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An Analysis upon the Role of Banking and Non-Banking Financial Companies in Indian Mutual Fund Market

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Abstract – The mutual fund industry started in India in a small way with the UTI Act creating what was effectively a small savings division within the RBI. Over a period of 25 years this grew fairly successfully and gave investors a good return, and therefore in 1989. as the next logical step, public sector banks and financial institutions were allowed to float mutual funds and their success emboldened the government to allow the private sector to foray into this area.

The most important trend in the mutual fund industry is the aggressive expansion of the foreign owned mu Mai fund companies and the decline of the companies floated by nationalized banks and smaller private sector players. Reliance Mutual Fund. UTI Mutual Fund. ICICI Prudential Mutual Fund. HDFC Mutual Fund and Biiia Sun Life Mutual Fund arc the top five mutual fund company in India.

Mutual fund companies in India are influencing the retail investors to invest their surplus funds with or without complete understanding to the mutual funds. It also explores the factors influencing the retail investor to invest in mutual fund schemes. It also seeks to understand the role of SEBI in safeguarding the interest of retail investor in mutual funds. It also identifies the key factor that influences the customer preference for a particular mutual fund. One of the objectives of the present study was to evaluate the financial performance of various mutual fund schemes on different parameters.

Performance of mutual fund schemes has been evaluated by using risk to standard deviation, sharp ratio Treynor Index. From the study it was found that, the majority of sample funds have experienced high returns and lower variability on the returns as compared to market portfolios. Earlier, every mutual fund offering resembled the other and this was one reason why the investors were a bit slow in embracing the mutual fund option. Now the time has changed and fund houses have come out with a host of new products that eye investor's wallet.

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INTRODUCTION

After the government policy of liberalization in the industrial and financial sector, many new financial instruments came into existence. Among these mutual fund products have proved to be the most catalytic instrument in the Indian capital market. Mutual Fund is designed to target small investors, salaried people and others who are intimated by the mysteries of stock market but, nevertheless like to reap the benefits of stock market investing. The growing importance and interest of investors towards Indian mutual fund may be noted, in terms of increased mobilization of funds and the increasing number of schemes and investors in the industry. To fulfill the expectations of millions of account holders, the mutual fund are required to function as successful institutional investors.

There is a substantial growth in mutual fund market is due to a high level of precision in the design and marketing of variety of mutual fund products. Researchers have attempted to study the changing perception of investors towards mutual fund investments, their needs and expectations from different type of mutual funds available in Indian market and identify the risk return perception with the purchase of mutual fund. Various techniques applied to find the important characteristics being considered by the Indian investors in investment decision. Today investors are on the way of exploring the mutual fund investment and willing to know how best it can serve as an investment tool.

Indian financial market presents multiple avenues to the investors. Though certainly not the best or the deepest of markets it has ignited the growth rate in mutual fund industry to provide reasonable options for an ordinary person to invest their savings. With the progressive liberalization of economic policies, there has been a rapid growth of captive markets and financial services industry including merchant banking, leasing and venture capital. Consistent with this evolution of the financial sector, the mutual fund industry has also come to occupy an important role.

Mutual Funds in India are financial instruments. A mutual fund is not an alternative investment option to stocks and bonds; rather it pools the money of several investors and invests this in stocks, bonds, money market instruments and other types of securities. The owner of a mutual fund unit gets a proportional share of the fund's gains, losses, income and expenses. Mutual Fund is vehicle for investment in stocks and bonds. Each Mutual fund has a specific stated objective. The fund's objective is laid out in the fund's prospectus, which is the legal document that contains information about the fund, its history, its officers and its performance.

The share value of the Mutual Funds in India is known as net asset value per share (NAV). The NAV is calculated on the total amount of the Mutual Funds in India, by dividing it with the number of shares issued and outstanding shares on daily basis. The company that puts together a mutual fund is called an AMC. An AMC may have several mutual fund schemes with similar or varied investment objectives. The AMC hires a professional money manager, who buys and sells securities in line with the fund's stated objective. The Securities and Exchange Board of India (SEBI) mutual fund regulations require that the fund's objectives are clearly spelt out in the prospectus. In addition, every mutual fund has a board of directors that is supposed to represent the shareholders' interests, rather than the AMC‟s.

In the financial industry, the talk of the day is 'mutual funds'. Mutual Fund Concept which has become popular in Western World since long is also gaining popularity in the developing countries like India as an institutional device to bridge the gap between supply and demand of capital in the market. Mutual funds are financial intermediaries which collect the savings of investors and invest them in a large and well diversified portfolio of financial assets with a view to reduce risks and to maximize the income and capital appreciation for distribution to the investors on a pro-rata basis. Mutual Funds are conceived as institutions for providing small investor with avenues of investment in the capital market. (Machiraju, 2007) