

**EXPLORING THE DYNAMICS BETWEEN MUTUAL FUND AND INVESTORS BEHAVIOUR****UNDER THE GUIDANCE OF PROF. DR. CHHAVI PRAKASH****Submitted By RIYA KUMARI    22GSOB2011032****SCHOOL OF BUSINESS GALGOTIAS UNIVERSITY****INTRODUCTION**

The basic purpose is to know about the Mutual Fund Industry and to know the behavior of the Indian Investors regarding different investment tools.

This project will provide me the better platform to understand the History, Growth and various other aspects of Mutual Fund. It will also help me to understand the behavior of Indian investor regarding different investment tools.

SEBI is the apex regulatory of capital markets. SEBI has enacted the SEBI (mutual fund) Regulations, 1996, which provides the scope of the regulation of the mutual fund in India. All Mutual funds are required to be mandatory registered with SEBI. The structure and formation of mutual funds, appointment of key functionaries, operation of the mutual funds, accounting and disclosure norms, rights and obligations of functionaries and investors, investment restrictions, compliance and penalties are all defined under the SEBI regulations. Mutual funds have to send half yearly compliance reports to SEBI, and provide all information about their operations

*The term investment plans generally refers to the services that the funds provide to investors offering different ways to invest or invest. The different investment plans are important considerations in the investment decisions because they determine the level of flexibility available to the investor*

*Alternate investment plans offered by the fund allow the investor freedom with respect to investing at one time or at regular intervals, making transfers to different schemes within the same fund family or receiving income at specified intervals or accumulating*

A mutual fund is a pool of money, collected from investors, and is invested according to certain investment options. A mutual fund is a trust that pools the savings of a number of investors who share a common financial goal. A mutual fund is created when investors put their money together. It is therefore a pool of the investor's funds. The money thus collected is then invested in capital market instruments such as shares, debentures and other securities. The income earned through these investments and the capital appreciations realized are shared by its unit holders in proportion to the number of units owned by them.

The most important characteristics of a fund are that the contributors and the beneficiaries of the fund are the same class of people, namely the investors. The term mutual fund means the investors contribute to the pool, and also benefit from the pool. There are no other claimants to the funds. The pool of funds held mutually by investors is the mutual fund.

A mutual funds business is to invest the funds thus collected according to the wishes of the investors who created the pool. Usually, the investors appoint professional investment managers, to manage their funds. The same objective is achieved when professional investment managers create a product and offer it for investment to the investor. This product represents a share in the pool, and pre states investment objectives. Thus a mutual fund is the most suitable investment for the common man as it offers an opportunity to invest in a diversified, professionally managed basket of securities at a relatively low cost.

Investors in the mutual fund industry today have a choice of 39 mutual funds, offering nearly 500 products. Though the categories of product offered can be classified under about a dozen generic heads, competition in the industry has led to innovative alterations to standard products. The most important benefit of product choice is that it enables investors to choose options that suit their return requirements and risk appetite.

## 1. Features that investors like in mutual fund

If mutual funds are emerging as the favorite investment vehicle, it is because of the many advantages they have over other forms and avenues of investing, particularly for the investor who has limited resources available in terms of capital and a ability to carry out detailed research and market monitoring. The following are the major advantages offered by mutual funds to all investors.

◆ **Portfolio diversification:** Mutual Funds normally invest in a well- diversified portfolio of securities. Each investor in a fund is a part owner of all of the fund's assets. This enables him to hold a diversified investment portfolio even with a small amount of investment that would otherwise require big capital.

◆ **Professional management;** Even if an investor has a big amount of capital available to him, he lacks the professional attitude that is generally present in the experienced fund manager who ensures a much better return than what an investor can manage on his own. Few investors have the skills and resources of their own to succeed in today's fast moving, global and sophisticated markets.

◆ **Reduction/ diversification of risk:** An investor in a mutual fund acquires a diversified portfolio, no matter how small his investment. Diversification reduces the risk of loss, as compared to investing directly in one or two shares or debentures or other

Instruments. When an investor invests directly, all the risk of

potential loss is his own. A fund investor also reduces his risk in

## 2. Automatic Reinvestment Plans (ARP)

In India, many funds offer two options under the same scheme the dividend option and the growth option. The dividend option or the Automatic Reinvestment Plans (ARP) allows the investor to reinvest in additional units the amount of dividends or other distribution made by the fund, instead of receiving them in cash. Reinvestment takes place at the ex-dividend NAV. The ARP ensures that the investors reap the benefit of compounding in his investments. Some funds allow reinvestments into other schemes in the fund family.

## 3. Automatic Investment Plans (AIP)

These require the investor to invest a fixed sum periodically, there by letting the investor save in a disciplined and phased manner. The mode of investment could be through debit to the investor's salary or bank account. Such plans are also known as the Systematic Investment Plans. But mutual funds do not offer this facility on all the schemes. Typically they restrict it to their plain vanilla schemes like diversified equity funds,

Income funds and balanced funds. SIP works best in equity funds. It enforces saving discipline and helps you profit from market volatility- you buy more units when the market is down and fewer when the market is up.

## 2.MUTUAL FUNDS



### Introduction to Mutual funds

A Mutual fund is a trust that pools the savings of a number of investors who share a common financial goal. The money thus collected is then invested in capital market instruments such as shares, debentures and other securities. The income earned through these investments and the capital appreciations realized are shared by its unit holders in proportion to the number of unit owned by them. Thus a Mutual fund is the most suitable investment for the common man as it offers an opportunity to invest in a diversified, professionally managed basket of securities at a relatively low cost.

The flow chart below describes broadly the working of a Mutual fund.



A Mutual fund is a body corporate registered with the Securities and Exchange Board of India (SEBI) that pools up the money from individual/corporate investors and invests the same on behalf of the investors/unit holders, in Equity shares, Government securities, Bonds, Call Money Markets etc, and distributes the profit. In the other words, a

Mutual fund allows investors to indirectly take a position in a basket of assets.

Mutual fund is a mechanism for pooling the resources by issuing unit to the investors and investing funds in securities in accordance with objectives as disclosed in offer document. Investments in securities are spread among a wide cross-section of industries and sectors thus the risk is reduced. Diversification reduces the risk because all stocks may not move in the same direction in the same proportion at same time. Investors of mutual funds are known as unit holders.

The investors in proportion to their investments share the profit or losses. The mutual funds normally come out with a number of schemes with different investment objectives which are launched from time to time. A Mutual fund is required to be registered with Securities Exchange Board of India (SEBI) which regulates securities markets before it can collect funds from the public.

## ORGANISATION OF A MUTUAL FUND

There are many entities involved and the diagram below illustrates the organizational set up of a Mutual fund:



Mutual funds diversify their risk by holding a portfolio of instead of only one asset. This is because by holding all your money in just one asset, the entire fortunes of your portfolio depend on this one asset. By creating a portfolio of a variety of assets, this risk is substantially reduced.

Mutual fund investments are not totally risk free. In fact, investing in Mutual funds contains the same risk as investing in the markets, the only difference being that due to professional management of funds the controllable risks are substantially reduced. A very important risk involved in Mutual fund investments is the market risk. However, the company specific risks are largely eliminated due to professional fund management.

**IMPORTANT CHARACTERISTICS OF A MUTUAL FUND**

- ☐ A Mutual fund actually belongs to the investors who have pooled their Funds. The ownership of the mutual fund is in the hands of the investors.
- ☐ A Mutual fund is managed by investment professional and other Service providers, who earn a fee for their services, from the funds.
- ☐ The pool of Funds is invested in a portfolio of marketable investments.
- ☐ The value of the portfolio is updated every day.
- ☐ The investor's share in the fund is denominated by "unit-s". The value of the unit changes with change in the portfolio value, every day. The value of one unit of investment is called net asset value (NAV).
- ☐ The investment portfolio of the mutual fund is created according to the stated investment objectives of the fund.



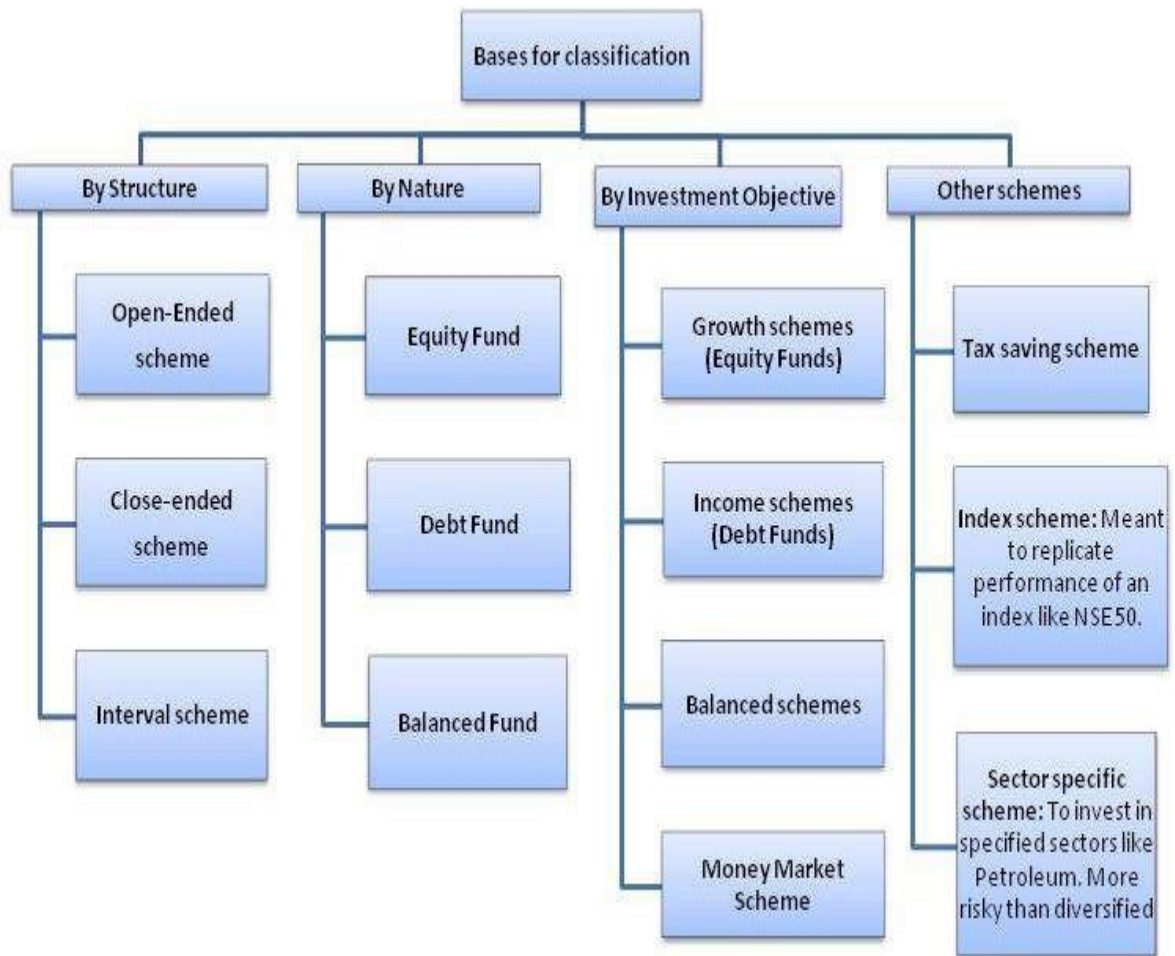
## OBJECTIVES OF A MUTUAL FUND

- ☐ To provide an opportunity for lower income groups to acquire without much difficulty, property in the form of shares.
- ☐ To cater mainly of the need of individual investors, whose means are small.
- ☐ To manage investors portfolio that provides regular income, growth, safety, liquidity, tax advantage, professional management and diversification.

## ADVANTAGES OF MUTUAL FUNDS

- ☐ Reduced risk.
- ☐ Diversified investment.
- ☐ Botheration free investment.
- ☐ Revolving type of investment (Reinvestment).
- ☐ Selection and timings of investment.
- ☐ Wide investment opportunities.
- ☐ Investments care.
- ☐ Tax benefits.

## STRUCTURE OF A MUTUAL FUND



## ● INVESTORS PROFILE

An investor normally prioritizes his investment needs before undertaking an investment. Different goals will be allocated to different proportions of the total disposable amount. Investments for specific goals normally find their way into the debt market as risk reduction is of prime importance, this is the area for the risk-averse investors and here, mutual funds are generally the best option to invest in, can be minimized by investing in mutual funds as the fund managers analyze the companies financials more minutely than an individual can do as they have the expertise to do so.

Moving up the risk spectrum, there are people who would like to take some risk and invest in equity funds/capital market. However, since their appetite for risk is also limited, they would rather have some exposure to debt as well. For these investors, balanced funds provide an easy route of investment, armed with expertise of investment techniques, they can invest in equity as well as good quality debt thereby reducing risks and providing the investor with better returns than he could otherwise manage.

Next comes the risk takers, risk takers by their nature, would not be averse to investing in high-risk avenues. Capital markets find their fancy more often than not, because they have historically generated better returns than any other avenue, provided, the money was judiciously invested. Though the risk associated is generally on the higher side of the spectrum, the return-potential compensates for the risk attached.



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## ■ TYPES OF MUTUAL FUNDS

### Schemes by investment Objective

- Growth / Equity Oriented Scheme
- Income / Debt Oriented Scheme
- Balanced Scheme
- Money Market or Liquid Fund Scheme

### Other Objective

- Gilt Fund
- Index Funds
- Load AND no-load Fund
- Tax Saving Schemes

### Schemes By Structure In Detail

A mutual fund scheme can be classified into open-ended scheme or close-ended scheme depending on its maturity period

#### **a. Open-ended Fund/ Scheme**

The holders of the shares in the fund can resell them to the issuing mutual fund company at the time. They receive in turn the net assets value (NAV) of the shares at the time of re-sale. Such mutual fund companies place their funds in the secondary securities market. They do not participate in new issue market as do pension funds or life insurance companies. Thus they influence market price of corporate securities. Open-end investment companies can sell an unlimited number of shares and thus keep going

larger. The open-end mutual fund company buys or sells their shares. These companies sell new shares NAV plus a loading or management fees

and redeem shares at NAV. In other words, the target amount and the period both are indefinite in such funds. An open-ended fund or scheme is one that is available for subscription and repurchase on a continuous basis. These schemes do not have a fixed maturity period. Investors can conveniently buy and sell units at Net Asset Value (NAV) related prices which are declared on a daily basis. The key feature of open-end schemes is liquidity.

**b. Close-ended Fund/ Scheme**

A closed-end fund is open for sale to investors for a specific period, after which further sales are closed. Any further transaction for buying the unit or repurchasing them, happen in the secondary markets, where closed end funds are listed. Therefore new investors buy from the existing investors, and existing investors can liquidate their unit by selling them to other willing buyers. In a closed end funds, thus the pool of funds can technically be kept constant. The asset management company (AMC) however, can buy out the unit from the investors, in the secondary markets, thus reducing the amount of funds held by outside investors. The price at which unit can be sold or redeemed depends on the market prices, which are fundamentally linked to the NAV. Investors in closed end funds receive either certificates or Depository receipts, for their holdings in a closed end mutual fund.

A close-ended fund or scheme has a stipulated maturity period e.g. 5-7 years.

The fund is open for subscription only during a specified period

at the time of launch of the scheme. Investors can invest in the scheme at the time of the initial public issue and thereafter they can buy or sell the unit of the scheme on the stock exchanges where the unit are listed. In order to

provide an exit route to the investors, some close-ended funds give an option of selling back the unit to the mutual fund through periodic re-purchase at NAV related prices. SEBI Regulations stipulate that at least one of the two exit routes is provided to the investor i.e. either repurchase facility or through listing on stock exchanges. These mutual funds schemes disclose NAV generally on weekly basis.

### **Schemes according to Investment Objective In Detail**

A scheme can also be classified as growth scheme, income scheme, or balanced scheme considering its investment objective. Such schemes may be open-ended or close-ended schemes as described earlier. Such schemes may be classified mainly as follows:

#### **a. Growth / Equity Oriented Scheme**

The aim of growth funds is to provide capital appreciation over the medium to long- term. Such schemes normally invest a major part of their corpus in equities. Such funds have comparatively high risks. These schemes provide different options to the investors like dividend option, capital appreciation, etc. and the investors may choose an option depending on their preferences. The investors must indicate the option in the application form. The mutual funds also allow the investors to change the options at a later date. Growth schemes are good for investors having a long-term outlook seeking appreciation over a period of time.

#### **b. Income / Debt Oriented Scheme**

The aim of income funds is to provide regular and steady income to investors. Such schemes generally invest in fixed income securities such as

bonds, corporate debentures, Government securities and money market instruments. Such funds are less risky compared to equity schemes. These funds are not affected because of fluctuations in equity markets. However, opportunities of capital appreciation are also limited in such funds. The NAVs of such funds are affected because of change in interest rates in the country. If the interest rates fall, NAVs of such funds are likely to increase in the short run and vice versa. However, long term investors may not bother about these fluctuations.

**c.                      Balanced Scheme**

The aim of balanced funds is to provide both growth and regular income as such schemes invest both in equities and fixed income securities in the proportion indicated in their offer documents. These are appropriate for investors looking for moderate growth. They generally invest 40-60% in equity and debt instruments. These funds are also affected because of fluctuations in share prices in the stock markets. However, NAVs of such funds are likely to be less volatile compared to pure equity funds.

**Other Schemes In Detail**

**a.                      Gilt Funds**

These funds invest exclusively in government securities. Government securities have no default risk. NAVs of these schemes also fluctuate due to change in interest rates and other economic factors as is the case with income or debt oriented schemes.

**b.                      Index Funds**

Index Funds replicate the portfolio of a particular index such as the BSE Sensitive index, S&P NSE 50 index (Nifty), etc. These schemes invest in the



securities in the same weightage comprising of an index. NAVs of such schemes would rise or fall in accordance with the rise or fall in the index, though not exactly by the same percentage due to some factors known as "tracking error" in technical terms. Necessary disclosures in this regard are made in the offer document of the mutual fund scheme. There are also exchange traded index funds launched by the mutual funds which are traded on the stock exchanges.

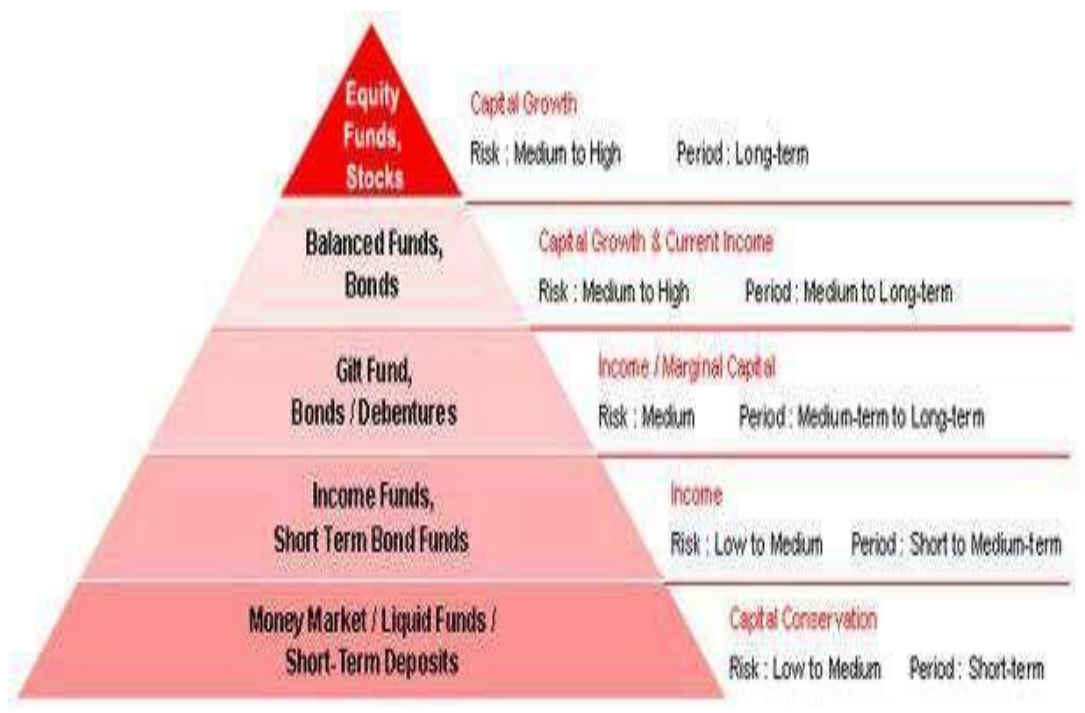
**c. Load And No-load Fund**

A load fund is one that charges a percentage of NAV for entry or exit. That is, each time one buys or sells unit in the fund, a charge will be payable. This charge is used by the mutual fund for marketing and distribution expenses. Suppose the NAV per unit is Rs.10. If the entry as well as exit load charged is 1%, then the investors who buy would be required to pay Rs.10.10 and those who offer their unit for repurchase to the mutual fund will get only Rs.9.90 per unit. The investors should take the loads into consideration while making investment as these affect their yields/returns. However, the investors should also consider the performance track record and service standards of the mutual fund which are more important. efficient funds may give higher returns in spite of loads.

A no-load fund is one that does not charge for entry or exit. It means the investors can enter the fund/scheme at NAV and no additional charges are payable on purchase or sale of unit.

**d. Tax Saving Schemes**

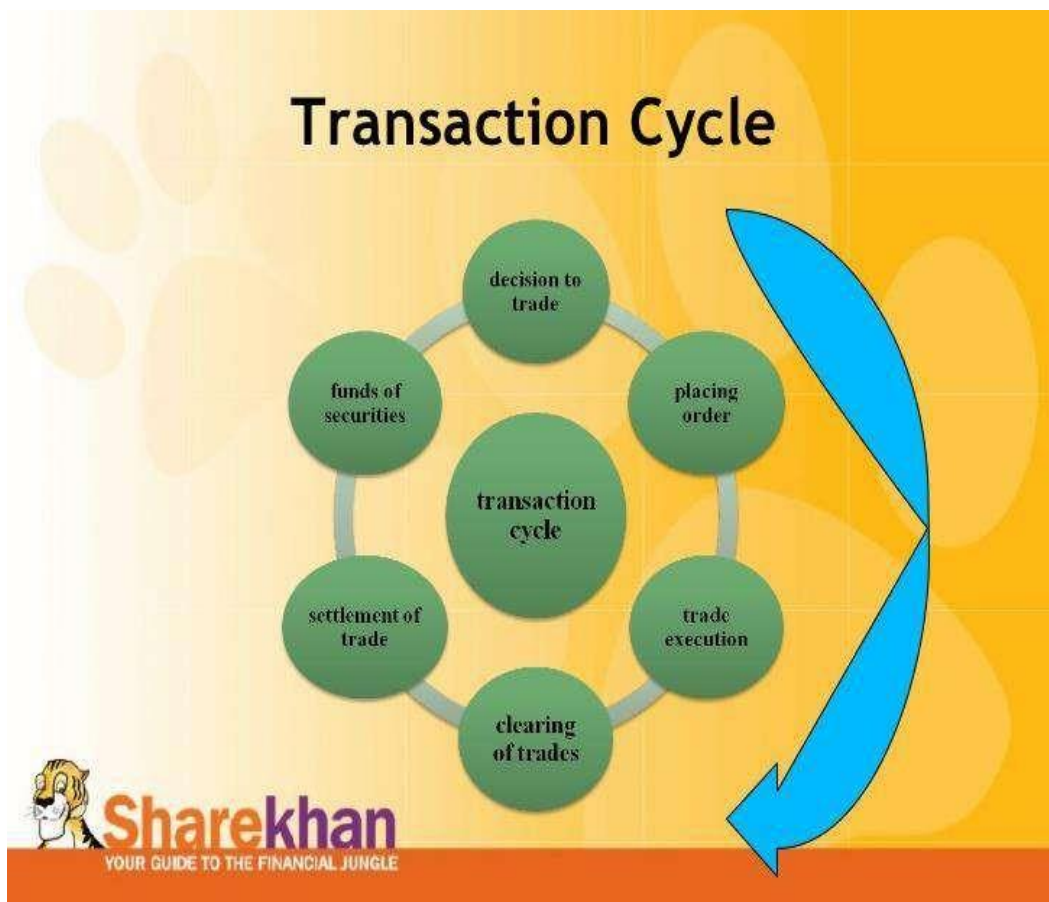
These schemes offer tax rebates to the investors under specific provisions of the Income Tax Act, 1961 as the government offers tax incentives for investment in specified avenues. e.g Equity Linked Savings Schemes (ELSS). Pension schemes launched by the mutual funds also offer tax benefits. These schemes are growth oriented and invest pre-dominantly in equities. Their growth opportunities and risks associated are like any equity- oriented scheme.



## ORGANISATION AND MANAGEMENT OF MUTUALFUNDS

In India mutual fund usually formed as trusts, three parties are generallyinvolved viz.

- ☐ Settler of the trust or the sponsoring organization.
- ☐ The trust formed under the **Indian trust act, 1982** or the trust company registered under the **Indian companies act, 1956**
- ☐ Fund managers or The merchant-banking unit
- ☐ Custodians.



## MUTUAL FUNDS TRUST

Mutual fund trust is created by the sponsors under the **Indian trust act, 1982** which is the main body in the creation of mutual fund trust

The main functions of mutual fund trust are as follows:

- ☐ Planning and formulating mutual funds schemes.
- ☐ Seeking SEBI's approval and authorization to these schemes.
- ☐ Marketing the schemes for public subscription.
- ☐ Seeking RBI approval in case NRI's subscription to mutual fund is invited.

☐ Attending to trusteeship function. This function as per guidelines can be assigned to separately established trust companies too. Trustees are required to submit a consolidated report six monthly to SEBI to ensure that the guidelines are fully being complied with trusted are also required to submit an annual report to the investors in the fund.

## FUND MANAGERS (OR) THE ASSETS MANAGEMENTCOMPANY (AMC)

AMC has to discharge mainly three functions as under:

- I. Taking investment decisions and making investments of the funds through market dealer/brokers in the secondary market securities or directly in the primary capital market or money market instruments
- II. Realize fund position by taking account of all receivables and realizations, moving corporate actions involving declaration of dividends, etc to compensate investors for their investments in units.

III. Maintaining proper accounting and information for pricing the units and arriving at net asset value (NAV), the information about the listed schemes and the transactions of units in the secondary market. AMC has to feed back the trustees about its fund management operations and has to maintain a perfect information system.

## **CUSTODIANS OF MUTUAL FUNDS**

Mutual funds run by the subsidiaries of the nationalized banks had their respective sponsor banks as custodians like Canara Bank, SBI, PNB, etc. Foreign banks with higher degree of automation in handling the securities have assumed the role of custodians for mutual funds. With the establishment of Stock Holding Corporation of India the work of custodian for mutual funds is now being handled by it for various mutual funds. Besides, industrial investment trust company acts as sub-custodian for stock Holding Corporation of India for domestic schemes of UTI, BOI MF, LIC MF, etc.

### **Fee structure**

Custodian charges range between 0.15% to 0.20% on the net value of the customer's holding for custodian services space is one important factor which has fixed cost element.

### RESPONSIBILITY OF CUSTODIANS

- ☐ Receipt and delivery of securities
- ☐ Holding of securities.
- ☐ Collecting income
- ☐ Holding and processing cost
- ☐ Corporate actions etc.

### FUNCTIONS OF CUSTOMERS

- ☐ Safe custody
- ☐ Trade settlement
- ☐ Corporate action
- ☐ Transfer agents

### RATE OF RETURN ON MUTUAL FUNDS

An investor in mutual fund earns return from two sources:

- ◆ Income from dividend paid by the mutual fund. Capital gains arising out of selling the unit at a price higher than

Schemes by structure

- Open-ended Fund/ Scheme
- Close-ended Fund/ Scheme
- ◆ the acquisition price

### Formation and regulations

1. Mutual funds are to be established in the form of trusts under the **Indian trusts act** and are to be operated by separate asset management companies (AMC s)
2. AMC's shall have a minimum **Net worth of Rs. 5 crores;**

3. AMC's and Trustees of Mutual funds are to be two separate legal entities and that an AMC or its affiliate cannot act as a manager in any other fund;
4. Mutual funds dealing exclusively with money market instruments are to be regulated by the Reserve Bank Of India
5. Mutual fund dealing primarily in the capital market and also partly money market instruments are to be regulated by the **Securities Exchange Board Of India (SEBI)**
6. All schemes floated by mutual funds are to be registered with SEBI

**Schemes**

1. Mutual funds are allowed to start and operate both closed-end and open-end schemes;
2. Each closed-end schemes must have a **Minimum corpus (pooling up) of Rs 20 crore;**
3. Each open-end scheme must have a **Minimum corpus of Rs 50 crore**
4. In the case of a Closed –End scheme if the **Minimum amount of Rs 20 crore or 60%** of the target amount, whichever is higher is not raised then the entire subscription has to be refunded to the investors;
5. In the case of an Open-Ended schemes, if the minimum amount of **Rs 50 crore or 60 percent** of the targeted amount, whichever is higher, is not raised then the entire subscription has to be refunded to the investors.

