investors with lump sum is systematic transfer plan (STP). This method serves the need of those investors, who are scared of a volatile market. He can put his money in the liquid funds and rotates it for 15 or 20 days according to his comfort zone.

Today, the Indian economy is growing at a faster and the real estate sector is growing even faster. As a result, in our economy, more and more money is chasing a limited quantity of high-quality property. This makes real estate investment potentially one of the best investment opportunities available. But it is the high price and high transaction cost which causes difficulty for a small investor to take participation in this booming sector. Fortunately, a new investment product known as real estate mutual fund is being developed which will make it easier for the average investor to invest his or her hard-earned money in real estate. The entry of mutual fund is not only good news for investors in mutual funds but also for the real estate sector as more funds will be available. Another big opportunity for the mutual funds industry is the untapped rural India.
There is huge potential for the mobilization of funds by way of mutual fund investment in rural India. One thing is for sure that in future most of funds would be targeting the rural India as it is still untapped in a significant way. Mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, and thereby giving positive results. The consistency in the performance of mutual funds has been a major factor that has attracted many retail investors. The Indian mutual funds industry has been growing at a healthy pace of 16.68.

3.7.4 Threats for the industry

Indian mutual funds do not give much of a choice for investors in terms of products for investments and though the industry has come a long way over the years, there are no differentiating factors to separate these mutual funds. The main reason for not offering innovative products is that more risk would come along with innovative funds. Mutual funds must realize that there are some small saving schemes like NSC and PPF which are still offering high return than debt and income funds. Too much focus is being given to equity and any downswing in equity market would severely dent investor's confidence. Again, there is lack of investor education which results in risk-return mismatch for investors investing in mutual funds. The SWOT analysis of the mutual fund industry suggests that the prospects for the industry in future are very bright. Undoubtedly the start of the mutual funds industry in India was slow but steady. But what is heartening to note is that after such a slow start, the industry has picked up and is presently going through a phase which can be described as an interesting one. The last few
years have really been noteworthy for the industry. Today, mutual funds have become popular among the customers and have gained wide acceptability as a savings vehicle among the investors. The performance of many funds has been good, a strong distribution network has been established, products are in line with customer preference and requirements and the industry on the whole is on a growth path. A very important noteworthy thing is that the Indian mutual fund industry is likely to increase its present share of 6 per cent to the Gross Domestic Product (GDP) to 40 per cent in the next ten years on the condition that India’s growth rate consistently exceeds at the rate of 6 per cent per annum. Globally, mutual funds have become a very popular avenue of investment. As far as India is concerned, the mutual funds have attracted mass investors only with the advent of private players. Also, there has been a distinct shift in investor’s preference towards mutual funds investment. According to a study conducted by the Associated Chamber of Commerce and Industry of India (ASSOCHAM) and the Association of Mutual Fund Industry of India (AMFI), the size of the Indian mutual fund industry is estimated to go up to over Rs 1,65,000 crore by 2014.

3.8 MFs Industry in India: Attaining Maturity

Though Capital Market attracts people, yet there are several problems associated with it. While investing directly into capital market one has to be careful enough to judge the valuation of the stock and understand the complexities involved in the stock price fluctuations. So, a person with moderate knowledge of capital market generally prefers to invest in mutual funds. In recent times, mutual
funds industry in India is growing very fast and also undergoing tremendous changes. The prices of gold and real estate have reached sky high levels not only in India but also throughout the world. And both these traditional investment avenues have been extremely popular with Indian investors. Regulations have also favored these two classes of investments with the Securities and Exchange Board of India introducing norms for gold traded funds and the government relaxing norms for foreign direct investments in real estate ventures. This article attempts to discuss some of the important developments which have taken place during the recent past.

During last one decade or so, Indian financial market has matured tremendously. The main reason for this is the LPG process which started in 1991. The LPG process has brought a lot of changes in the various aspect of financial market. During last few recent years, saving of the country has been around 23% which is one of the highest in the world. Saving forms an important part of the economy of any country. As various options are available for this saving to be invested, money acts as a driver for the growth of a country. Indian financial scene provides ample opportunities for investment. If not the best, but mutual funds provide one of the better options for an ordinary investor to earn a reasonable rate of return. R.B.I also reduced the S.L.R and C.R.R to their minimal extent. As a result of this, the bank rate and market rate of interest drastically fell down. Though stock market is booming as never before, it is always subject to unknown fluctuation. All these factors, directly or indirectly, have led to the tremendous growth of Indian mutual fund industry. People willing
Role of Mutual Funds

to earn higher rate of return by taking minimal risks are finding Mutual Funds (MFs) as good avenues to invest their savings. Along with the significant growth of MF industry, there came lots of significant changes too. India’s mutual fund and stock market has witnessed phenomenal growth over the last few years. According to a study, mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, giving positive results. The consistency in the performance of mutual funds has been a major factor that has attracted many investors. 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. 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. Fund houses with the greatest brand equity are sure to capture the biggest spending investors. Mutual Fund industry today, with about 34 players and more than five hundred schemes, is one of the most preferred investment avenues in India. 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 ballooning, revealing the efficiency of growth in the mutual fund industry. The UTI Mutual Fund continues to maintain the top position by adding over Rs.3800 Crores in the month to take its total corpus to Rs.41622.51 Crores. The second slot once again captured by Prudential ICICI Mutual fund with Rs.35232.16 Crores of asset under management as on 30
November, 2006. With the growth in the securities markets and tax advantages granted for investment in mutual fund units, MF is sure to develop more and more in the near future and become one of the most sought after Investment Avenue. 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.

3.8.1 Analysis of Recent Changes

Mutual fund industry started in India in 1963-64 with the formation of U.T.I. With the passage of time, slowly but surely, private and foreign players started to enter into the industry and as a result of which the rules of the game started to change quickly. Till 1999, U.T.I had the monopoly in mutual fund industry and controlled around 80% of all mutual fund assets. But now, it holds only something around 12% of mutual fund assets. Most of the Indian mutual fund companies are having foreign tie-ups. These rapid changes can be mostly attributed to the Government deregulation. The most important year was 1992, when Securities and Exchange Board of India (SEBI) was set up. It provided regulatory framework under which mutual funds would function. Foreign participation in any sector would soon change the rule of the game. This is what has exactly happened with Indian Mutual funds industry. Global players are finding Indian mutual fund industry as a very potential sector. Their increased interest resulted in dramatic growth of the industry as they are coming with newer varieties and options to attract more and more investors. The foreign owned
AMCs are the ones which are now setting the pace for the industry. They are introducing new products, setting new standards of customer service, improving disclosure standards and experimenting with new types of distribution. The booming stock market is making investors more confident about the capital market and as a result, they are participating more in it. The mutual fund industry has made a concerted effort in the last year to try and introduce mutual fund products that would invest in commodities instead of equity or debt. The Securities and Exchange Board of India (Sebi) has taken several key steps to strengthen the Mutual Fund (MF) industry during 2005-06. As a very significant step, it has allowed MFs players to invest in foreign securities including American Depository Receipts (ADRs) and Global Depository Receipts (GDRs). In the finance bill 2006-07, the aggregate ceiling for the mutual fund industry to invest in ADRs and GDRs issued by Indian companies have been raised from US $1 billion to US $2 billion. This will enable Indian investors to invest in global equity markets with a wider choice of stocks to permit greater diversification and the convenience of dealing with an Indian mutual fund. The regulator has also introduced guidelines for the Gold Exchange Traded Funds (GETFs) and capital protection schemes. For GETF, the assets of the scheme have to be kept in the custody of a bank which is registered with Sebi. However, the scheme is subject to certain investment restrictions. The funds of any such scheme should be invested only in gold or gold-related instruments in accordance with the investment objective, except to the extent necessary to meet the liquidity requirements for honoring redemptions or repurchase of units as disclosed in the
Role of Mutual Funds

