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PROBLEM AND PROSPECTS OF MUTUAL FUND IN INDIA

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ABSTRACT

Mutual fund as an institutional investor provides the character and strength to capital market and meets the peoples' requirement of increase their wealth. Since the start of liberalization policy, activity of mutual funds has increased the intensive penetration of market institutionalization in Indian national economy which attracts sufficiently the many role played by it in developmental process. So as to accelerate the developmental process, a rustic not only needs high savings rate but also the high holding pattern of such savings. Savings kept in the sort of idle assets is of no use until or unless deposited or invested somewhere to induce it multiplied. Indian household investors value more highly to invest only 10 percent of their wealth in capital market. The household sector investors have always been the most important contributors of country's total savings. They have the sort of monetary intermediary like investment trust which may manage their wealth in an exceedingly more productive manner. This is often why mutual funds are presupposed to be the simplest investment vehicle for household investors, and have proved the last word source globally for guiding the investors of small means. Our study could also be useful to many groups of individuals – fund managers, asset management companies, investment policy makers, monetary economists and investors for having a thought about nature and intensity of the problematic areas in Indian mutual funds and also the likely creation of strategies suitable to chase away the negative effects. It's some broader implications for the investment company professionals like developing the customer/ investor focused strategies, specializing in the areas important to boost fund performance, uncovering hidden growth drivers and framing policies/ regulations conducive to the healthy growth of the mutual funds industry.

Keywords: *Investors, Savings, Global, Capital, Intermediary, Monetary, Contributions, Growth.*

Introduction

Government generally utilised the idle savings of a rustic for its various purposes of achieving economic process. Savings are given paramount importance in promoting the economic process of India since independence. Present savings rate of India is above 30 percent which continues to stay one in every of the high among the emerging market economies. But, its conversion rate into investment from the household sector is extremely low. That's why people in India are rated nearly as good savers due to their great savings habits but they're poor investors due their limited knowledge about investment. Indian mutual funds industry couldn't establish its worthiness because the preferred investment vehicle among the overall investors till now despite having quite 45 years of its existence. There are factors adversely affecting the investors' confidence in mutual funds industry in India but at the identical time, fostering economic variables are giving faith for its bright future. This contradictory state prompted us to assess the aforesaid phenomenon by examining the performance, regulations, problems and prospects of mutual funds in India. Growth and development of varied investment company products in Indian Capital market has proved to be one in every of the foremost catalytic instruments in generating momentous investment growth in the capital market. During this

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context, close monitoring and evaluation of mutual funds has become essential. With emphasis on increase in domestic savings and improvement in deployment of investment through markets, the necessity and scope for mutual funds operation has increased tremendously. Thus, the involvement of mutual funds in the transformation of Indian economy has made it urgent to look at their services not only as financial intermediary but also as a pace setter as they play a major role in spreading equity culture. Our study attempts to analyse the performance of open-end fund schemes in India so on understand the issues and challenges faced by the industry. In the present chapter, we've outlined the database and methodology of the study.

Advantages of Mutual Funds

Mutual fund offers several advantages to the overall investors. Investors gain the automated good thing about research and low-cost information services by investing in mutual funds. Major advantages of mutual funds are as follows:

- **Professional Management:** open-end fund portfolio is managed by highly experienced and skilled professionals who are supported by dedicated investment research team for analysing the performance and prospects of companies and therefore the entire range of economic sectors, with an aim to pick the acceptable investment plan matching the investor’s risk profile.
- **Diversification:** Diversification could be a risk reduction strategy that works on the maxim of “do not put all of eggs in one basket”. Investment firm follows this maxim and reduces risk by investing in a very sizable amount of companies across a broad section of industries and sectors. Diversification reduces the investment risk of a portfolio because seldom do all stocks decline at the identical time and in the same proportion. A small investor gets the advantage of such diversification by buying the units of open-end fund.
- **Higher Returns:** Returns offered by mutual funds are comparatively better than the other investment alternative. People can invest their money in medium to long-term investment horizon and might enjoy the upper returns as generated from investing during a diversified basket of selected securities.
- **Affordable, Flexible and Low Costs:** open-end fund offers comparatively less costly due to invest as compared to other avenues like capital market investment. The fee in terms of brokerages, custodial fees and other management fees are substantially under other options and are directly linked to the performance of the scheme. Investment in mutual funds also offers plenty of flexibility with features like regular investment plans, regular withdrawal plans and dividend reinvestment plans enabling systematic investment or withdrawal of funds. Even the investors, who could otherwise not enter stock markets with low investible funds, can get pleasure from a portfolio comprising of high-priced stocks because they're purchased from pooled funds.
- **Liquidity:** Investors in open-ended investment firm schemes can withdraw or redeem their investment anytime at the online asset value (NAV) related prices. In close-ended schemes, the units is redeemed at the prevailing market prices in an exceedingly exchange.
- **Regulatory Supervision:** to guard the interest of investors, investment trust must fit the strict regulatory norms framed by country/ state regulatory authorities. These norms stipulate mutual funds to disclose necessary information submit several reports and publish operational details for public information.
- **Numerous Options:** Mutual funds provide variety of options to their investors so on meet their diverse needs. These options are in the kind of different funds like income funds, balanced funds, liquid funds, gilt funds, index funds, exchange traded funds, sectoral funds etc. Investor can choose the fund of his or her particular need in the available basket of securities.
- **Transparency:** Mutual funds are required to disclose their portfolio composition, investment pattern, strategies, outlook and every one other relevant information that may be considered as useful to investors. The frequency of normal investment information maintains the arrogance of investors in open-end investment company and ensures transparency in the system.
- **Accessibility:** An investor can easily purchase the open-end investment company units from registered brokers/ agents with or without the desired sales charges. Units can even be purchased directly from the web site of particular investment firm. Hence, investment firm units are accessed anywhere, regardless of where the investor is situated.