**Investment norms**

1. No mutual fund, under all its schemes can own more than five percent of any company's paid up capital carrying voting rights;
2. No mutual fund, under all its schemes taken together can invest more than 10 percent of its funds in shares or debentures or other instruments of any single company;
3. No mutual fund, under all its schemes taken together can invest more than 15 percent of its fund in the shares and debentures of any specific industry, except those schemes which are specifically floated for investment in one or more specified industries in respect to which a declaration has been made in the offer letter.
4. No individual scheme of mutual funds can invest more than five percent of its corpus in any one company's share;
5. Mutual funds can invest only in transferable securities either in the money or in the capital market. Privately placed debentures, securitized debt.
6. Unquoted debt, and other unquoted debt instruments holding cannot exceed 10 percent in the case of growth funds and 40 percent in the case of income funds.

**Distribution**

Mutual funds are required to distribute at least 90 percent of their profit's annually in any given year. Besides these, there are guidelines governing the operations of mutual funds in dealing with shares and also seeking to ensure greater investor protection through detailed disclosure and reporting by the mutual funds. SEBI has also been granted with powers to oversee the constitution as well as the operations of mutual funds, including a common advertising code. Besides, SEBI can impose penalties on Mutual funds after due investigation for their failure to comply with the guidelines.





## MUTUAL FUND SCHEME TYPES



### **Equity Diversified Schemes**

These schemes mainly invest in equity. They seek to achieve long-term capital appreciation by responding to the dynamically changing Indian economy by moving across sectors such as Lifestyle, Pharma, Cyclical, Technology, etc.



### **Sector Schemes**

These schemes focus on particular sector as IT, Banking, etc. They seek to generate long-term capital appreciation by investing in equity and related securities of companies in that particular sector.



### **Index Schemes**

These schemes aim to provide returns that closely correspond to the return of a particular stock market index such as BSE Sensex, NSE Nifty, etc. Such schemes invest in all the stocks comprising the index in approximately the same weightage as they are given in that index.



### **Exchange Traded Funds (ETFs)**

ETFs invest in stocks underlying a particular stock index like NSE Nifty or BSE Sensex. They are similar to an index fund with one crucial difference. ETFs are listed and traded on a stock exchange. In contrast, an index fund is bought and sold by the fund and its distributors.

**Equity Tax Saving Schemes**

These work on similar lines as diversified equity funds and seek to achieve long-term capital appreciation by investing in the entire universe of stocks. The only difference between these funds and equity-diversified funds is that they demand a lock-in of 3 years to gain tax benefits.

**Dynamic Funds**

These schemes alter their exposure to different asset classes based on the market scenario. Such funds typically try to book profits when the markets are overvalued and remain fully invested in equities when the markets are undervalued. This is suitable for investors who find it difficult to decide when to quit from equity.

**Balanced Schemes**

These schemes seek to achieve long-term capital appreciation with stability of investment and current income from a balanced portfolio of high quality equity and fixed-income securities.

**Medium-Term Debt Schemes**

These schemes have a portfolio of debt and money market instruments where the average maturity of the underlying portfolio is in the range of five to seven years.

**Short-Term Debt Schemes**

These schemes have a portfolio of debt and money market instruments where the average maturity of the underlying portfolio is in the range of one to two years.

**Money Market Debt Schemes**

These schemes invest in debt securities of a short-term nature, which generally means securities of less than one-year maturity. The typical short-term interest-bearing instruments these funds invest in Treasury Bills, Certificates of Deposit, Commercial Paper and Inter-Bank Call Money Market.

□ **Medium-Term Gilt Schemes**

These schemes invest in government securities. The average maturity of the securities in the scheme is over three years.

□ **Short-Term Gilt Schemes**

These schemes invest in government securities. The securities invested in are of short to medium term maturities.

□ **Floating Rate Funds**

They invest in debt securities with floating interest rates, which are generally linked to some benchmark rate like MIBOR. Floating rate funds have a high relevance when interest rates are on the rise helping investors to ride the interest rate rise.

□ **Monthly Income Plans (MIPS)**

These are basically debt schemes, which make marginal investments in the range of 10-25% in equity to boost the scheme's returns. MIP schemes are ideal for investors who seek slightly higher return than pure long-term debt schemes at marginally higher risk.

**DIFFERENT MODES OF RECEIVING THE INCOME EARNED FROM MUTUAL FUND INVESTMENTS**

Mutual funds offer three methods of receiving income:

**Growth Plan**

In this plan, dividend is neither declared nor paid out to the investor but is built into the value of the NAV. In other words, the NAV increases over time due to such incomes and the investor realizes only the capital appreciation on redemption of his investment.

**Income Plan**

In this plan, dividends are paid-out to the investor. In other words, the NAV only reflects the capital appreciation or depreciation in market price of the underlying portfolio.

**Dividend Re-investment Plan**

In this case, dividend is declared but not paid out to the investor, instead, it is reinvested back into the scheme at the then prevailing NAV. In other words, the investor is given additional unit and not cash as dividend.

**MUTUAL FUND INVESTING STRATEGIES****1. Systematic Investment Plans (SIPs)**

These are best suited for young people who have started their careers and need to build their wealth. SIPs entail an investor to invest a fixed sum of money at regular intervals in the mutual fund scheme the investor has chosen, an investor opting for SIP in xyz mutual fund scheme will need to invest a certain sum of money every month/quarter/half-year in the scheme.

**2. Systematic Withdrawal Plans (SWPs)**

These plans are best suited for people nearing retirement. In these plans, an investor invests in a mutual fund scheme and is allowed to withdraw a fixed sum of money at regular intervals to take care of his expenses

### **3. Systematic Transfer Plans (STPs)**

They allow the investor to transfer on a periodic basis a specified amount from one scheme to another within the same fund family – meaning two schemes belonging to the same mutual fund. A transfer will be treated as redemption of unit from the scheme from which the transfer is made. Such redemption or investment will be at the applicable NAV. This service allows the investor to manage his investments actively to achieve his objectives. Many funds do not even charge any transaction fees for this service – an added advantage for the active investor.

## CHAPTER 2

### LITERATURE REVIEW

## LITERATURE REVIEW

Fund is different from the normal balance sheet of a bank or a company. All of the fund's assets belong to the investors and are held in the fiduciary capacity for them. Mutual fund employees need to be aware of the special requirements concerning accounting for the fund's assets, liabilities and transactions with investors and the outsiders like banks, securities custodians and registrars. This knowledge will help them better understand their responsibilities and their place in the organization, by getting an overview of the functioning of the fund.

Even the mutual fund agents need to understand the accounting for the fund's transaction with investors and how the fund accounts for its assets and liabilities, as the knowledge is essential for them to perform their basic role in explaining the mutual fund performance to the investor. For example, unless the agent knows how the NAV is computed, he cannot use even simple measures such as NAV change to assess the fund performance. He also should understand the impact of dividends paid out by the fund or entry/exit loads paid by the investor on the calculation of the NAV and therefore the fund performance.

The mutual funds in India are required to follow the accounting policies as laid down by the SEBI (Mutual Fund) Regulations 1996 and the amendments in 1998. Company form. In which investors hold shares of the mutual fund. In this structure management of the fund in the hands of an elected board, this in turn appoints investment managers to manage the fund. Trust form, in which the

investors are held by the trust, on behalf of the investors. The appoints investment managers monitors their functioning in the interest of the investors.

The company form of organization is very popular in the United States. In India mutual funds are organized as trusts. The trust is created by the sponsors who is actually the entity interested in creating the mutual fund business. The trust is either managed by a Board of trustees or by a trustee company, formed for this purpose. The investors' funds are held by the trust.

Though the trust is the mutual fund, the AMC is its operational face. The AMC is the first functionary to be appointed, and is involved in the appointment of all the other functionaries. The AMC structures the mutual fund products, markets them and mobilizes the funds and services the investors. It seeks the services of the functionaries in carrying

### **Net Asset Value (NAV)**

Net Asset Value is the market value of the assets of the scheme minus its liabilities. The per unit NAV is the net asset value of the scheme divided by the number of units outstanding on the Valuation Date.

### **Sale Price**

It is the price you pay when you invest in a scheme. It is also called Offer Price. It may include a sales load.

### **Repurchase Price**

It is the price at which a close-ended scheme repurchases its units and it may include a back – end load. This is also known as Bid price.



**Redemption Price**

It is the price at which open- ended schemes repurchase their units and close – ended schemes redeem their units on maturity. Their prices are NAV related.

**Sales Load**

It is a charge collected by a scheme when it sells the units. It is also known as Front End Load. Schemes that do not charge a load are called No Load schemes.

**Repurchase or Back – End Load**

It is a charge collected by a scheme when it buys back the units from the unit – holders.

**USES OF MUTUAL FUNDS**

1. We Add Value Through Active Management.
2. Mutual funds give us access to a variety of the world’s best managers.
3. Mutual funds allow us to achieve better diversification for our clients.
4. Mutual funds allow us access to great managers at reasonable minimums.
5. Mutual funds are highly liquid and can be traded quickly and efficiently
6. Mutual funds make excellent managers available at a reasonable cost.
7. Mutual funds provide the opportunity for solid investment performance.
8. The quantity and quality of analytical material on mutual funds is excellent.

## **INTERNATIONAL HISTORY OF MUTUAL FUNDS**

When three Boston securities executives pooled their money together in 1924 to create the first mutual fund, they had no idea how popular mutual funds would become. The idea of pooling money together for investing purposes started in Europe in the mid 1880s. The first pooled fund in the U.S. was created in 1893 for the faculty and staff of Harvard University. On March 21<sup>st</sup>, 1924 the first official mutual fund was born. It was called Massachusetts Investors Trust.

After one year, the Massachusetts Investors Trust grew \$50,000 in assets in 1924 to \$392,000 in assets (with around 200 shareholders). In contrast, there are over 10,000 mutual funds in the U.S. today totaling around \$7 trillion (with approximately 83 million individual investors) according to the Investment Company Institute.

The stock market crash of 1929 slowed the growth of mutual funds. In response to the stock market crash, Congress passed the Securities Act of 1933 and the Securities Exchange Act of 1934. These laws require that a fund be registered with the SEC and provide prospective investors with a prospectus. The SEC (U.S. Securities and Exchange Commission) helped create the Investment Company Act of 1940 which provides the guidelines that all funds must comply with today.

With renewed confidence in the stock market, mutual funds began to blossom. By the end of the 1960s there were around 270 funds with \$48 billion in assets.

In 1976, John C. Bogle opened the first retail index fund called the "First Index Investment Trust". It is now called the Vanguard 500 Index Fund and in November 2000 it became the largest mutual fund. Growth was Individual Retirement Account (IRA) provisions made in 1981, allowing individuals (including those already in corporate

pension plans ) to contribute \$2,000 a year. Mutual funds are now popular known for ease of use, liquidity and unique diversification capabilities.

### **History of the Indian Mutual Fund Industry**

The mutual fund industry in India started in 1963 with the formation of Unit Trust of India, at the initiative of the government of India and Reserve Bank. The history of mutual funds in India can be broadly divided into four distinct phases:

#### **First Phase: - 1964 – 1987**

Unit Trust of India (UTI) was established in 1963 by an Act of Parliament. It was set up by the Reserve Bank of India and functioned under the regulatory and administrative control of the Reserve Bank of India. In 1978 UTI was de-linked from the RBI and the Industrial Development Bank of India (IDBI) took over the regulatory and administrative control in place of RBI. The first scheme launched by UTI was Unit Scheme 1964. At the end of 1988 UTI had Rs.6700 crores of assets under management.

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

1987 marked the entry of non-UTI, public sector mutual funds set by public sector banks and life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC). SBI Mutual funds was the first non-UTI Mutual fund established in June 1987 followed by Can bank Mutual Fund ( Dec 87 ) , Punjab National Bank Mutual Fund ( Aug 89 ), Indian Bank Mutual Fund ( Nov 89 , Bank Of India ( Jun90), Bank Of Baroda Mutual Fund (Oct92), LIC established its Mutual Fund in June 1989 while GIC had set up its mutual fund in December 1990. At the end of 1993, the mutual fund industry had assets under management of Rs. 47,004 crores.

#### **Third Phase – 1993-2003 (Entry of Private Sector Funds)**

With the entry of private sector funds in 1993, a new era started in the Indian mutual fund industry, giving the Indian investors a wider choice of fund families. Also, 1993 was the year in which the first Mutual Fund Regulations came into being, under which all mutual funds, except UTI were to be registered and governed. The erstwhile Kothari Pioneer (now merged with Franklin Templeton) was the private sector mutual fund registered in July 1993.

The 1993 SEBI (Mutual Fund) Regulations were substituted by a more comprehensive and revised Mutual Fund Regulations in 1996. The Industry now functions under the SEBI (Mutual Fund) Regulation 1996.

The number of mutual fund houses went on increasing, with many foreign mutual Funds setting up funds in India and also the industry have witnessed several mergers and acquisitions. As at the end of January 2003, there were 33 mutual funds with total assets of Rs.1, 21,805 cores. The Unit Trust of India with Rs .44, 541 cores of assets under management were way ahead of other mutual funds.

#### **Fourth Phase – since February 2003**

In February 2003, following the repeal of the Unit Trust of India Act 1963 UTI was bifurcated into two separate entities. One is the specified Undertaking of the Unit Trust of India with assets under management of Rs 29,835 cores as at the end of January 2003, representing broadly, the assets of US 64 scheme, assured return and certain other Schemes. The specified Undertaking of Unit Trust of India, functioning under administrators and under the rules framed by Government of India and does not come under the purview of the Mutual Fund Regulations.

The second is the UTI Mutual Fund Ltd, sponsored by SBI, BOB, and LIC. It is registered with SEBI and functions under the Mutual Fund Regulations. With the bifurcation of the erstwhile UTI which had in March 2000 more than Rs.76, 000 cores

Of assets under management and with the setting up of a UTI Mutual Fund, conforming to the SEBI Mutual Fund Regulations, and with recent mergers taking place among different private sector funds, the mutual fund industry has entered its current phase of consolidation and growth. As per the numbers released by the Association of Mutual Funds in India (AMFI), AUM as at the end of March stood at Rs 2, 95,286 cores as against AUM of Rs 3, 52,686 cores as at the end of February.