offer document. Since physical gold and other permitted instruments linked to gold are denominated in gold tonnage, it will be valued based on the market price of gold in the domestic market and will be marked to market on a daily basis. Securities and Exchange Board of India, vide its circular dated 14th August 2006 has amended the SEBI (Mutual Funds) Regulations to provide for the launch of capital protection oriented schemes. The term 'capital protection oriented scheme' means a mutual fund scheme which is designated as such and which protects the capital invested therein through suitable orientation of its portfolio structure. Capital guarantee means the capital sum invested by an investor is intact at the end of a specific time period. For example, if a person invests Rs 10,000 in a capital guaranteed scheme, then at the end of a certain time period, say five years, he will get back a sum of at least Rs 10,000. There can be a higher payout depending on the earnings of the scheme, but this will be additional earnings. So, an investor can be sure that he will not lose his capital. Hence, there is a guarantee of protection of capital, but no guarantee of return. Another significant development was in the area of ELSS (Earning Linked Saving Schemes). Experts were of the opinion that ELSS was the way ahead. The Government of India also gave heed to their prescription and has now said that investment up to Rs 1,00,000 in ELSS scheme will qualify for section 88 rebates. Investors need no longer be restricted by the fact that only up to Rs 10,000 will qualify for section 88 benefits. As results of this, there were several investments of 1, 00,000 in three recently launched ELSS schemes last year as against earlier where investors would stop at Rs 10,000 only. The three ELSS launched last year
mopped up Rs 886 crores in all. Another new trend noticed in the Mutual funds industry in India is the increasing interest of FII in various schemes of Mutual funds. Just as individual investors in India have started to accept MFs as viable saving options, MFs have started warming up to an unorthodox category of bulk investor, the foreign institutional investor. Several funds have announced discounted entry loads for FII. The FII find it convenient to step up exposure to companies where cumulative or individual FII holdings have hit the permitted ceiling. The main reason why FII are taking interest in MF is their need to take indirect exposure to stocks that have already reached the maximum permissible FII investment limit.

The concentration of Mutual funds was mostly on 'A' cities. But this trend is also changing slowly. They have started to realize that there is huge untapped potential in the semi-urban and rural market. The increase in the standard of living of middle class people resulted in the increase in the disposable income. This segment is now being targeted by more and more mutual funds companies. As a latest development in mutual funds industry, SEBI, the market regulator, has finally approved new guidelines for mutual funds and thereby allowing them to invest in real estate. It has also eased the existing norms for the registered local as well as the foreign venture capital investor Real Estate Mutual Funds (REMF) will invest directly or indirectly in real estate property and shall be governed by the provisions and guidelines under Sebi (mutual funds) regulations. This new category of mutual funds can purchase real estate as well as shares of real estate companies. Real estate development across the country has been
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estimated at US$15 billion and growing at the rate of 30 per cent every year. Till now, as the real estate investment needs huge money, it was beyond the capacity of retail investors. By opening up this sector to the mutual funds industry, retail investors have been given a unique opportunity to enter into the high profit making zone. Property prices in India are rising fast, and not just in the biggest cities. As the tech boom spreads across the country, as more Indians by virtue of growth of their income buy homes, and as the economy grows at faster than 8% a year, real estate is and will be attracting more investors, even many of them from abroad. India is said to be the most exciting real estate market in Asia. In another significant development recently, the RBI has allowed non-banking finance companies (NBFCs) and residuary non-banking companies (RNBCs) on a selective basis to market and distribute mutual fund products as agents of mutual funds. The NBFCs must have a minimum net-owned fund of Rs 100 crore and should have made a net profit as per its last two years audited balance sheet. In addition to this, their Non Performing Assets must be less than 3% and CRAR must be at least 10%. These developments will also be very helpful in promoting mutual funds industry in India.

E-commerce has lot to do with the growth of mutual fund industry in India. Many had questioned the success of E-commerce but it is one aspect of the technology which can not be ignored and would certainly change the way financial market function. Mutual funds have realized the potential of internet and are equipping themselves to perform better. These changes have facilitated easy access, lower intermediation cost and better services for all. There has been
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A substantial amount of reduction in the cost associated with the mutual funds because of growth of information technology. Mutual funds could now bring down their administration costs to 0.75% if trading could be done on line. As per SEBI regulation, bond funds can charge a maximum of 2.2% and equity fund can charge 2.5% as administration fees. This lower administration cost can be applied to attract more investors. The growth in information technology has made the availability of information easy to various investors and even the investors can get advice of expert on internet. This is another changing dimension in the mutual fund industry. Now-a-days, the focus of the mutual funds is on corporate governance as against their earlier traditional approach.

3.8.2 Future Scenario

During last few years, India’s position as a market with potential for long-term growth has really been noteworthy as the Indian economy is being ranked among the top 10 globally (in terms of GDP), and as the fourth-largest in terms of purchasing power parity (PPP). Another good thing to note about Indian mutual funds industry is that is has grown at a rapid pace of 16.4% during last 8 years as compared to global growth rate of 13% during the same period. However, when it comes to assets under management (AUM) of the global mutual fund (MF) industry, India’s ranks is 25th which is not very satisfactory, rather dismissal. With assets of around $76.5 billion (Rs 3.41 lakh crore) as per AMFI figures at the end of November '06, India forms just 0.4% of the world’s global MF AUMs. MF assets worldwide stood at $19.41 trillion at the end of the second quarter of
2006. US with $12.4 trillion of MF assets is the topper, followed by Luxembourg ($1.9 trillion), France ($1.6 trillion) and Australia ($723 billion). Another important criterion which is used by the analysts as parameter to judge the majority of a country’s mutual fund industry is MF assets to GDP (PPP basis) ratio. According to available date, the ratio was 75.2% for US and 34.9% for U.K. Even in the emerging economies’ list, India’s numbers were far from encouraging. The figure was 23.1% for Brazil, 26% for Russia, as compared to 1.3% for India. There are few other threats which Indian mutual fund is currently facing. Mutual funds must realize that there are some small saving schemes like NSC and PPF which are still offering high return than debt and income funds. Too much focus is being given to equity and any downswing in equity market would severely dent investor’s confidence. Again, there is lack of investor education which results in risk-return mismatch for investors investing in mutual funds. However, it can be said, in coming years, mutual fund industry is going to take off to newer heights. The Indian equity market has seen unbelievable rise in the last couple of years. From an index level of 5,590 as at March 31, 2004 to 14,000 during December, 2006, the markets have moved in top gear, at breathtaking speed, tumbling records after records in this unrelenting journey. The prices of gold and real estate have reached to sky high levels not only in India but also throughout the world. And both these traditional investment avenues have been extremely popular with Indian investors. Regulations have also favored these two classes of investments with the Securities and Exchange Board of India introducing norms for gold traded funds and the government relaxing
norms for foreign direct investments in real estate ventures. Retail investors have largely participated through mutual funds and this is clearly evident from the number of equity funds that have been launched in the last couple of years and the record collections they have witnessed. The Reserve Bank of India has relaxed norms for overseas investments thereby opening up more investment avenues. In recent years, SEBI has taken several steps to consolidate the Indian MF industry. There are some changes in guidelines that include standardization of the Funds Portfolios and disclosure of the balance sheet of the fund. Among other changes that are scheduled is reduction in the time taken by AMCs to complete formalities from 90 to 42 days. Also proposed is the use of unclaimed money for investor education. The present structure of funds is likely to change from the three-tier framework. This is expected to streamline the operations of the funds and will give them more flexibility. Finally, though mutual funds are primarily composed of stocks, there is a slight difference between these two which makes mutual funds more advantageous to the common investors. Diversification is the biggest advantage associated with mutual funds. Diversification is the idea of investing money across many different types of investment avenues. When one investment is not doing well other might be yielding good profit. Diversification reduces risk significantly. In addition to this, by purchasing mutual funds, one is actually hiring a professional manager at an especially inexpensive price. Now-a-days, a higher portion of investors' savings is now invested in market-linked avenues like mutual funds as compared to earlier times. However, if we compare proportion of people investing in mutual funds in India with that in U.S, then we find that in
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U.S more than 50 % people invest in mutual funds whereas in India the proportion is less than 10%. This gives the indication that there is much more untapped potential for growth in this industry in India which must be explored in the coming time. In conclusion, it can be said that despite few problems, the recent changes in the mutual funds industry in India has really favored its amazing growth and same is expected to continue in future too.

Today, India's financial system is considered to be sound and stable as compared to many other asian countries where the financial market is facing many crises. During last one decade or so, role of Indian mutual funds industry as a significant financial service in financial market has really been noteworthy. In fact, Mutual funds have emerged as an important segment of financial market of India, especially as a result of the initiatives taken by the Govt. Of India for resolving problems relating to UTI's US-64 and to liberalize tax liabilities on the incomes earned by the mutual funds. In recent times, mutual funds industry in India is growing very fast and also undergoing tremendous changes. Many claim that MFs industry in India is on the verge of attaining maturity. They now play a very significant role in channelizing the saving of millions of individual into the investment in equity and debt instruments. But at the same time a concern is being raised that there are not sufficient varieties of mutual funds products to attract more and more urban and semi-urban investor.

The economic and financial scenario of India prior to 1991 was not very optimistic. Indian economy at that time was suffering from low savings, low
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GDP, high inflation, high unemployment, high rates of interest, low forex reserve etc. When India approached IMF for financial assistance in 1991, we were imposed certain condition on which the financial assistance was sanctioned to India. These restrictions which we accepted under the pressure from IMF were actually the starting point of economic reforms popularly known as LPG process. The result of the LPG process of 1991 is more clearly visible now. India is now being ranked as one of the fastest growing economy of the world. As already 11th planning period has started, Indian economy is in a much stronger position. The saving of the country is now around 29%. Foreign investors are finding Indian market with high potential. India’s forex reserve is now $220 billion plus. Inflation is also at 5% which is considered good for developing economies. So it is the Vigorous growth with strong macroeconomic fundamentals has characterized development in the Indian economy in 2006-07 so far. However, there are some genuine concerns on the inflation front. But it is not a very big matter of worry. Growth of 9.0 per cent and 9.2 per cent in 2005-06 and 2006-07, respectively, by most accounts, has surpassed expectations. Some experts have opined that, the share of the US in world GDP is expected to fall (from 21 per cent to 18 per cent) and that of India to rise (from 6 per cent to 11 per cent in 2025), and hence India will emerge as the third pole in the global economy after the US and China. All these favorable things could have not been possible without the sound financial market. It is the financial market which finances economic development. It is the financial market which channelizes the saving of the people into the investment. Indian financial markets are getting more and
more institutionalized. Foreign investors, local institutions and mutual funds are now playing a bigger role. This is the case in developed markets. Mutual Fund is an instrument of investing money. Nowadays, bank rates have fallen down below the inflation rate. Therefore, keeping large amounts of money in bank is not a wise option, as in real terms the value of money decreases over a period of time. One of the options available is to invest the money in stock market. But a common investor is not well informed and competent enough to understand the complexities involved in the price movement of shares in the stock market. This is where mutual funds come to rescue them. The role of mutual funds will increase in the Indian markets also. This means that retail investors will opt for mutual funds. In the US, 35 to 40 per cent of the investments currently come through mutual funds while in India it is very negligible. With the stock markets reaching to newer heights in 2006, mutual funds could not be far behind. Total assets under management of 30 funds rose by Rs 125,296 crore, or 63 per cent, to Rs 323,601 crore during the calendar year 2006, according to the data published by the Association of Mutual Funds of India (AMFI). Mutual funds saw record resource mobilization as investors lined up to take advantage of the stock market boom. In the first six months of the years 2007 the Indian mutual fund industry has grown 25 per cent, accumulating assets worth over Rs 4 trillion as a result of the bullish sentiments in the stock market and robust economic growth in the country. The assets under management of all the 32 mutual funds in the country increased by 24.6 per cent to Rs 4,00,842.12 crore in June as against Rs 3,21,488.47 crore in December last year. It is the Reliance MF which is the
ICICI Prudential is standing at the second place with AUM of Rs 43,613.75 crore, a growth of over 30 per cent in just six months. However, the public sector UTI MF, which was at the top in terms of AUM last year, has dropped to third place with AUM of Rs 39,031.87 crore in June. UTI MF has witnessed just 2.4 per cent growth in its assets over the six months.