Problems of Mutual Funds

Mutual funds industry in India has emerged jointly of the most important constituents of Indian economic system. It's completed over 45 years of its presence. During this short period, it grew fast and also suffered from equally fast decline. It became sick in its early life. It's witnessed noticeable structural transformation, quantitative growth, qualitative and quantitative decline and maybe the revival, which can put the industry back on the right track. The decline in funds industry had been attributed to the factors like

- Prolonged bearish trends and scams in Indian securities market that killed the investors' interest in equities and units
- The autumn of UTI broke the investors' faith and confidence
- Unattractive returns on mutual fund schemes. Although, good performance of debt funds helped the industry for a few time, the continual reduction in interest rates in the economy has adversely affected the expansion momentous of investment company's industry again
- Withdrawal of tax benefits under Section 80M of Income Tax Act
- Poor performance of mutual fund schemes
- Series of crisis, scandals and frauds.

The above-mentioned factors have created supplementary flaws and setbacks for the mutual funds industry at various points of time and are among the most important causes of the decline in mutual funds industry. The foremost weaknesses and problems of the Indian mutual funds industry are examined below:

- **Low Level of Awareness:** the notice of investors determines the success of mutual funds industry. In India, low investors awareness/ information level and financial literacy are causing biggest threats to mutual funds industry in channelising the household savings into mutual funds. The bulk of recent investors don't understand the concept, operations and advantages of investment in mutual funds. The shortage of understanding about open-end fund products is more pervasive in semi-urban and rural areas. Majority of individuals in these areas find it difficult to differentiate between mutual funds and direct exchange investments.
- **Regulatory Problems**: a powerful regulatory framework is that the key to success for any business environment and then is that the case for Indian mutual funds industry. The extent of competition in the industry has continuously been mounting. So, it has to perform a more dynamic and vibrant role to satisfy the tests of time. We've observed some areas in investment firm regulations which are to be addressed soon so to make it more competitive and transparent.
- **Improper Investment Policy Disclosure:** Mutual funds are stipulated to possess investment policy in written form. Investment policy links the investment objective of a fund, to a fund manager's daily working strategy. The efficacy of the investment policy depends on the clarity of visions with which it's executed or achieved. Investment company schemes have followed tough and vague language in writing their investment policies. These are written during a manner that the investor may get confused. Also, the investment objectives of schemes are found descriptive in nature and it's difficult to draw the generalisations out of them. The portfolio turnover rates of last five years of the schemes also are not mentioned in the offer documents.
- **Low Participation and Penetration:** Low retail participation is the biggest challenge posed before the Indian mutual funds industry regardless the provision of favourable retail environment and ample growth opportunities in the Indian economy. This is often due to the mindset of current investment managers who think institutional money because the easiest route of getting a giant slice of cake in one goes. The supply of tax arbitrage and enormous ticket volume to corporates on investing in securities industry mutual funds and therefore the easy accessibility of institutional investors in Tier I cities appear to be important factors accountable for this phenomenon. The main focus on retail segment requires significant distribution capabilities, wide network and intense foot prints. It's noteworthy that Asset Management Companies (AMCs) have recently begun to target these aspects.