### **REGULATORY STRUCTURE OF MUTUAL FUNDS IN INDIA**

The structure of mutual fund in India is governed by the SEBI Regulations, 1996. These regulations make it mandatory for mutual funds to have a three-tier structure SPONSER

–TRUSTEE-ASSET MANAGEMENT COMPANY (AMC). The sponsor is the promoters of the mutual fund and appoints the AMC for managing the investment portfolio. The AMC is the business face of the mutual fund. As its manages all the affairs of the mutual fund. The mutual fund and the AMC have to be registered with SEBI.

### **Mutual Funds can be structured in the following ways:**

Company form. In which investors hold shares of the mutual fund. In this structure management of the fund in the hands of an elected board, this in turn appoints investment managers to manage the fund. Trust form, in which the investors are held by the trust, on behalf of the investors. The appoints investment managers monitors their functioning in the interest of the investors.

The company form of organization is very popular in the United States. In India mutual funds are organized as trusts. The trust is created by the sponsors who is actually the entity interested in creating the mutual fund business. The trust is either managed by a Board of trustees or by a trustee company, formed for this purpose. The investors' funds are held by the trust.

Though the trust is the mutual fund, the AMC is its operational face. The AMC is the first functionary to be appointed, and is involved in the appointment of all the other functionaries. The AMC structures the mutual fund products, markets them and mobilizes the funds and services the investors. It seeks the services of the functionaries in carrying Out these functions. All the functionaries are required to the trustees, who lay down the ground rules and monitor them, working.

## **REGULATORY FRAMEWORK**

### **Regulatory jurisdiction of SEBI:**

SEBI is the apex regulatory of capital markets. SEBI has enacted the SEBI (mutual fund) Regulations, 1996, which provides the scope of the regulation of the mutual fund in India. All Mutual funds are required to be mandatory registered with SEBI. The structure and formation of mutual funds, appointment of key functionaries, operation of the mutual funds, accounting and disclosure norms, rights and obligations of functionaries and investors, investment restrictions ,compliance and penalties are all defined under the SEBI regulations. Mutual funds have to send half yearly compliance reports to SEBI, and provide all information about their operations.

### **Regulatory jurisdiction of RBI:**

RBI is the monetary authority of the country and is also the regulatory of the banking system. Earlier bank sponsored mutual funds were under the dual regulatory control of RBI and SEBI. These provisions are no longer in vogue. SEBI is the regulator of all mutual funds. The present position is that the RBI is involved with the mutual fund industry, only to the limited extent of being the regulator of the sponsors of bank sponsored mutual funds.

**Role of Ministry of Finance in Mutual Fund:**

The Finance Ministry is the supervisor of both the RBI and SEBI. The Ministry Of Finance is also the appellate authority under SEBI Regulations. Aggrieved parties can make appeals to the Ministry of Finance on the SEBI rulings relating to the mutual fund

**Role of Companies Act in Mutual Fund:**

The AMC and the Trustee Company may be structured as limited companies, which may come under the regulatory purview of the Company Law Board (CLB).The provisions of the Companies Act, 1956 is applicable to these company forms of organizations. The Company Law Board is the apex regulatory authority for companies. Any grievance against the AMC or the trustee company can be addressed to the Company Law Board for redresses.

**Role of Stock Exchanges:**

If a mutual fund is listed its schemes on stock exchanges, such listings are subject to the listing regulation of stock exchanges. Mutual funds have to sign the listing agreement and abide by its provisions, which primarily deal with periodic notifications and disclosure of information that may impact the trading of listed units.

## **LEGAL STRUCTURE**

Mutual funds have a unique structure not shared with other entities such as companies or the firms. It is important for employees and agents to be aware of the special nature of this structure, because it determines the rights and the responsibilities of the fund's constituents viz. sponsor, trustees, custodian, transfer agents and of course the fund and the AMC. The legal structure also drives the inter relationship between these constituents.

Like other countries, India has a legal framework within which mutual funds must be constituted along one unique structure as unit trust. A mutual fund in India is allowed to issue open ended and a close ended under a common legal structure. Therefore, a mutual fund may have a several different scheme under it at any point of time.

### **The Fund Sponsor**

"Sponsor" is defined by the SEBI regulations as any person who acting alone or in combination with another body corporate establishes a mutual fund. The sponsor of a fund is akin to the promoter of the company as he gets the fund registered with the SEBI.

The sponsor will form a trust and appoint the Board of Trustees. The sponsor will also generally appoint the AMC as the fund managers. The sponsor, either directly or acting through the trustees will also appoint a Custodian to hold the fund assets. All these appointments are made in accordance with the guidelines of the SEBI.

As per the existing SEBI regulations, for a person to qualify as the sponsor, he must contribute at least 40% of the net

## **CHAPTER 3 OBJECTIVE OF THE STUDY**



## OBJECTIVE OF THE STUDY

My main and important objective of that study is I am more interested in mutual funds investments. I give more safety to its investors. Here are many more objectives of my study given as under-

1. To know the investors behavior.
2. To know about the literacy on mutual fund in India.
3. Interest of the investors.
4. Different occupation investor's knowledge.
5. Purpose of the investors for investing in the mutual funds.
6. To know the investment duration of investment in Mutual Funds etc

## CHAPTER 4 RESEARCH METHODOLOGY

## RESEARCH METHODOLOGY

### **DATA COLLECTION PROCEDURE**

#### **Sampling Method**

Universe: banks and brokers in North Delhi

#### **Sampling unit**

General public and the financial analyst in Banks and Brokerage Firms.

#### **Sample Size**

40

#### **Basis of sampling**

Convenient sampling and judgmental sampling



#### **Methodology:**



Primary Data: - Personal interaction with the respondents.



Secondary Data: - Information through websites, books, fact sheets of various fund houses etc.

## CHAPTER 5

### HISTORY, TYPES, USE AND

### REGULATORY

### FRAMEWORK

#### Mutual Funds as Trusts

A mutual fund is constituted in the form of a Public Trust created under the Indian Trusts Act, 1882. The fund sponsor acts as the settler of the trust, contributing to its initial capital and appoints a Trustee to hold the assets of the Trust for the benefit of the unit holders, who are the beneficiaries of the trust. The fund then invites investors to contribute their money in the common pool, by subscribing to “units” issued by various schemes established by the trust, units being the evidence of their beneficial interest in the fund.

#### Trustees

The trust – the mutual fund may be managed by a board of Trustees- a body of the individuals, or a trust company- a corporate body. Most of the funds in India are managed by the Board of Trustees. While the Board is governed by the provisions of the Indian Trust act, where the Trustee is a corporate body, it would also be required to comply the provisions of the Companies Act, 1956, the Board as an independent body, act as the protector of the interest of the unit holders. The Trustees do not directly manage the portfolio of the securities. For this specialist function, they appoint AMC. They ensure that the fund is managed by the AMC as per the defined objective and in accordance with the trust deed and the regulations of the SEBI.

The trust is created through a document called the Trust Deed that is executed by the fund sponsor in the favor of the trustees. The Trust Deed is required to be stamped as registered under the provisions of the Indian Registration Act and registered with SEBI. Clauses in the Trust Deed, inter alias, deal with the establishment of the Trust, the appointment of the trustees, their powers and duties and the obligations of the trustees Towards the unit holders and the AMC. These clauses also specify activities that the fund

/ AMC cannot undertake. The third schedule of the SEBI (MF) Regulations, 1996 specifies the contents of the Trust Deed.

## **CLASSIFICATION OF MUTUAL FUND SCHEMES**

Any mutual fund has an objective of earning objective income for the investors and / or getting increased value of their investments. To achieve these objectives mutual funds adopt different strategies and accordingly offer different schemes of investments. On these bases the simplest way to categorize schemes would be to group these into two broad classifications:

- Operational Classification
- Portfolio Classification.

Operational Classification highlights the two main types of schemes, i.e. open ended and close ended which are offered by the mutual funds.

Portfolio classification projects the combination of investment instruments and investment avenues available to mutual funds to manage their funds. Any portfolio scheme can be either open ended or close ended.

### **Operational Classification**

(A) **Open ended schemes:** As the name implies the size of the scheme (fund) is open i.e. Not specified or pre determined. Entry to the fund is always open to the investor who can subscribe at any time. Such fund stands ready to buy or sell its securities at any time. It implies that the capitalization of the fund is constantly changing as investors sell or buy their shares. Further the shares or units are normally not traded on the stock exchange but are repurchased by the fund at announced rates. Open ended schemes have comparatively better liquidity despite the fact that these are not listed. The reason is that investor can at any time approach mutual funds for sale of such units. No intermediaries are required. Moreover; the realizable amount is certain since repurchase is at a price based on declared net asset value (NAV). No minute to minute fluctuations in rate haunts the investors. The portfolio mix of such schemes has to be investments, which are actively traded in the market. Otherwise, it will not be possible to calculate NAV. This is the reason that generally open – ended schemes are equity based. Moreover , desiring frequently traded securities, open –ended schemes are hardly have in their portfolio shares of comparatively new and smaller companies since these are not generally not traded. In such funds, option to reinvest its dividend is also available. Since there is always a possibility of withdrawals, the management

of such funds becomes more tedious as managers have to work from crisis to crisis. Crisis may be on two fronts; one is that unexpected withdrawals require funds to maintain a high level of cash available every time implying thereby idle cash. Fund managers have to face question like “what to sell”. He could very well have to sell his most liquid assets. Second, by virtue of this situation such funds may fail to grab favorable opportunities. Further to match quick cash payments, funds cannot have matching realization from their portfolio due to intricacies of the stock market. Thus, success of the open ended schemes to a great extent depends on the efficiency of the capital market.

**(B) Close ended schemes:**

Such schemes have a definite period after which their shares/ units are redeemed. Unlike open ended, these funds have fixed capitalization, i.e. corpus normally does not change throughout its life period. Close ended funds units’ trade among the investors in the secondary market since these are to be quoted on the stock exchanges. Their price is determined on the basis of demand and supply in the market. Their liquidity depends on the efficiency and understanding of the engaged brokers. Their price is free to deviate NAV, i.e., there is very possibility that the market price may be above or below its NAV. If one takes into account the issue expenses, conceptually close ended funds units cannot be trade at a premium or over NAV because of a package of investments, i.e., cannot exceed the sum of the prices of the investments constituting the package. Whatever premium exists that may exist only on account of speculative activities. In India as per SEBI (MF) Regulations every mutual fund is free to launch any or both types of schemes.

**Portfolio Classification of Funds:**

Following are the portfolio classification of funds, which may be offered. This classification may be on the basis of (a) Return (b) Investment Pattern (c) Specialized sector of investment

(d) Leverage (e) Others

**Return Based Classification**

To meet the diversified needs of the investors, the mutual fund schemes are made to enjoy a good return. Returns expected are in form of regular dividends or capital appreciation or a combination of these two.

**Income Funds:** For investors who are more curious for returns, income funds are floated. Their objective is to maximize current income. Such funds distribute periodically the income earned by them. These funds can further be spitted up into categories: those that stress constant income at relatively low risk and those that attempt to achieve maximum income possible, even with the use of leverage. Obviously, the higher the expected returns, the higher the potential risk of the investment.

**Growth Funds:** Such funds aim to achieve increase in the value of the underlying investments through capital appreciation. Such funds invest in growth oriented securities which can appreciate through the expansion production facilities in long run. An investor who selects such funds should be able to assume a higher than normal degree of risk.

**Conservative Funds:** The fund with a philosophy of “all things to all” issue offer document announcing objectives as (I) To provide a reasonable rate of return, (ii) To protect the value of investment (iii) To achieve capital appreciation consistent with the fulfillment of the first two objectives. Such funds which offer a blend of immediate average return and reasonable capital appreciation are known as “middle of the road “funds. Such funds divide their portfolio in common stocks and bonds in a way to achieve the desired objectives. Such funds have been most popular and appeal to the investors who want both growth and income.

## **B) Investment Based Classification:**

Mutual funds may also be classified on the basis of securities in which they invest. Basically, it is renaming the subcategories of return based classification.

**Equity Fund:** Such funds, as the name implies, invest most of their investible shares in equity shares of companies and undertake the risk associated with the investment in equity shares. Such funds are clearly expected to outdo other funds in rising market, because these have almost all their capital in equity. Equity funds again can be of different categories varying from those that invest exclusively in high quality ‘blue chip’ companies to those that invest solely in the new, un established companies. The strength

of these funds is the expected capital appreciation. Naturally they have a higher degree of risk.

**Bond Funds:** Such funds have their portfolio consisted of bonds, debentures, etc. this type of fund is expected to be very secure with a steady income and little or no chance of capital appreciation. Obviously risk is low in such funds. In this category we may come across the funds called 'Liquid Funds' which specialize in investing short term money market instruments. The emphasis is on liquidity and is associated with lower risks and low returns

### **TYPES OF MUTUAL FUNDS**

All mutual fund would be either close ended or open ended or either load or no load. These classifications are general. For example all open – end funds operate the same way; or in case of a load a deduction is made from investor's subscription or redemption and only the net amount used to determine his number of shares purchased or sold.

Funds are generally distinguished from each other by their investment objectives and types of securities they invest in. The major types of funds available:-



#### **Money Market Funds**

Often considered to be at the lowest ring in the order of risk level. Money Market Funds invest in securities of short term nature which generally means securities of less than one year maturity. The typical short term interest bearing instruments these funds invest in Treasury Bills issued by governments, Certificate of Deposits issued by banks and Commercial Paper issued by companies. The major strengths of money market funds are the liquidity and safety of principal that the investors can normally expect from short term investments.



#### **Gilt Funds**

Gilts are the governments' securities with medium to long term maturities typically of over one year (under one year instruments being money market securities). In India, we



have now seen the emergence of government securities or gilt funds that invest in government paper called dated securities. Since the issuer is the government, these funds have little risk of default and hence offer better protection of principal. However, investors have to recognize the potential changes in values of debt securities held by the funds that are caused by changes

In the market price of debt securities held by the funds that are caused by changes in the market price of debt securities quoted on the stock exchanges.

□ **Debt Funds (Income Funds)**

These funds invest in debt instruments issued not only by the governments, but also by private companies, banks and financial institutions and other entities such as infrastructure companies. By investing in debt these funds target low risk and stable income for the investor as their key objectives.

Debt funds are largely considered as income funds as they do not target capital appreciation, look for high current income and therefore distribute a substantial part of their surplus to investors. The income funds fall largely in the category of debt funds as they invest primarily in fixed income generating debt instruments

□ **Equity Fund**

As investors move from debt funds category to equity funds, they face increased risk level. However there are a large variety of equity funds and all of them is not equally risk prone. Investor and their advisors need to sort out and select the right equity fund that risk appetite.

Equity funds invest a major portion of their corpus in equity shares issued by the companies, acquired directly in initial public offerings or through the secondary

Market. Equity funds would be exposed to the equity price fluctuations risk at the market level, at the industry or the sector level and the company specific level. Equity Funds NAV fluctuates with all these price movement. These price movements are caused by all kinds of external factors, political and social as well economic. The issuers of equity shares offer no guaranteed repayments in case of debt instruments. Hence, equity funds

are generally considered at the higher end of the risk spectrum among all funds available in the market. On the other hand, unlike debt instruments that offer fixed amounts of repayments, equities can appreciate in value in line with the issuers' earning potential and so offer the greatest potential for growth in capital.

Equity funds adopt different investment strategies resulting in different levels of risk. Hence they are generally separated into different types in terms of their investment styles. Some of these equity funds are as under:



#### **Equity Income Funds**

Usually income funds are in the debt funds category, as they target fixed income investments. However there are equity funds that can be designed to give the investors a high level of current income along with some steady capital appreciation, investing mainly in shares of companies with high dividend yields.

As an example an equity income fund would invest largely in power/ utility companies'

shares of established companies that pay higher dividend and whose

Price does not fluctuate as much as the other shares. These equity funds should therefore be less volatile and less risky than nearly all other equity funds.



#### **Hybrid Funds**

We have seen that in terms of the nature of financial securities held, there are three major mutual fund types: money market, debt and equity. Many mutual funds mix these different types of securities in their portfolios. Thus, most funds equity or debt always have some money market securities in their portfolios as these securities offer the much needed liquidity. However money market holdings will constitute a lower proportion in the overall portfolios. These are the funds that seek to hold a relatively balanced holding of debt or equity in their portfolios. Such funds are termed as "hybrid funds" as they have a dual equity/ bond focus.



### **Balanced Funds**

A balanced fund is the one that has a portfolio comprising debt instruments, convertible securities, and preference and equity shares. Their assets are generally held in more or less equal proportion between debt / money market securities and equities. By investing in a mix of this nature, balanced funds seek to attain the objectives of the income, moderate capital appreciation and preservation of capital and are ideal for investors with a conservative and long term orientation.



### **Growth and Income Funds**

Unlike income or growth focused funds, these funds seek to strike a balance between capital appreciation and income for the investor. Their portfolios are a mix between companies with good dividends paying records and those with Potential for capital appreciation. These funds would be less risky than the pure growth funds though more risky than the income funds.

## **INVESTMENT PLANS**

The term investment plans generally refers to the services that the funds provide to investors offering different ways to invest or invest. The different investment plans are important considerations in the investment decisions because they determine the level of flexibility available to the investors. Alternate investment plans offered by the fund allow the investor freedom with respect to investing at one time or at regular intervals, making transfers to different schemes within the same fund family or receiving income at specified intervals or accumulating distributions. Some of the investment plans offered are as follows:-

### **Automatic Reinvestment Plans (ARP)**

In India, many funds offer two options under the same scheme the dividend option and the growth option. The dividend option or the Automatic Reinvestment Plans (ARP) allows the investor to reinvest in additional units the amount of dividends or other distribution made by the fund, instead of receiving them in cash. Reinvestment takes

place at the ex-dividend NAV. The ARP ensures that the investors reap the benefit of compounding in his investments. Some funds allow reinvestments into other schemes in the fund family.

### **Automatic Investment Plans (AIP)**

These require the investor to invest a fixed sum periodically, thereby letting the investor save in a disciplined and phased manner. The mode of investment could be through debit to the investor's salary or bank account. Such plans are also known as the Systematic Investment Plans. But mutual funds do not offer this facility on all the schemes. Typically they restrict it to their plain vanilla schemes like diversified equity funds,

Income funds and balanced funds. SIP works best in equity funds. It enforces saving discipline and helps you profit from market volatility- you buy more units when the market is down and fewer when the market is up.

### **Systematic Withdrawal Plan (SWP)**

Such plan allow the investor to make systematic withdrawal from his fund investment account on a periodic basis, thereby providing the same benefit as regular income. The investor must withdraw a specific minimum amount with the facility to have withdrawal amounts sent to his residence by cheque or credited directly into his bank account. The amount withdrawn is treated as redemption of units at the applicable NAV as specified in the offer document. For example, the withdrawal could be at NAV on the first day of the month of payment. The investor is usually required to maintain a minimum balance in his bank account under this plan. Agents and the investors should understand that the SWP's are different from the Monthly Income Plans, as the former allow investors to get back the principal amount invested while the latter only pay the income part on a regular basis.

### **Systematic Transfer Plans (STP)**

These plans allow the customer to transfer on a periodic basis a specified amount from one scheme to the another within the same fund family- meaning two schemes by the same AMC and belonging to the same fund. A transfer will be treated as the redemption

of the units from the scheme from which the transfer is made, and as investments in units of the scheme into which the transfer is made. Such redemption or investment will be at the applicable NAV for the respective schemes as specified in the offer document. It is necessary for the investor to maintain a minimum balance in the scheme from which the transfer is made. Both UTI and other private funds now generally offer these services to the investor in India. The service allows the investor to maintain his investment actively To achieve his objectives. Many funds do not even charge any transaction fees for this service.

### **The Importance of Accounting Knowledge**

The balance sheet of a mutual fund is different from the normal balance sheet of a bank or a company. All of the fund's assets belong to the investors and are held in the fiduciary capacity for them. Mutual fund employees need to be aware of the special requirements concerning accounting for the fund's assets, liabilities and transactions with investors and the outsiders like banks, securities custodians and registrars. This knowledge will help them better understand their responsibilities and their place in the organization, by getting an overview of the functioning of the fund.

Even the mutual fund agents need to understand the accounting for the fund's transaction with investors and how the fund accounts for its assets and liabilities, as the knowledge is essential for them to perform their basic role in explaining the mutual fund performance to the investor. For example, unless the agent knows how the NAV is computed, he cannot use even simple measures such as NAV change to assess the fund performance. He also should understand the impact of dividends paid out by the fund or entry/exit loads paid by the investor on the calculation of the NAV and therefore the fund performance.

The mutual funds in India are required to follow the accounting policies as laid down by the SEBI (Mutual Fund) Regulations 1996 and the amendments in 1998.

### **NET ASSET VALUE (NAV)**

A mutual fund is a common investment vehicle where the assets of the fund belong directly to the investors. Investors' subscription is accounted for by the fund not as the liabilities or deposits but as the Unit Capital. On the other hand, the investments made on the behalf of the investors are reflected on the assets side and are the main constituents of the balance sheet, there are, however, liabilities of a strictly short-term nature that may be the part of the balance sheet. The fund's Net Assets are therefore defined as the assets minus the liabilities. As there are many investors in the fund. It is common practice for the mutual funds to compute the share of each of the investor on the basis of the value of the Net Assets per Share/Unit, commonly known as the Net Assets Value (NAV).

The following are the regulatory requirements and accounting definitions as laid down by the SEBI.

$NAV = \text{Net Assets of the Scheme} / \text{Number of the Units Outstanding}$ , i.e.

$\text{Market value of the investments} + \text{Receivables} + \text{Other Accrued Income}$

$+ \text{Other Assets} - \text{Accrued Expenses} - \text{Other Payables} - \text{Other Liabilities}$  No. of units outstanding as at the NAV date.

For the purpose of the NAV calculation, the day on which NAV is calculated by a fund is known as the valuation date.

NAV of all schemes must be calculated and published at least weekly for closed end schemes and daily for open end schemes. NAV's for a day must also be posted on AMFI website by 8 P.M. on that day.

A fund's NAV is affected by four sets of factors

- ◆ Purchase and sale of investment securities
- ◆ Valuation of all investment securities held
- ◆ Other assets and liabilities and,

◆ Units sold or redeemed

## **TAXATION**

Investors often view the tax angle as an important consideration while deciding on the appropriate investments. This section examines the area of mutual fund taxation with respect to the taxation of income (dividends and capital gains) in the hands of the fund itself and the income when received in the hands when received in the hands investors.

### **Taxation in the hands of the funds**

When we talk about a mutual fund for taxation purpose, we mean the legally constituted trust that holds the investors' money. It is this trust that earns and receives income from the investments it makes on the behalf of the investors. Most countries do not impose any tax on this entity- the trust- because this income that it earns is meant for the investors. The trust is considered to be only a pass through entry. It would amount to double taxation if the trust first pays the tax and then the investor is also required to pay the tax. Generally, the trust is exempted from the tax and it the investor who pays tax on his share of income. After the 1999 /2000 budget of finance minister Mr. Yashwant Sinhal, the investors are totally exempted from paying any tax on the dividend income they receive from the mutual funds, while certain types of schemes pay some taxes. This section deals with what the fund or the trust pays by the way of tax.

### **Tax provisions**

◆ Generally, income earned by any mutual fund registered with SEBI is exempt from tax.

◆ However, income distributed to unit- holders by a closed- end or debt fund is liable to a dividend distribution tax of 10% plus a surcharge of 2%, i.e., a tax of 10.2%. This tax is also applicable to

distributions made by open- end equity funds ( i. e., funds with more than 50% of their portfolio in equity) on or after April 1, 2002.

### **The impact on the Fund and the Investor**

◆ It should be noted that although this tax is payable by the fund on its distributions and out of its income, the investors pay indirectly since the fund's NAV, and therefore the value of his investment will come down by the amount of tax paid by the fund. For example, if a closed end fund declares a dividend distribution of Rs. 100, Rs. 10. 20 ( 10. 20%) will be the tax in the hands of the funds. While the investor will get Rs. 100, the fund will have Rs. 10. 20 less to invest. The fund's current cash flow will diminish by Rs. 10. 20 paid as a tax, and its impact will be reflected in the lower value of the fund's NAV and hence investor's investment on a compounded basis in future periods.

◆ Also, the tax bears no relationship to the investor's tax bracket and is payable by the fund even if the investor's income does not exceed the taxable limit prescribed by the Income Tax Act

In fact, since the tax is on distributions, it makes income schemes less attractive in comparison to the growth schemes, because the objective of the income schemes is to pay regular dividends.

◆ The fund cannot avoid the tax even if the investor chooses to reinvest the distribution back into his fund. For example, the fund will still pay Rs. 10. 20 tax on the announced distribution, even if the investor chooses to reinvest his dividends in the concerned schemes.

### **Taxation in the hands of the investor**

#### **Tax rebate available to individual investor on subscriptions to Mutual Funds**

In accordance with the section 88 of the Income Tax Act,

Investments up to Rs.10, 000 in an ELSS qualifies for tax rebate of 20%.



In case of “infrastructure” mutual fund units, investments up to Rs.80,000 is eligible for 20% tax rebate.

However, total investment eligible for tax rebate under section 88 is not allowed to exceed Rs. 60,000 (Rs.80,000 in case of investment qualifying under ‘infrastructure’).

### **Dividends received from Mutual Funds**

From the accounting year 1999/2000, income distributed by a fund is exempt in the hands of the investors.

### **Capital gains on sale of Units**

However, if the investors sell his units and earn “Capital Gains”, the investor is subject to the Capital Gains Tax as under:

- ❖ If units are held for not more than 12 months, they will be treated as short term capital assets, otherwise as long term capital assets. (This period is 36 months for assets other than shares and listed securities).
- ❖ Tax law definition of capital gains = sale consideration - (Cost of Acquisition + Cost of improvements + cost of transfer)
- ❖ If the units were held for over one year, the investors get the benefit of “indexation”, which means his purchase price is marked up by an inflation index, so his capital gains amount is less than otherwise. Purchase price of a long term capital asset after indexation is computed as,  $\text{Cost of acquisition or improvement} = \text{actual cost of acquisition or improvement} \times \frac{\text{cost inflation index for year of transfer}}{\text{cost inflation index for year of acquisition or improvement or for 1981, whichever is later.}}$

### **Mutual Fund Performance The Investor Perspective**

The investor would actually be interested in tracking the value of his investments, whether he invests directly in the market or indirectly through the mutual funds. He would have to make intelligent decisions on whether he gets an acceptable return on his investments in the funds selected by him, or if he needs to switch to the fund. He therefore, needs to understand the basis of appropriate performance measurement for the funds, and acquire the basic knowledge of the different measures of evaluating the performance of a fund. Only then would he be in a position to judge correctly whether his fund is performing well or not.

### **The Advisor's Perspective**

If you are an intermediary recommending a mutual fund to a potential investor, he would expect you to give him proper advice on which funds have a good performance track record. If you want to be an effective investment advisor, then you too have to know how to measure and evaluate the performance of the different funds available to the investor. The need to compare the performance of the different funds requires the advisor to have the knowledge of the correct and appropriate measures of evaluating the fund performance.

### **Different Performance Measures**

Remember that there are many ways to evaluate the performance of the fund. One must find the most suitable measure, depending upon the type of the fund one is looking at, the stated investment objective of the fund and even depending on the current financial market condition. Let us discuss few common measures.



Change in NAV- The most common measure

**Purpose:** If an investor wants to compute the Return on Investment between two dates, he can simply use the Per Unit Net Assets Value at the beginning and the end periods and calculate the change in the value of the NAV between the two dates in absolute and percentage terms.

**Formula:** for NAV change in absolute terms:

$(\text{NAV at the end of the period}) - (\text{NAV at the beginning of the period})$

**For NAV change in percentage terms:**

$(\text{Absolute changes in NAV} / \text{NAV at the beginning}) * 100.$

If period covered is less /more than one year: for annualized NAVChange

$\{[(\text{absolute change in NAV} / \text{NAV at the beginning}) / \text{months covered}] * 12\} * 100$

**Suitability :** NAV change is most commonly used by the investors to evaluate fund performance, and so is also most commonly published by the mutual fund managers. The advantage of this measure is that it is easily understood and applies to virtually any type of fund.

**Interpretation :** Whether the return in terms of NAV growth is sufficient or not should be interpreted in light of the investment objective of the fund, current market conditions and alternative investment returns. Thus, a long term growth fund or infrastructure fund will give low returns in its initial years. All equity funds may give lower returns when the market is in bearish phase.

**Limitation:** However, this measure does not always give the

Correct picture, in case where the fund has distributed to the investors a significant amount of dividend in the interim period. If, in the above example, yearend NAV was Rs. 22 after declaration and payment of dividend of Re.1, the NAV change of 10% gives an incomplete picture.

Therefore, it is suitable for evaluating growth funds and accumulation plans of debt and equity fund, but should be avoided for income funds and funds with withdrawal plans.