3.8.3 Existing Products Range in the MFs Industry

Mutual fund industry started in India in 1963-64 with the formation of U.T.I. With the passage of time, slowly but surely, private and foreign players started to enter into the industry and as a result of which the rules of the game started to change quickly. Till 1999, U.T.I had the monopoly in mutual fund industry and controlled around 80% of all mutual fund assets. But now, it holds only something around 12% of mutual fund assets. Most of the Indian mutual fund companies are having foreign tie-ups. These rapid changes can be mostly attributed to the Government deregulation. The most important year was 1992, when Securities and Exchange Board of India (SEBI) was set up. It provided regulatory framework under which mutual funds would function. Foreign participation in any sector would soon change the rule of the game. This is what has exactly happened with Indian Mutual funds industry. Global players are finding Indian mutual fund industry as a very potential sector. Their increased interest resulted in dramatic growth of the industry as they are coming with newer varieties and options to attract more and more investors. The foreign owned
AMCs are the ones which are now setting the pace for the industry. They are introducing new products, setting new standards of customer service, improving disclosure standards and experimenting with new types of distribution. The booming stock market is making investors more confident about the capital market and as a result, they are participating more in it. The mutual fund industry has made a concerted effort in the last year to try and introduce mutual fund products that would invest in commodities instead of equity or debt. The asset under management in the mutual fund industry has risen to a level of Rs.4.14 trillion as on May 31st 2007, recording a growth rate of nearly 50 percent as compared to the same month during year 2006. However, one cannot deny the fact that in India we have limited mutual funds products as compared to developed countries like US and UK. If we consider the various products of the top most mutual funds company across both public and private sector i.e. of UTI Mutual funds, then we get the following varieties of products available:

1. Equity Funds: This includes various schemes like UTI Tax saving Plan, UTI MEPUS, UTI – Mastreshare Unit Scheme, UTI Opportunity Fund, UTI Service Sector Fund, UTI Master Growth, UTI MNC Fund etc.

2. Balanced Funds: This includes various schemes like UTI – US 2002, UTI – Mahila Unit Scheme, UTI - Retirement Benefit Pension Fund, UTI – CRTS, UTI – ULIP etc.

3. Index Funds – This includes various schemes like UTI - Master Index Fund, UTI - Index Select Fund, UTI - Nifty Index Fund, UTI – Sunder etc.
4. Liquid Funds: This includes various schemes like UTI - Money Market Fund, UTI - Floating Rate Fund, UTI - Liquid Fund - Cash Plan etc.

5. Income Funds: This includes various schemes like UTI - G-Sec Fund - Investment Plan, UTI - GILT Advantage Fund - LTP, UTI - Variable Investment Scheme etc.

6. Assets Allocation Funds: This includes schemes like UTI - Variable Investment Scheme.

The Securities and Exchange Board of India (Sebi) has taken several key steps to strengthen the Mutual Fund (MF) industry during 2005-06. As a very significant step, it has allowed MFs players to invest in foreign securities including American Depository Receipts (ADRs) and Global Depository Receipts (GDRs). In the finance bill 2006-07, the aggregate ceiling for the mutual fund industry to invest in ADRs and GDRs issued by Indian companies have been raised from US $1 billion to US $2 billion. This will enable Indian investors to invest in global equity markets with a wider choice of stocks to permit greater diversification and the convenience of dealing with an Indian mutual fund. The regulator has also introduced guidelines for the Gold Exchange Traded Funds (GETFs) and capital protection schemes. For GETF, the assets of the scheme have to be kept in the custody of a bank which is registered with Sebi. However, the scheme is subject to certain investment restrictions. The funds of any such scheme should be invested only in gold or gold-related instruments in accordance with the investment objective, except to the extent necessary to meet the liquidity requirements for honoring redemptions or repurchase of units as disclosed in the
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offer document. Since physical gold and other permitted instruments linked to gold are denominated in gold tonnage, it will be valued based on the market price of gold in the domestic market and will be marked to market on a daily basis. Securities and Exchange Board of India, vide its circular dated 14th August 2006 has amended the SEBI (Mutual Funds) Regulations to provide for the launch of capital protection oriented schemes. The term ‘capital protection oriented scheme’ means a mutual fund scheme which is designated as such and which protects the capital invested therein through suitable orientation of its portfolio structure. Capital guarantee means the capital sum invested by an investor is intact at the end of a specific time period. For example, if a person invests Rs 10,000 in a capital guaranteed scheme, then at the end of a certain time period, say five years, he will get back a sum of at least Rs 10,000. There can be a higher payout depending on the earnings of the scheme, but this will be additional earnings. So, an investor can be sure that he will not lose his capital. Hence, there is a guarantee of protection of capital, but no guarantee of return.

Net mobilization of resources by mutual funds increased by more than four-fold to Rs. 104,950 crore in 2006 from Rs. 25,454 crore in 2005. The sharp rise in mobilisation by Mutual funds were due to buoyant inflows under both income/debt oriented schemes and growth/equity oriented schemes. After suffering negative inflows in 2003 and 2004, inflows turned positive for public sector mutual funds in 2005 and accelerated in 2006. The share of UTI and other public sector mutual funds in the total amount mobilized was around 22.5 per cent.
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in 2005 and 17.8 per cent in 2006. A idea on sector-wise resource mobilization by MF industry in India can be presented in the form of the following table:

<table>
<thead>
<tr>
<th>Particular</th>
<th>Private Sector MFs</th>
<th>Public Sector MFS</th>
<th>UTI MF</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Open-ended</td>
<td>Close-ended</td>
<td>Total</td>
<td>Open-ended</td>
</tr>
<tr>
<td>Mobilization of Funds</td>
<td>875917 (720603)</td>
<td>38786 (15860)</td>
<td>914703 (736463)</td>
<td>110142 (55771)</td>
</tr>
<tr>
<td>Repurchase/Redemption Amount</td>
<td>859367 (718440)</td>
<td>12360 (10423)</td>
<td>871727 (728864)</td>
<td>103580 (58976)</td>
</tr>
<tr>
<td>Net Inflow/Outflow of funds</td>
<td>16550 (2163)</td>
<td>26426 (5437)</td>
<td>42977 (7600)</td>
<td>5662 (-3205)</td>
</tr>
</tbody>
</table>

Source: Annual Report of RBI 2005-06

Though India have recently entered into the elite club of trillion dollar economies, and Indian companies here are playing a major role in the international business arena, but at $88-billion worth of assets under management, India's mutual fund industry ranks a lowly 24th in the world. And despite the rapid growth in assets, fuelled by a booming economy and stock market, India has managed to improve its ranking by only a notch in 2006. According to Investment Company Institute (ICI), a world MF tracker, total assets under management worldwide was $21.8 trillion at the end of 2006. The mutual fund industry in US tops that list with assets worth $10 trillion under its belt.
Luxembourg is placed at a distant second with $2.2 trillion of mutual fund assets, while France is third on the list at $1.8 trillion. The world MF assets grew by a record 22.5% in 2006 to $21.8 trillion. The growth rate in 2006 was higher compared with 9.9% growth rate levels seen in 2005. Equity markets across the world have been registered new heights of growth and as result bringing huge inflows into mutual funds.

The MF sector has 30 active players and they have mopped up nearly $8 billion through equity mutual fund schemes. It is expected that this will further grow to $10-12 billion. Thirty-eight new equity schemes were launched in 2006 and mopped around $6.3 billion. New categories of funds, like capital protection-oriented funds and equity derivative funds were launched. Pure equity new fund offerings (NFOs) raked in a whopping Rs 32,309 crore in 2006, almost 33% more than the money raised by Indian corporates through initial and follow-on issues. This is a clear indication that retail investors are increasingly tapping the stock market through the mutual fund route. The mutual fund (MF), as a capital market intermediary, has emerged as new avenue for capital resources. It bridges the gap between retail investors and capital markets. According to Value Research data, the top five equity NFOs were Reliance Equity (Rs 5,790 crore), SBI Bluechip (Rs 2,850 crore), Reliance Long Term Equity (Rs 2,100 crore), UTI Leadership Equity (Rs 2,080 crore) and Templeton India Equity Income (Rs 2,030 crore). Close to 40 NFOs were made in 2006 with average collections of Rs 950 crore. The top five IPOs of 2006 were made by the following companies — Cairn India
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(Rs 5,260 crore), Reliance Petroleum (Rs 2,700 crore), Bank of Baroda (Rs 1,633 crore), Parsvnath Developers (Rs 1,089 crore) and Lanco Infratech (Rs 1,067 crore). So, it is clearly evident that MF is providing more opportunities for the corporates to raise more funds. It is offering several options in structured forms. The industry is going to a major role model in the capital markets. According to a study conducted by the Associated Chambers of Commerce and Industry of India, the size of the mutual funds industry is expected to be worth Rs. 4 lakh crores by 2010. Mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, giving positive results. The following table given an idea about money rose by mutual funds industry in India under different schemes:-

TABLE: 5

<table>
<thead>
<tr>
<th>Assets under management of mutual funds (Rs. Crore)</th>
<th>Calendar year (Year end)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Schemes</strong></td>
<td><strong>2003</strong></td>
</tr>
<tr>
<td>Money Market</td>
<td>32,424</td>
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<tr>
<td>Gilt</td>
<td>6,917</td>
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<tr>
<td>Income</td>
<td>71,258</td>
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<tr>
<td>Growth</td>
<td>22,938</td>
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<tr>
<td>Balanced</td>
<td>4,663</td>
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<tr>
<td>ELSS</td>
<td>1,893</td>
</tr>
<tr>
<td>Total</td>
<td>140,093</td>
</tr>
</tbody>
</table>

Source: NSE
The consistency in the performance of mutual funds has been a major factor that has attracted many retail investors. 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. According a study, it has been found out that almost 54% of people invest for security and certainty while 38% of the people invest for current spending. Some 53% of the people prefer long term investment whereas 23% people each prefer medium term and small term investment. All these studies relate to retail investors. Actually, it is the consistence performance of mutual funds which is attracting retail investors towards it. Today, MF equity portfolio is worth around $32 billion, while individual investors own $88 billion. It is the Retail investors who have been heavily investing in equities through MFs over the past couple of years. This observation can be made from the fact that close to $17 billion of NFO collections made in the last four years from equity funds. Eventually, money collected on these have made their way to equity market. On an average, MF net investments into equity markets remained around 50% of that by FIIs in the past three to four years. As Retail investor’s investments are typically long-term oriented, they are therefore important for maintaining stability in any equity market. Another very significant development for retail investors in the field of mutual funds is the entry of mutual funds in real estates. For the last three years the real estate sector has been growing at a fast pace of 30-40%, especially in the metros. But for retail investors, participating in this growth was not easy. By opening the real estates investment for mutual funds, retail investors, who cannot invest directly in real estates which needs huge
Role of Mutual Funds

investments to start with, are actually allowed to investment in real estates through mutual funds. Retail investors are expected to account for 60% of the industry’s AUM. But this can be possible only if mutual funds in the country manage to enter into non-urban cities. This becomes more important because this is where saving deposits account for 49% of the total assets. These small towns account for only 30% of their holdings in mutual funds. So, one thing can be said for sure that retail investors are going to participate more and more in mutual funds in the times to come and thereby a lot of financial resources are going to be mobilized to financial market of India.

3.8.4 Needs for New products

There is a need for Indian mutual fund industry to look at other options to grow rather than simply rely on fund inflows from corporate. As Indian mutual fund industry is on the verge of attaining maturity, it the best time that it widens its range of products with affordable and competitive schemes which would cater to the needs of semi-urban and rural population in order to attract more investments from them. The industry has still not been able to tap the retail investors to the achievable extent and we must adopt some of the policies from developed markets like US and UK where mutual funds are the most preferred form of investment. Mutual fund companies need to introduce products for the semi-urban and rural markets that are affordable and yet competitive against low-risk assured returns of government sponsored saving schemes such as post office saving deposits. Since, there are some technological infrastructures scarce which need serious attention. Further, some sort of collaboration with other sector like
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banking, insurance and telecommunication would have favorable result. Since there are growing opportunities in the commodity market, it must be tapped by the Mutual fund companies. Further, the mutual funds could also enable the small investors to participate in the real estate boom through real estate mutual funds. The mutual fund industry also faces some major challenges in terms of manpower crunch, diminishing talent pool of fund managers, pressure of consolidation, innovation and product differentiation as increasing responsibility is being placed on the trustees to ensure that the funds are managed to the full benefit of the unit holders.

Undoubtedly, Indian mutual funds industry has registered significant growth not only in terms of assets under management but also in terms of the number of various products that have been launched by various mutual funds companies. But when we compare our mutual funds industry with that of developed countries, we even do not come in the top 20 countries in terms of assets under mutual funds industry. When it comes to assets under management (AUM) of the global mutual fund (MF) industry, India’s ranks is 25th which is not very satisfactory, rather dismissal. With assets of around $76.5 billion (Rs 3.41 lakh crore) as per AMFI figures at the end of November '06, India forms just 0.4% of the world’s global MF AUMs. MF assets worldwide stood at $19.41 trillion at the end of the second quarter of 2006. US with $12.4 trillion of MF assets is the topper, followed by Luxembourg ($1.9 trillion), France ($1.6 trillion) and Australia ($723 billion). Another important criterion which is used by the analysts as parameter to judge the majority of a country’s mutual fund industry is
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MF assets to GDP (PPP basis) ratio. According to available data, the ratio was 75.2% for US and 34.9% for UK. Even in the emerging economies' list, India's numbers were far from encouraging. The figure was 23.1% for Brazil, 26% for Russia, as compared to 1.3% for India. So, the clear indication is that there is a need to expand which can be done by tapping the untapped semi-urban and rural population of India by offering various new products which are mostly designed to satisfy their needs. No doubt, tapping rural India will be a big challenge for mutual fund companies. The fund houses should offer products, which are not only affordable but also competitive against low-risk and assured returns of government sponsored saving schemes. It has been suggested the fund houses should tap on savings of retail investors by meeting basic requirements such as retirement planning, child education, taking a cue from mature markets like those of the US and the UK.

3.9 Indian MF Industry: Money Raining

Today our economy is in a much stronger position than even before. The success story of any economy can only be scripted on the basis of sound financial system of the country. Economic reform process of 1991 had a great impact on the financial system of the country leading to the overall development of the Indian economy. Today, India's financial system is considered to be sound and stable as compared to many other Asian countries where the financial market is facing many crises. During last one decade or so, role of Indian mutual funds industry as a significant financial service in financial market has really been noteworthy. In fact, Mutual funds have emerged as an important segment of
financial market of India, especially as a result of the initiatives taken by the Govt. Of India for resolving problems relating to UTI's US-64 and to liberalize tax liabilities on the incomes earned by the mutual funds. They now play a very significant role in channelizing the saving of millions of individual into the investment in equity and debt instruments. One thing is for sure that lot of money is raining in Indian MF industry. This paper aims at making a critical study of the role performed by mutual funds as mobilizer of huge money in Indian financial market.

The result of the LPG process of 1991 is more clearly visible now. India is now being ranked as one of the fastest growing economy of the world. On the beginning of 11th Planning period, we are already targeting a GDP growth of over 9%. As per the economy survey 2006-07, the saving rate of the country is 32.4 per cent and investment rate is 33.8 per cent. These rates are expected to continue in the year 2007-08 also. Foreign investors are finding Indian market with high potential. Forex reserve has also touched the $200-billion in April, 2007. This is a very good show considering that we had negligible forex reserve in 1991. Inflation is slightly above 5% which is considered good for developing economies. So, Indian economy is really booming today. If India can manage a growth rate of over 8% in next one decade, it would imply that our per capita income would double with multiple favorable effects on India's export and market share. All these favorable things could have not been possible without the sound financial market. It is the financial market which finances economic development. It is the financial market which channelizes the saving of the
people into the investment. Indian financial markets are getting more and more institutionalized. Foreign investors, local institutions and mutual funds are now playing a bigger role. This is the case in developed markets. Mutual Fund is an instrument of investing money. Nowadays, bank rates have fallen down below the inflation rate. Therefore, keeping large amounts of money in bank is not a wise option, as in real terms the value of money decreases over a period of time. One of the options available is to invest the money in stock market. But a common investor is not well informed and competent enough to understand the complexities involved in the price movement of shares in the stock market. This is where mutual funds come to rescue them. The role of mutual funds will increase in the Indian markets also. This means that retail investors will opt for mutual funds. In the US, 35 to 40 per cent of the investments currently come through mutual funds while in India it is very negligible. With the stock markets reaching to newer heights in 2006, mutual funds could not be far behind. Total assets under management of 30 funds rose by Rs 125,296 crore, or 63 per cent, to Rs 323,601 crore during the calendar year 2006, according to the data published by the Association of Mutual Funds of India (AMFI). GDP growth is inching towards double digits, industry and manufacturing sectors are showing good results, service sector is also booming, employment and consumption is increasing. Investments in mutual funds as a percentage of disposable income have increased from 1 per cent in 2005 to 3.9 per cent in 2006. As a result,
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Mutual funds saw record resource mobilization as investors lined up to take advantage of the stock market boom.

In order to critically examine the role of mutual funds in Indian financial market, we should first of all have a good idea about the Indian financial system. The financial system in India comprises of financial institutions, financial markets, financial instruments and services. Financial market refers to those places where financial assets are created and traded. Financial assets represent a claim for the payment of principal amount some times in future date and for periodic payment of money in the form of interest or dividends. The Reserve Bank of India (RBI) as the main regulator of credit is the apex institution in the financial system. Other important financial institutions are the commercial banks (in the public and private sector), cooperative banks, regional rural banks and development banks. Non-bank financial institutions include finance and leasing companies and other institutions like LIC, GIC, UTI, Mutual funds, Provident Funds, Post Office Banks etc. The banking system is, by far, the most dominant segment of the financial sector accounting for over 80 per cent of the funds flowing through the financial sector. The Indian financial sector reforms aim at improving the productivity and efficiency of the economy. It remained stable, even when other markets in the Asian region were facing a crisis. The opening of the Indian financial market to foreign and private Indian players has resulted in increased competition and better product offerings to consumers. The main function of all these financial institution is financial intermediation i.e. facilitating the flow of saving from common man to industrial houses. In the initial stages,
the role of the intermediary was mostly related to ensure transfer of funds from
the lender to the borrower. This service was offered by banks, FIs, brokers, and
dealers. However, as the financial system widened along with the developments
taking place in the financial markets, the scope of its operations also widened.
Some of the important intermediaries operating in the financial markets include;
investment bankers, underwriters, stock exchanges, registrars, depositaries,
custodians, portfolio managers, mutual funds, financial advertisers, financial
consultants, primary dealers, satellite dealers, self-regulatory organizations, etc.

Financial Markets are mainly classified as Money Market and Capital
Market. The term money market is used to denote the financial institutions which
deal with the short-term borrowing and lending of money. The term capital
market is used to mean the institutes which deal with the lending and borrowing
of long-term money. Resource mobilization by mutual funds is an important
activity in the capital markets. India's mutual fund and stock market has
witnessed phenomenal growth over the last few years. According to a study,
mutual funds would be one of the major instruments of wealth creation and
wealth saving in the years to come, giving positive results. As India is targeting a
GDP growth rate of 9% in the 11th Plan Period, the role of the financial sector as
well the role of mutual funds industry in India as an important segment of
financial market for resource mobilization in capital market is going to be very
significant. The consistency in the performance of mutual funds has been a major
factor that has attracted many investors. The mutual fund industry growth is
Role of Mutual Funds

estimated at about 50 per cent, far higher than that of bank fixed deposits which are growing at about 20 per cent.

Pure equity new fund offerings (NFOs) raked in a whopping Rs 32,309 crore in 2006, almost 33% more than the money raised by Indian corporates through initial and follow-on issues. This is a clear indication that retail investors are increasingly tapping the stock market through the mutual fund route. The mutual fund (MF), as a capital market intermediary, has emerged as new avenue for capital resources. It bridges the gap between retail investors and capital markets. According to Value Research data, the top five equity NFOs were Reliance Equity (Rs 5,790 crore), SBI Bluechip (Rs 2,850 crore), Reliance Long Term Equity (Rs 2,100 crore), UTI Leadership Equity (Rs 2,080 crore) and Templeton India Equity Income (Rs 2,030 crore). Close to 40 NFOs were made in 2006 with average collections of Rs 950 crore. The top five IPOs of 2006 were made by the following companies — Cairn India (Rs 5,260 crore), Reliance Petroleum (Rs 2,700 crore), Bank of Baroda (Rs 1,633 crore), Parsvnath Developers (Rs 1,089 crore) and Lanco Infratech (Rs 1,067 crore). So, it is clearly evident that MF is providing more opportunities for the corporates to raise more funds. It is offering several options in structured forms. The industry is going to a major role model in the capital markets. According to a study conducted by the Associated Chambers of Commerce and Industry of India, the size of the mutual funds industry is expected to be worth Rs. 4 lakh crores by 2010. Mutual funds would be one of the major instruments of wealth creation and wealth saving in the years to come, giving positive results. The consistency in the
Role of Mutual Funds

The performance of mutual funds has been a major factor that has attracted many retail investors. 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. According to a study, it has been found out that almost 54% of people invest for security and certainty while 38% of the people invest for current spending. Some 53% of the people prefer long-term investment whereas 23% people each prefer medium term and small term investment. All these studies relate to retail investors. Actually, it is the consistent performance of mutual funds which is attracting retail investors towards it. Today, MF equity portfolio is worth around $32 billion, while individual investors own $88 billion. It is the Retail investors who have been heavily investing in equities through MFs over the past couple of years. This observation can be made from the fact that close to $17 billion of NFO collections made in the last four years from equity funds. Eventually, money collected on these have made their way to equity market. On an average, MF net investments into equity markets remained around 50% of that by FIIs in the past three to four years. As Retail investor’s investments are typically long-term oriented, they are therefore important for maintaining stability in any equity market. Another very significant development for retail investors in the field of mutual funds is the entry of mutual funds in real estates. For the last three years the real estate sector has been growing at a fast pace of 30-40%, especially in the metros. But for retail investors, participating in this growth was not easy. By opening the real estates investment for mutual funds, retail investors, who cannot invest directly in real estates which needs huge investments to start with, are
actually allowed to investment in real estates through mutual funds. Retail investors are expected to account for 60% of the industry's AUM. But this can be possible only if mutual funds in the country manage to enter into non-urban cities. This becomes more important because this is where saving deposits account for 49% of the total assets. These small towns account for only 30% of their holdings in mutual funds. So, one thing can be said for sure that retail investors are going to participate more and more in mutual funds in the times to come and thereby a lot of financial resources are going to be mobilized to financial market of India.

The funds industry was never better than today: Assets under management is on the rise, the number of players looks set to jump, products are being rolled out by the dozen. Total asset size of the Mutual Funds (MF) industry grew four times to US$ 65 billion since 1993. Its contribution to the country's gross domestic product rose to almost 10 per cent in the last decade, as per Deutsche Bank Research (DBR). Equity asset under managements (AUMs) of fund houses are going stronger, with sturdy capital market growth. AUMs of the 30 fund houses increased 2.2 per cent (monthly basis) to US$ 259.6 billion in January 2007 from US$ 32.2 billion in December 2006. As the Indian MF industry is witnessing sustained high growth, the foreign players are also eyeing to take advantage of the huge opportunity that Indian economy is providing. It is expected that Indian stock market witness the entry of more global mutual funds in 2007. As many as five leading global asset management companies are having plans to enter into India's mutual fund industry which has already recorded a spectacular 65 per cent growth in 2006. American International Group (AIG). JP
Morgan, AXA Investment, Korean financial services major Mirae Asset Group and a Japanese company are planning to enter into the MF business in India in 2007. Yet, a point of concern for the industry today is that its total size is still a mere fraction of the nation's GDP. The mutual fund industry received 90 lakh fresh investment orders from December '05 to December '06, which has raised up the total investment folios to 2.57 crore. One of the important issues with our MF industry was that the penetration of mutual funds is still not widespread and millions of households needed to be tapped. Keeping this in view, Unit Trust has already started some schemes in rural areas and others would follow. In the annual policy statement for the year 2007-08, RBI has enhanced Aggregate ceiling on overseas investment by mutual funds to US $ 4 billion. While most of the Mutual fund managers have welcomed the RBI's decision, some of them are of the opinion that the central bank should raise the individual limit of $150 million per fund house. They are afraid that the limit prevents the asset management companies from achieving a scale of economy. According to them, such investment in overseas securities provides a valuable opportunity to investors to diversify their risk. If money could be invested across multitude of markets say in Latin America, South East Asia, Central Europe and Eastern Europe, an investor would have the benefit of diversification, which would cushion the risks arising from having a concentrated portfolio. In the financial year 2007, Assets under management in the mutual fund continued to grow at a very faster rate. Despite, most of the funds manager are not very happy. That is
because the growth has been driven by a surge in debt assets rather than the
lucrative equity assets.

The MF industry never had it better. For the time ever, entry-level
individual investors will account for half the assets under management (AUM).
Retail investor share is expected to reach 50 per cent—or more—in view of last
year's figures and the folio trends, as per the Association of Mutual Funds in India
(AMFI). With new, innovative products—woven around commodities, even real
estate—as many as 54,000 distributors (including 80 banks), and retail investors
will flood investments in MFs. Capital inflows into India remained strong in last
few years. The composition of flows, however, has witnessed fluctuation from
year to year. In the three-year period, 2002-05, there were large 'other flows'
delayed export receipts and others accounting for a sizable proportion of net
capital flows. After being outflows in the previous two years, external assistance
and external commercial borrowing (ECBs) — two major debt-creating flows —
picked up in 2004-05. These debt flows, as a proportion of total capital flows,
were 25% in 2004-05 and 18% in 2005-06. Foreign investment, as a proportion
of capital flows, has remained in the range of 39.1% to 79.3% in the last four
years ending in 2005-06. There was strong growth in foreign direct investment
(FDI) flows (net), with three-quarters of such flows in the form of equity. The
growth rate was 27.4% in 2005-06 followed by 98.4% in April-September 2006.
This was even after gross outflows under FDI with domestic corporate entities
seeking a global presence to harness scale, technology and market access
advantages through acquisitions overseas. The Indian government is expecting to
see foreign direct investment (FDI) inflows reach $26 billion in the fiscal year ending in March 2008. FII flows, after remaining buoyant until 2005-06, turned into net outflows in the first half of 2006-07. FII flows are reported to have turned positive again in the second half of the current year. Resource mobilized through the primary market indicated a very favorable position. Aggregate mobilization, especially through private placements and initial public offerings (IPOs), grew by 30.5% to Rs 161,769 crore in calendar year 2006, with about six IPOs every month, on average. Net mobilization of resources by mutual funds increased by more than four fold from Rs 25,454 crore in 2005 to Rs 1,04,950 crore in 2006.