- **Limited Products:** The mutual funds industry in India offers limited products to satisfy the wants of investors. Unlike the US, UK and Japan, the Indian mutual funds industry is incredibly slow in offering innovative products to investors. In US, different mutual funds are available for the complete life of investors. Schemes, quite 10,000 in number, appropriate every economic and social need of investors, be it a university admission (College Target Date Funds), retirement (Retirement Target Date Funds) or purchasing of the property. The products catering to the wants of investors require the event of funds associated with education, marriage and housing etc. The industry remains to launch a spread of ETFs, college savings fund, e-funds, green funds, socially responsible financial instruments, fund of hedge funds, advanced securities industry funds, renewable and energy/ temperature change funds, rural and concrete development funds etc. The industry doesn't offer the capital guarantee schemes for the investors who are risk averse. It's not introduced schemes suitable for farmers, small entrepreneurs and merchant to tap the savings in the rural segment. The merchandise restructuring to tap the target customers is additionally not excellent.
- **Malpractices in Trading:** Mutual funds are founded as trusts and thereby have a legal duty towards their investors. They need the responsibility to confirm that the trading of mutual funds is aligned to the regulations and interests of investors are duly protected. Regulations are devised to forestall fraudulent activities and digressions from deceptive and manipulative practices by insiders related to personal securities transactions. Mutual funds involved in unfair trade practices are restrained in the manner provided under the Securities and Exchange Board of India (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002.

Prospects of Mutual Funds in India

Mutual funds constitute a awfully important component of the capital market in developed countries and now, are becoming the colourful institutions in emerging markets like India. In the coming years, the mutual funds in India are likely to emerge as important players in the capital marketplace for managing the funds of small investors. The country's economic and financial health, regulatory framework, and therefore the performance of the funds are likely to play a crucial role when making a decision the longer term prospects of the industry. Undoubtedly, SEBI has put in situation a well-defined regulatory framework for mutual funds in India. The regulatory mechanism and supervisory control are strong and efficient enough to safeguard the interest of investors. A number of these major steps are allowance of upper expense ratio, removal of internal limits in expense ratio, crediting back of exit load to schemes, charge on investors, option of direct selling, cash investment in mutual funds and therefore the regulation of distributors. These steps will definitely improve the penetration of mutual funds and strengthen the distribution network in our country. The distributors must work effortlessly to induce more business because lower business means proportionately lower expense ratios. Under the approach, mutual funds must disclose all the efforts taken by them to extend the geographical penetration and also the details of the opening of recent branches especially at locations aside from the highest 15 cities. This move will increase the reach of mutual funds to smaller towns and places in India and thus augment the expansion of the industry in coming years. Another step that features, the removal of internal limits on the expense ratio could be a big change for the AMCs.

The all above data we will predict a awfully bright future for the mutual funds industry in India. However, to be more competitive, the industry is usually recommended to require necessary steps with relevance regulations involving fund governance, penalty, education, distribution, fund names and investment policies disclosure provisions. Also, to spice up up the boldness of investors, the issues and queries of investors are needed to be handled properly and promptly. Hence, check on operational costs is required. After sales services is required to be sound. There's also a requirement to feature variety into products marketed by mutual funds. Differing kinds of ETFs, college savings fund, e-funds, green funds, socially responsible financial instruments, fund of hedge funds, advanced market funds, renewable and energy/ global climate change funds, rural and concrete development funds etc. need to be developed to cater to the complete needs of investors and economy. Investment trust companies are required to upgrade their skills, technology and price management techniques.

Conclusion

The study of problems of mutual funds reveals that investor low level of awareness and rising costs are the mainstream problems of industry. Due to this, retail participation has been quite low. The industry has yet to tap potential customers in small cities and rural areas. Compared to US, UK and Japan, the Indian mutual funds industry is incredibly slow in innovative product offering. The mis selling by distributors that basically put a matter mark on the competence, value and degree of commitment of fund distributors to investors. In our review of offer documents of selected investment firm schemes viz., Birla Sun Life, LIC Nomura, UTI and Sahara found ambiguous description of risk factors and risk controlling procedures, absence of portfolio turnover rates and use of tough and vague language. On regulatory front, the industry, in spite of getting a comprehensive set of regulations, still has some problematic areas. A number of these are inadequate fund governance provisions, small penal provisions for officers and key personnel, absence of qualification for fund managers and trustees, lack of proper regulations for distributors, low flexibility in funds investment objectives and confusing products names and definitions. Other problems of mutual funds include the rising investors' complaints, malpractices in trading, low financial literacy, single lingual mechanism, secrecy in documents and herding behaviour of investors. The mutual funds industry in India has evolved in many aspects, be it the entire assets accretion, products offered, number of investor accounts, players or the amount of technological up gradation. The industry is anticipated to grow rapidly due to favourable economic & financial scenario, conducive regulatory environment and due the very fact that Indian class has shown enormous interest in recent years. The rising saving rate and dealing age population in the country may further accelerate investment in mutual funds in coming years.

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