**Purpose:** This measure corrects the shortcomings of the NAV Change measure, by taking into account of the dividends distributed by the fund between the two NAV dates, and adding them to the NAV change to arrive at the total return.

**Formula :**
$$[(\text{distributions} + \text{change in NAV}) / \text{NAV at the beginning of the period}] * 100$$

**Suitability :** total return is the measure suitable for all types of funds. Performance of different types of funds can be compared on the basis of Total Return. Thus, during a given period, one can find out whether a debt fund has given better returns than the equity fund. It is also more accurate than simple NAV change, because it takes into account distribution during the period. While using Total Return, performance must be interpreted in the light of market conditions and investment objectives of the fund.

**Limitation :** although more accurate than NAV change, simple Total Return as calculated here is still inadequate as a performance measure, because it ignores the fact that distributed dividends also get reinvested if received during the year. The investor's total return should take account of reinvestment of interim dividends.



### Return On Investment

**Purpose:** the short coming of the simple total return is overcome by the total return with reinvestment of the dividends in the funds it self at the NAV on the date of the distribution. The appropriate measure of the growth of an investor's mutual fund holdings is therefore, the return on investment.

**Formula:**  $\{(units\ held + dividend / (ex - dividend\ NAV) * end\ NAV\} - begin\ NAV / begin\ NAV * 100$

**Suitability:** Total return with distributions reinvested at NAV is a measure accepted by mutual fund tracking agencies such as Residence in Mumbai and Value Research in New Delhi. It is appropriate for measuring performance of accumulation plans, monthly/ quarterly income schemes that distribute interim dividends.



### The Income Ratio

**Formula:** a fund's income ratio is defined as its net investment income dividend by its net assets for this period.

**Purpose/Suitability:** this ratio is a useful measure for evaluating income-oriented fund, particularly debt funds. It is not recommended for funds that concentrate primarily on capital appreciation.

**Limitation:** the income ratio cannot be considered in isolation; it should be used only to supplement the analysis based on the expense ratio and total return.

### **Tracking Mutual Fund Performance**

Having identified appropriate measures and benchmarks for the mutual funds available in the market, the challenge is to track fund performance on a regular basis. This is indeed the key towards maximizing wealth through mutual fund investing. Proper tracking allows the investor to make informed and timely decisions regarding his fund portfolio –whether to acquire attractive funds, dispose of poor performers or switch between funds/plans.

To be able to track fund performance, the first step is to find the relevant information on NAV, expenses cash flow, appropriate indices and so on. The following are the sources of information in India:

◆ **Mutual Funds' Annual and Periodic Reports:** These include data on the fund's financial performance, so indicators such as income/ expense ratios and Total Return can be computed on the basis of this data. The annual report includes a listing of the fund's portfolios holdings at market value, statement of revenue and expenses, unrealized appreciation/depreciation at year- end, and changes in the net assets. On the basis of the annual report, the investors can develop a perspective on the quality of the fund's assets and portfolio concentration and risk profile, besides computing returns. He can also assess the quality of the fund management company by reviewing their entire scheme's performance. The profit and loss account part of the annual report will also give details of transaction costs such as brokerage paid, custodian/registrar fees and stamp duties.

◆ **Mutual Funds' Websites :** With the increasing spread of the internet as a medium, all mutual funds have their own websites. SEBI even requires funds to disclose certain types of the information on these sites- for example, the Portfolio Composition.

Similarly, AMFI itself has a websites, which displays all of its member's funds' NAV information.

◆ **Financial papers:** Daily newspapers such as the Economic Times provide daily NAV figures for the open end schemes and share prices of the closed end listed schemes. Besides, weekly supplements of the economic newspapers give more analytical information on the fund performance. For example, Business Standard- the Smart Investor gives total returns over 3 month, 1 year and 3 year periods, besides the fund size and rankings with the other funds separately for Equity, Balanced, Debt, Money Market, Short Term Debt and Tax Planning Funds. Similarly, Economic Times weekly supplement gives additional data on open end

Schemes such as Loads and Dividends besides the NAV and other Information and performance data on closed end scheme.

**Fund Tracking Agencies:** In India, agencies such as Credence and Value Research are a source of information for mutual fund performance data and evaluation. This data is available only on request and payment.

◆ **Newsletters:** Many stockbrokers, mutual fund agent and banks and non- ranking firms catering to retail investors publish their own newsletters, sometimes free or else for their subscribes, giving fund performance data and recommendations.

◆ **Prospectus:** SEBI Regulations for mutual fund require the fund sponsors to disclose performance data relating to scheme being managed by the concerned AMC, such as the beginning and end of the year.

## **Evaluating Fund Performance**

### **Importance of Benchmarking in Evaluating Fund Performance**

The measures mentioned above are obsolete, i.e., none of the measure should be used to evaluate the fund performance in isolation. A fund's performance can only be judged in relation to the investor's expectations. However, it is important for the investor to define his expectations in relation to the certain "guideposts" on what is possible to achieve, or moderate his expectations with realistic investments alternatives available to him in the financial market. These guideposts or the indicators of performance can be thought of as benchmarks against which a fund's performance ought to be judged. For example, an investor's expectations

Of returns from equity fund should be judged against how the overall stock market performed, in the other words by how much the stock market index itself moved up or down, and whether the fund gave a return that was better or worse than the index movement. In this example, we can use a market index like S&P CNX Nifty or BSE SENSEX as "benchmarks to evaluate the investor's mutual fund performance.

The advisor needs to select the right benchmark to evaluate a fund's performance, so that he can compare the measured performance figures against the selected benchmark. Historically, in India, investors' only options to evaluate the performance of the units were UTI schemes or the bank fixed deposit interest rates. UTI itself to tend to "benchmark" its returns against what interest rates were available on bank deposits of 3/5 year maturity. Thus, for a long period, US 64 scheme dividends were compared on bank interest rates and investors would be happy if the Dividend Yield on US 64 units was greater than comparable deposits interest rate. However, with increasing investment options in the market, bank interest rates should not be used to judge a mutual fund's



performance in all cases. Let us therefore look at how to choose the correct benchmarks of mutual fund performance.

### **Basis of choosing an Appropriate Performance Benchmark**

The appropriate benchmark for any fund as to be selected by reference to:

- i. The asset class it invests in. Thus, an equity fund has to be judged by an appropriate benchmark from the equity markets, a debt fund performance against a debt market bench mark and so on; and
- ii. The fund's stated investment objective. For example, if a fund invests in long term growth stocks, its performance ought to be

Evaluated against a benchmark that captures a growth stocks' performance.

There are in fact three types of benchmarks that can be used to evaluate a fund's performance relative to the market as whole, relative to other mutual funds, comparable financial products or investments options open to the investor.

### **Benchmarking relative to the market:**

#### **Equity Funds**

Index Funds- a Base Index: If an investor were to choose an Equity Fund, now being offered in India, he can expect to get the same return on his investments as the return on the equity index used by the fund as its benchmark, called the Base Index. The fund would invest in the index stocks, and expects NAV changes to mirror the changes in the index itself. The fund and therefore the investor would not expect to beat the benchmark, but merely earn the same return as the index.

**Tracking Error:** In order to obtain the same returns as the index, an index fund invests in all of the stocks included in the index calculation, in the same proportion as the stocks' weight age in the index. The tracking error arises from the practical difficulties faced by the fund manager in trying to always buy or sell stocks to remain in line with the weight age that the stock enjoys in the index.

**“Active” Equity Funds:** An index fund is passively managed, to track a given index. However, most of the other equity funds/ schemes are actively managed by the fund managers. If an investor holds such an actively managed equity fund, the fund manager would not specify in advance the benchmark to evaluate his expected performance as in case of

An index fund. However, the investor still needs to know whether the fund performance is good or bad. To evaluate the performance of the equity scheme, therefore, we still need to select an appropriate benchmark and compare its return to the returns on the benchmark; usually this means using the appropriate market index. The appropriate index to be used to evaluate a broad based equity fund should be decided on the basis of the size and the composition of the fund's portfolio. If the fund in question has a large portfolio, a broader market index like BSE 100 or 200 or NSE 100 may have to be used as the rather than S&P CNX NIFTY or BSE 30. An actively managed fund expects to be able to beat the index, in other words give higher returns than the index itself.

Somewhat like the Index Funds, the choice of benchmarks in case of Sector Funds is easier. Clearly, for example, an investor in Info Tech or Parma sector funds can only expect the same return as the relative sectoral indices. In such cases, he should expect the same or higher returns than the Info Tech or Parma sector index if such index exists. In other words, the choice of the correct equity index as a benchmark also depends upon the investment objective of the fund. The performance of a small cap fund has to be compared with the small cap index. A Growth Fund investing in new growth sectors but is diversified in many sectors can

only be judged against the appropriate growth index if available. If not, the returns can only be compared to either a broad based index or a combined set of sectoral indices.

### **Evaluating the Fund Manager /Asset Management Company**

While every fund is exposed to market risks, good funds should at least match major market indices, and be able to sustain bearish market phases better than other funds. Good funds manager operate long term perspective, do not sacrifice investor value by excessive trading which

Generates a high level of transaction costs, and will turn out more consistent performance, which is more valuable than one-time high and otherwise volatile performance record.

The investor must evaluate the fund manager's track record, how his schemes have performed over the years. There is a difference between institution-managed funds that have a team of managers with successful records as against funds that are managed by the individuals only. The team approach also helps by offsetting bad performance by one manager with good performance from the others in the team. In practice, however, single person managed funds are widely prevalent in the countries like the U. S. In India, many individuals operate as Portfolio Managers. However, currently, we have mainly institution sponsored funds, either bank - sponsored, corporate owned or government / financial institution -owned. The reliability and track record of these sponsors has been an important factor in investor perceptions.

In the final analysis, Asset Management Companies and their fund managers ought to be judged on consistency in the returns obtained, and performance record against competing or peer group managers running

similar funds. While transaction costs incurred are also an important factor, this information is not generally available in India

## **LIFE CYCLE AND WEALTH CYCLE STAGES**

### **Life cycle guide to financial planning**

Financial goals and plans depend to a large extent on the expenses and cash flow requirement of individuals. It is well known that the age of the investors is an important determinant of financial goals. Therefore financial planners have segmented investors according to certain stages in their life cycle as follows:

<b>LIFE CYCLE STAGE</b>	<b>FINANCIAL NEEDS</b>	<b>ABILITY TO INVEST</b>	<b>CHOICE OF INVESTMENT</b>
Childhood stage	Taken care of by parents	Investment of gifts	Long term
Young unmarried	Immediate and short term	Limited due to higher spending	Liquid plans and short term investment some exposure to equity and pension products
Young married stage	Short and intermediate term Housing and insurance needs Consumer finance needs	Limited due to higher spending Cash flow requirements are also limited	Medium to long – term investment Ability to take risks Fixed income insurance and equity products
Young married	Medium to long	Limited Financial	Medium to long-

with children	term children's education Holidays and consumer finance Housing	planning needs are highest at this stage is ideal for discipline spending and saving regularly	term investments Ability to take risks Portfolio of products for growth and long term
Married with older children	Medium term needs for children	Higher saving ratios recommended for intermittent for intermittent cash flows higher	Medium term investment with high liquidity needs Portfolio of products including equity debt ant pension plans
Retirement stage	Short to medium term	Lower saving ratios Higher requirement for regular cash flows	Medium term investment Preference for liquid and income generating products Low appetite for risky investment

## **CHARACTERISATION OF THE LIFE CYCLE OF INVESTORS**

**Life cycle can be broadly classified into phases:**

- Birth and education
- Earning Years
- Retirement

On an average, the first stage lasts for 22 years, the second for 38 years and the last for 25-30 years.

The earning year is when income and expenses are highest. The retirement stage is when incomes are low and expenses are high.

## **CLASSIFICATION OF INVESTOR NEEDS**

Needs are generically classified into protection needs and investment needs. Protection needs refer to needs that have to be primarily taken care of to protect the living standards, current requirement and survival requirement of investors. Needs for regular income. Need for retirement income and need for insurance cover are protection needs. Investment needs are additional financial needs that can be served through saving and investments. These are needs for children's professional growth.

### **WEALTH CYCLE CLASSIFICATION OF INVESTORS**

Wealth cycle based classification of investor's financial needs. Refers to using a generalized approach to saving and investment as the classifications, than age or life stages. The following table illustrates:

STAGE	FINANCIAL NEEDS	INVESTMENT PREFERENCES
Accumulation stage	Investing for long term identified financial goals	Growth option and long term products. High risk appetite
Transition stage	Near term needs for funds as per specified needs draw closer	Liquid and medium term investment. Preference for income and debt products.
Reaping stage	Higher liquidity requirements	Liquid and medium term investment, for income low risk appetite
Inter generation transfer	Long term investment of inheritance	Low liquidity needs, Ability to take risks and invest for the long term
Sudden wealth surge	Medium to long term	Wealth preservation. Preference for low risk products.

## **Asset Allocation**

Asset Allocation refers to the process of deciding the composition of a portfolio. In order to achieve the goals of a financial plan, investors should allocate their funds to equity, debt and other asset classes, according to the risk and return features of these classes. This process is called asset allocation.

### **Asset Allocation Strategies for Investors**

Benjamin Graham recommends the following allocations

Basic Managed Portfolio	50% in diversified equity value funds 25% in government securities fund 25% in high grade corporate bond fund
Basic Indexed Portfolio	50% in stock market index fund 50% in bond market index fund
Simple Managed portfolio	85% in balanced fund 15% in medium term bond fund
Complex Managed Portfolio	20% in diversified equity fund 20% in aggressive growth fund10% in specialty fund 30% in long term bond funds 20% in short term bond funds
Readymade Portfolio	Single index fund with 60% in equity and 40% in debt



## CHAPTER 6 ANALYSIS AND FINDINGS

### **Analysis and Findings**

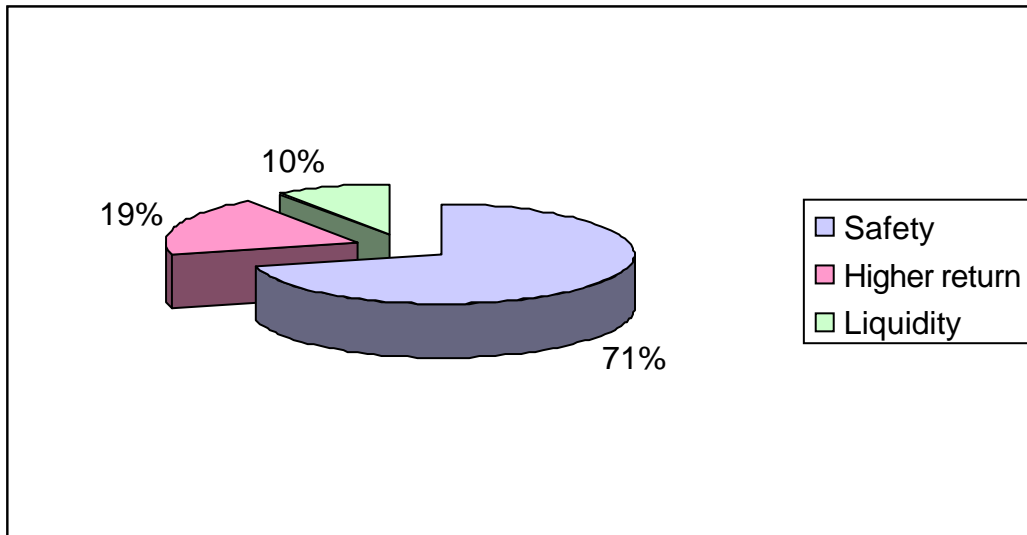
I visit to 45 people with questionnaires out of whom only 30 responded. I have analyzed my survey on the basis of these respondents feedback. Once the questionnaires were filled up, the next work that comes up is the analysis of the data arrived. We find out that more Business Men were inclined towards investing their in the Current A/c. Ladies are more inclined towards investing their funds in gold and other jeweler. On the other hand, service class people and retired fellows prefer more either Savings and/or Fixed Deposits. People with high income and who are young enough to take risks prefer shares and mutual funds.