Household savings play an important role in domestic capital formation of any economy. But unfortunately, only a small part of the household savings in India is being channelised to the capital market. So, there is a need to channelize this saving to the corporate investment. But, attracting more households savings to the capital market requires efficient intermediation. The mutual funds have emerged as one of the important class of financial intermediaries which cater to the needs of retail investors. As a traditional investment vehicle, the mutual funds pool resources from the households and allocate them to various investment opportunities. The gross mobilization of resources by all mutual funds during 2005-06 stood at Rs.10,98,149 crore compared to Rs.8,39,708 crore during the previous year – an increase of 30.8 per cent over the year. The following table gives an idea about the resource mobilization by mutual funds from 1999-00 to 2005-06:-
**Table: 6**

Mobilization of Resources by Mutual Funds

<table>
<thead>
<tr>
<th>Period</th>
<th>Gross Mobilization</th>
<th>Redemption</th>
<th>Net Inflow</th>
<th>Assets at the end of the period</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999-00</td>
<td>61241</td>
<td>42271</td>
<td>18970</td>
<td>107946</td>
</tr>
<tr>
<td>2000-01</td>
<td>92957</td>
<td>83829</td>
<td>9128</td>
<td>90587</td>
</tr>
<tr>
<td>2001-02</td>
<td>164523</td>
<td>157348</td>
<td>7175</td>
<td>100594</td>
</tr>
<tr>
<td>2002-03</td>
<td>314706</td>
<td>310510</td>
<td>4196</td>
<td>109299</td>
</tr>
<tr>
<td>2003-04</td>
<td>590190</td>
<td>543381</td>
<td>46808</td>
<td>139616</td>
</tr>
<tr>
<td>2004-05</td>
<td>839708</td>
<td>837308</td>
<td>2200</td>
<td>149600</td>
</tr>
<tr>
<td>2005-06</td>
<td>1098149</td>
<td>1045370</td>
<td>52779</td>
<td>231862</td>
</tr>
</tbody>
</table>

Source: Annual Report of RBI 2005-06

Of the net amount of resources mobilised by all mutual funds, the private sector mutual funds accounted for 81.4 per cent, followed by public sector mutual funds (12.1 per cent) and the UTI Mutual Fund (6.5 per cent). The shares of private sector mutual funds, public sector mutual funds and the UTI Mutual Fund in the gross mobilisation were 83.3 per cent, 10.1 per cent and 6.6 per cent, respectively during 2005-06. The share of private sector mutual funds in the gross mobilisation of resources declined modestly in 2005-06 over the previous year. On the contrary, the shares of other two categories of mutual funds improved marginally during the same period. Scheme-wise, resource mobilization witnessed an important shift in the pattern in the wake of strong rally in the stock markets during 2005-06. In consonance with the unusual buoyancy in the stock market, the amount of resources mobilised under growth and equity oriented schemes rose
Role of Mutual Funds

substantially in 2005-06. The net inflow of funds at Rs.35,231 crore in 2005-06
was the highest under growth/ equity oriented schemes in a single year, followed
by income and debt oriented schemes (Rs.16,622 crore). This can be depicted by
the following table:-

Table: 7

Sector-wise Resource Mobilization by Mutual Funds during 2005-06
(Rs in Crore)

<table>
<thead>
<tr>
<th>Particular</th>
<th>Private Sector MFs</th>
<th></th>
<th>Public Sector MFs</th>
<th></th>
<th>UTI MF</th>
<th>UTI MF</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Open-ended</td>
<td>Close-ended</td>
<td>Total</td>
<td>Open-ended</td>
<td>Close-ended</td>
<td>Total</td>
</tr>
<tr>
<td>Mobilization of</td>
<td>875917 (720603)</td>
<td>38786 (15860)</td>
<td>914703 (736463)</td>
<td>110142 (55771)</td>
<td>176 (818)</td>
<td>110319 (56589)</td>
</tr>
<tr>
<td>Funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Repurchase/</td>
<td>859367 (718440)</td>
<td>12360 (10423)</td>
<td>871727 (728864)</td>
<td>103580 (58976)</td>
<td>360 (290)</td>
<td>10390 (59266)</td>
</tr>
<tr>
<td>Redemption Amount</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net Inflow / Outflow of funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(16550 (2163))</td>
<td>(26426 (5437))</td>
<td>(42977 (7600))</td>
<td>(5662 (-3205))</td>
<td>(-183 (528))</td>
<td>(6379 (-2677))</td>
<td>(2671 (-2930))</td>
</tr>
</tbody>
</table>

Source: Annual Report of RBI 2005-06

Undoubtedly the start of the mutual funds industry in India was slow but
steady. But what is heartening to note is that after such a slow start, the industry
has picked up and is presently going through a phase which can be described as
an interesting one. The last few years have really been noteworthy for the
industry. Today, mutual funds have become popular among the customers and
have gained wide acceptability as a savings vehicle among the investors. The performance of many funds has been good, a strong distribution network has been established, products are in line with customer preference and requirements and the industry on the whole is on a growth path. A very important noteworthy thing is that the Indian mutual fund industry is likely to increase its present share of 6 per cent to the Gross Domestic Product (GDP) to 40 per cent in the next ten years on the condition that India’s growth rate consistently exceeds at the rate of 6 per cent per annum. Globally, mutual funds have become a very popular avenue of investment. As far as India is concerned, the mutual funds have attracted mass investors only with the advent of private players. Also, there has been a distinct shift in investor’s preference towards mutual funds investment. According to a study conducted by the Associated Chamber of Commerce and Industry of India (ASSOCHAM) and the Association of Mutual Fund Industry of India (AMFI), the size of the Indian mutual fund industry is estimated to go up to over Rs 1, 65, 000 crore by 2014. If the market is to access a greater portion of savings, then MFs will have to mobilise funds from many more households and channelise them to the bourses. On the other hand, distributors should also be regulated quickly, so as to maintain a crucial interface between funds and investors attains some sense of structure and also avoid the malpractices which currently plague it. Often, distributors have been blamed for creating an artificial churn among funds, causing problems for investors. A set of regulations and a clear institutional set-up to implement these and monitor distributors will have to be an essential part of what the MF industry would call “second generation reforms” of the sector. Amfi
is also working on standardization of operational areas and services, including investor communication. However, if we compare proportion of people investing in mutual funds in India with that in U.S, then we find that in U.S more than 50% people invest in mutual funds whereas in India the proportion is less than 10%. This gives the indication that there is much more untapped potential for growth in this industry in India which must be explored in the coming time. In conclusion, it can be said that despite few problems, the recent changes in the mutual funds industry in India has really favored its amazing growth and in conclusion it can be said that in times to come mutual funds will continue to remain a financial services where lot of money would be raining.
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