Similarly, people are interested in knowing what the returns of their investments are. Similar large numbers of people are equally interested in the safety of their funds. There are the people who want easy liquidity of money and these are basically the business people who have to deal in the ready cash all the time. Surprisingly, while a large number (24) of people are aware of the tax benefits, a very small number of them, only 9, are interested in it.

Whilst a large number of people are aware of mutual funds, comparatively a very less number invests into it. On asking how they get knowledge of Mutual Funds, a large number of them attributed it to Print Media. Even Banks today follow the role of investment advisors. Very few get any information from the Electronic Media or the Relatives/Friends. Hence AMCs must increase the awareness about their product through Electronic Media (TV's, Cables, Radios etc) as well as and should not just constrained itself to the print advertisement. Those who do not read newspaper/magazines due to any reasons may watch or listen to the advertisements.

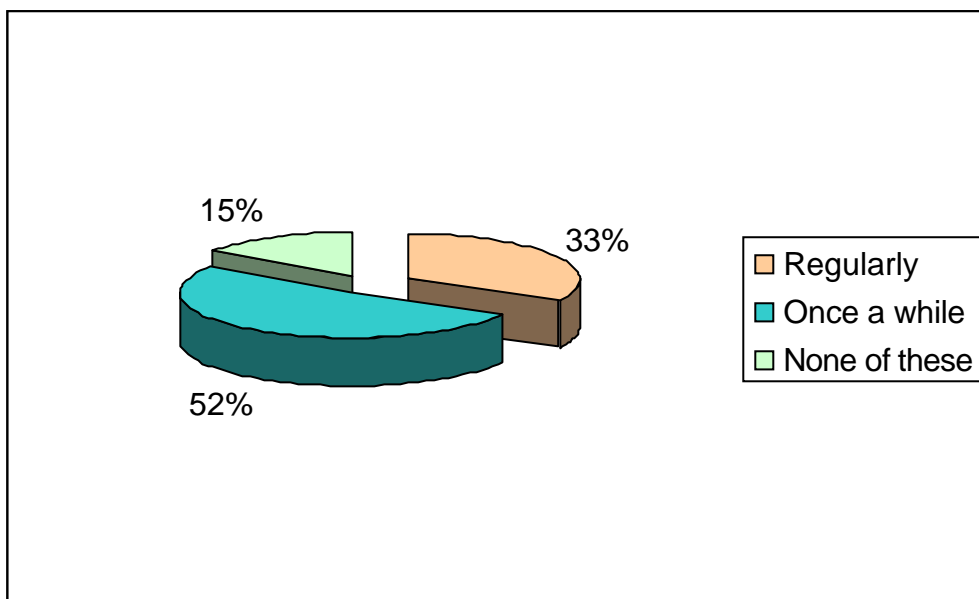
A large part of respondents said that their knowledge about MF does not allow them to invest into it while to another segment considered government bonds much better.

### **PRIORITY OF INVESTORS WHILE INVESTING**



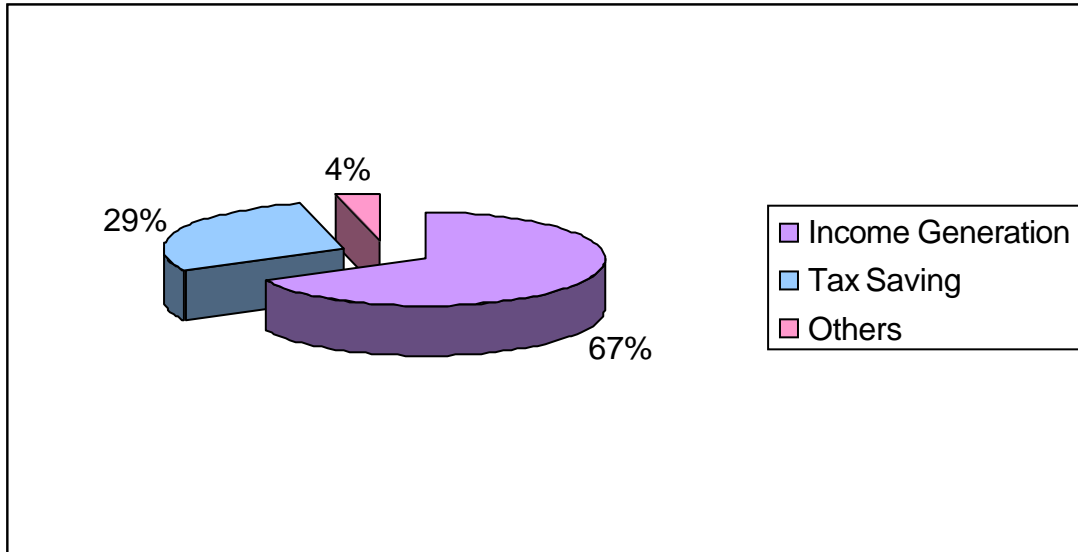
**Interpretation-** In my study the 71% peoples believe in invest in mutual funds because of safety. This is the most recommended in investment.

### **FREQUENCY OF INVESTMENT**



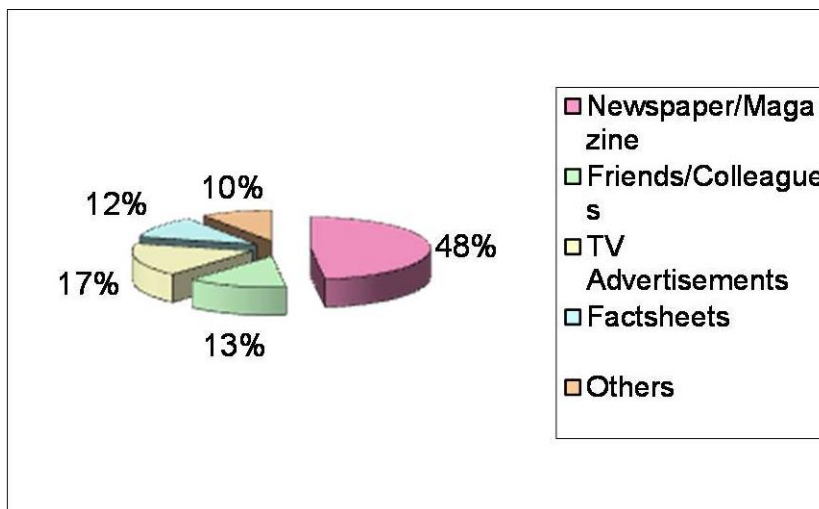
**Interpretation-** In my study I was 33% persons were regularly invited in mutual funds. 52% peoples want to try to invest and 15% are not interested.

### **OBJECTIVE BEHIND INVESTMENT**



**INTERPRITATION-** I was found that 67% peoples were invested in mutual funds for the regular income generation, 29% for tax saving.

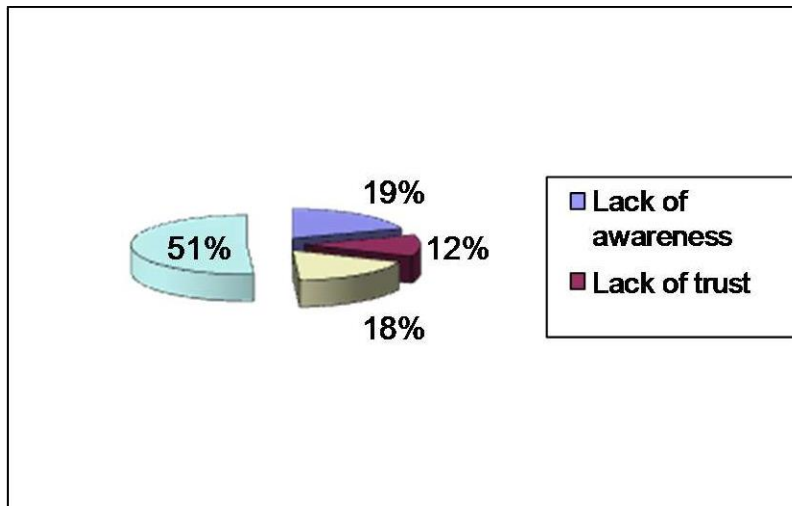
### **SOURCES OF AWARENESS**



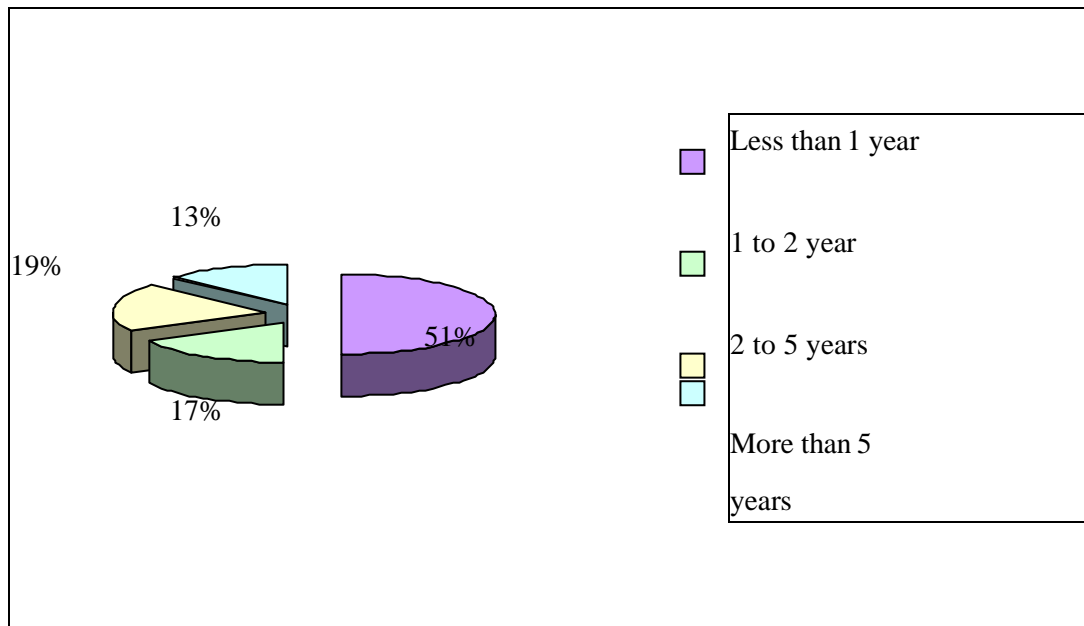
**INTERPRETATION-** I also found that many of the peoples get the knowledge about the mutual fund with the help of media like newspapers, TV etc.

### **SPECIFIC APPREHENSIONS ABOUT INVESTING IN MUTUAL FUNDS**

**INTERPRETATION-** In my study 20% population are having the lack of

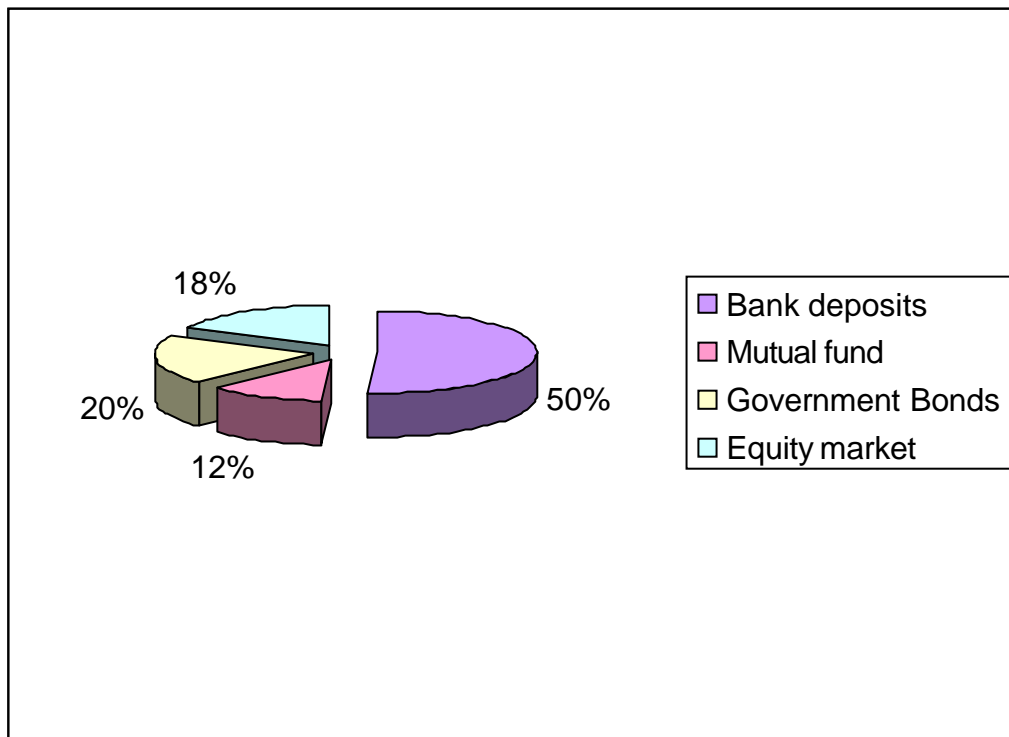


awareness, 50% are don't have knowledge that is a mutual fund is an investment sources.

**TIME PERIOD FOR INVESTMENT**

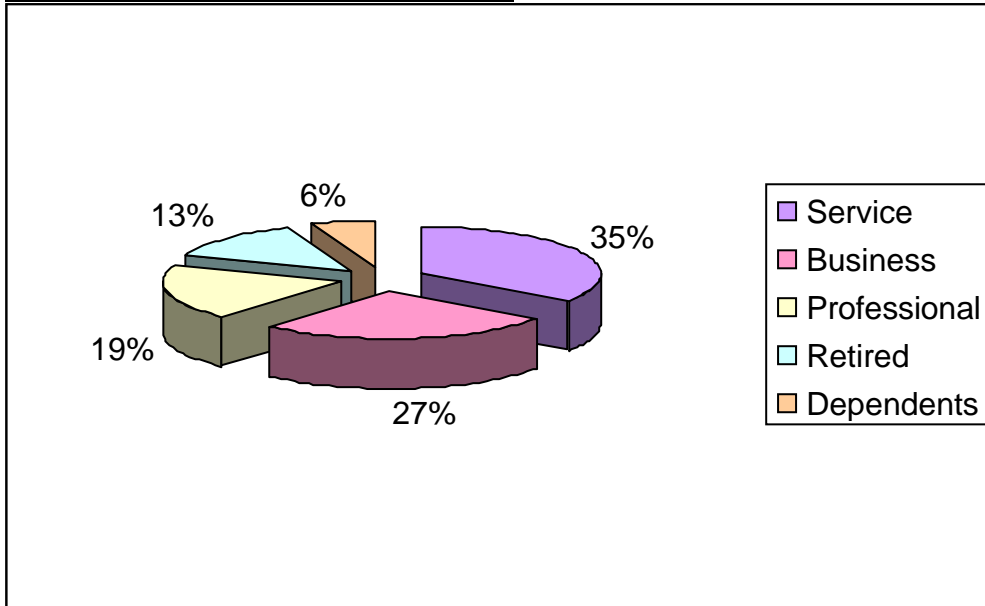
**INTEPRITATION-** I was found that 51% peoples will invested in mutual funds for the less than year because of trust

### PRIORITY OF INVESTORS TO INVEST IN VARIOUS FINANCIAL PRODUCTS



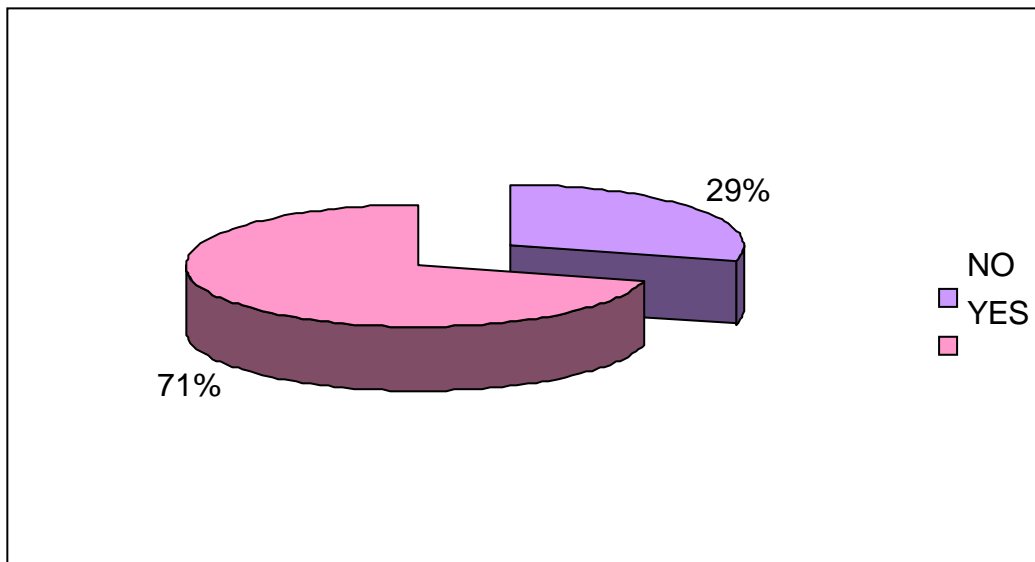
**INTERPRITATION-** In India 50% peoples invest their money in banks with thefaze of trust.

### OCCUPATION WISE DISTRIBUTION



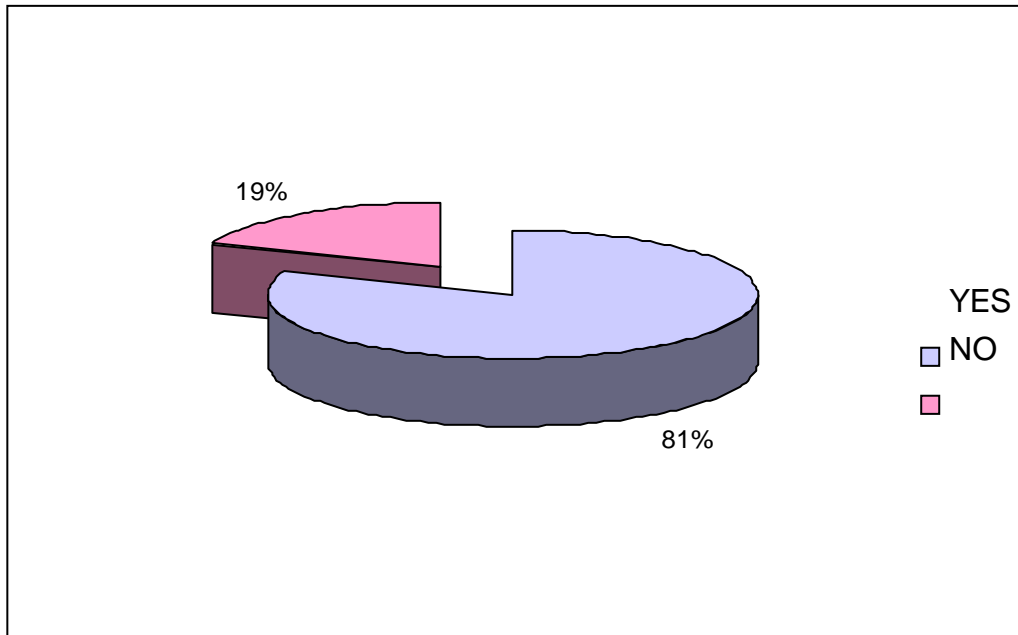
**INTEPRITATION-** In above diagram I will show the investors by their occupation like students, businessman etc.

### AWARENESS OF MUTUAL FUNDS



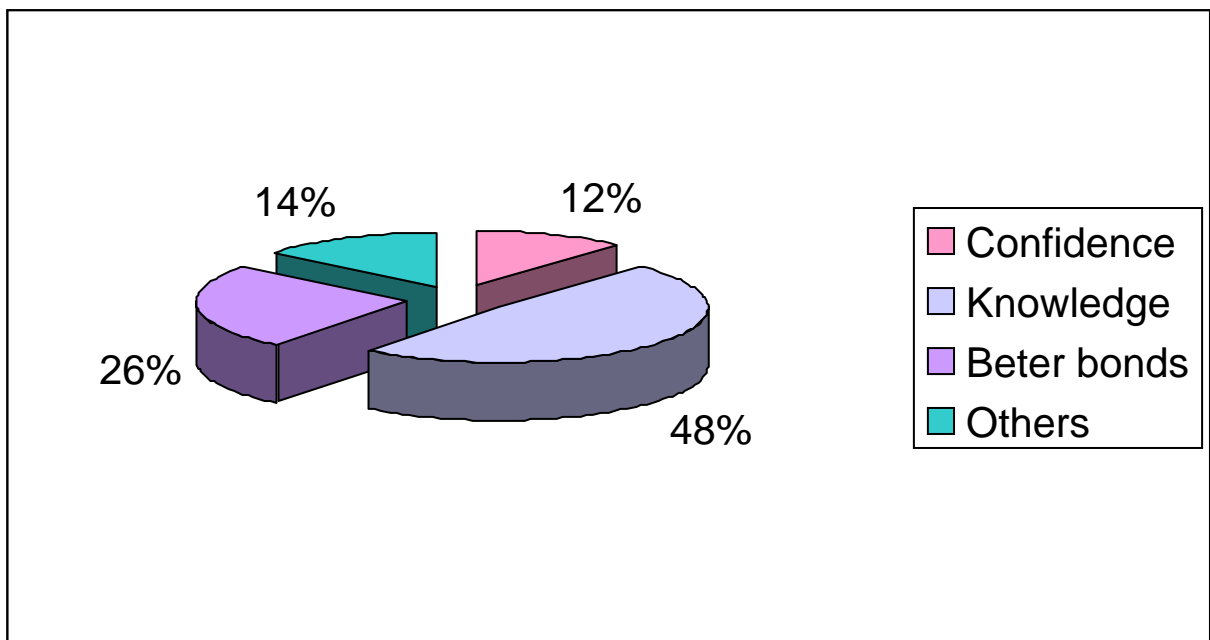
**INTEPRITATION-** In above diagram 71% peoples have the knowledge of mutual funds founded by the survey on 100 peoples.

### **AWARENESS OF TAX BENEFITS**



**INTERPRITATION-** By the survey on 100 peoples I am found that 82% peoples have the knowledge of tax benefit by investing in mutual funds.

### **REASONS FOR NOT INVESTING IN MUTUAL FUNDS**



**INTERPRITATION-** By the taking survey it is also found that 48% people invested in mutual funds with the help of



knowledge.

### **KEY FINDINGS**

- Today people are more aware about the various changing in investment products and new plans.
- More opportunities in India for investment and managing proper wealth.
- Competition and growth both are increasing day by day in the market.
- More companies are coming and providing better information and services.
- There are huge benefits for long-term investment.
- Markets are growing very rapidly in terms of products availability and services providers.
- Advisors and agents are providing better services and timely information to the clients as they are bound to.
- Agents and advisors ready to gain knowledge and also improve PLANNING in Indian financial markets.
- Today people are more aware about the various changing in investment products and new plans.
- More opportunities in India for investment and managing proper wealth.
- Competition and growth both are increasing day by day in the market.
- More companies are coming and providing better information and services.
- There are huge benefits for long-term investment.
- Markets are growing very rapidly in terms of products availability and services providers.

## CHAPTER 7 RECOMMENDATION AND CONCLUSION



### **Investors point of view**

The question the entire customer, irrespective of the age group and financial status, think of is- Are Mutual Funds are a safe option? What makes them safe? The basis of mutual fund industry's safety is the way the business is defined and regulations of law. Since the mutual fund invests in the capital market instruments, so proper knowledge is essential. Hence the essential requirement is the well informed seller and equally informed buyer. Who understands and help them to understand the product (here we can say the capital market and the money market instruments) are the essential pre- conditions.

Being prudent investors one should:

- i. Ask one's agent to give details of different schemes and match the appropriate ones.
- ii. Go to the company or the fund house regarding any queries if one is not satisfied by the agents.
- iii. Investors should always keep an eye on the performance of the scheme and other good schemes as well which are available in the market for the closed comparison.
- iv. Never invest blindly in the investments before going through the fact sheets, annual reports etc. of the company since, according to the guidelines of the

SEBI, the AMCs are bound to disclose all the relevant data that is necessary for the investment purpose by the investor.



### **Companies point of view**

Following measures can be taken up by the company for getting higher Investments in the mutual fund schemes.

- i. Educate the agents or the salesmen properly so that they can take up the queries of the customer effectively.
- ii. Set up separate customer care divisions where the customers can any time pose their query, regarding the scheme or the current NAV etc. These customer care units can work out in accordance with the requirements of the customer and facilitate him to choose the scheme that suits his financial requirements.
- iii. Conduct seminars or programs on about mutual funds where each and every minute information about the product is outlined including the risk factor associated with the different classes of assets.
- iv. Developed, design separate schemes for rural/semi urban areas and lower the minimum investment amount from Rs.500.
- v. Recruit appropriate number of agents for rural/urban and semi-urban areas.
- vi. Make customer care services faster.

**Choose appropriate media, newspaper/magazines, T.V.  
for marketing the product and educate**

**Commercials, etc.**

## CHAPTER 8 LIMITATION

### LIMITATION

#### LIMITATIONS

This project is limited in scope as the survey is conducted with a shortage of time constraint and is also based on secondary data.

- ❖ The answers given by the respondents may be biased due to several reasons or could be attachment to a particular bank or brand.
- ❖ Due to ignorance factor some of the respondents were not able to give correct answers.
- ❖ The respondents were not disclosing their exact portfolio because they have a fear in their minds that they can come under tax slabs.

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**<http://ezinearticles.com>**

JOURNALS AND MAGAZINES – BUSINESS, MARKET WATCH, INVESTORS.

THE FINANCIAL EXPRESS MAGAZINE

**CHAPTER 10 ANNEXURES****ANNEXURES****QUESTIONNAIRE**

- 1) Name of the customer Mr./Mrs./Ms.
- 2) Address /Contact
- 3) Bank you are dealing with
- 4) What occupation you are in?
- 5) What is the age group you fall in?
  - a) 20-30
  - b) 30-40
  - c) 40-50
  - d) 50-60
  - e) above 60
- 6) What is the per month income of your family?
  - a) Less than 10,000
  - b) 10,000-30,000
  - c) 30,000-50,000
  - d) Above 50,000
- 7) Type of investment
  - a) Current
  - b) Savings
  - c) Fixed Deposits
  - d) Shares
  - e) Bonds/Debentures
  - f) Mutual Funds
  - g) Gold/Real Estate
- 8) Preference
  - a) Liquidity
  - b) Return
  - c) Tax benefit
  - d) Safety
- 9) Are you aware of the Mutual Funds?  
Yes/No

If yes, then please attempt next question else go to question no.12

10) Have you ever invested in Mutual Funds?

If yes, please attempt next five questions else go to question no.11

i) which scheme did you last invest in?

ii) What returns did you get out of that scheme?

iii) Since how long you are in that scheme?

iv) Would you like to switch to current NPO?

YES/NO

v) Do you have any knowledge of the tax benefits?

Where do you get information about Mutual Funds?

a) Print Media b) Electronic Media c) Friends/Relatives d) Broker/Investment e)

Bank

11) If you've never invested in the Mutual funds then attempt the next question

i) what has been the reason of your not investing into the mutual funds?

a) Lack of confidence b) Imperfect knowledge c) Finds Government securities/bonds better d) other reasons

ii) Are you aware of the SEBI/RBI guidelines?

12) If you are not aware of the Mutual Funds then attempt the next Are you not interested in generating higher returns?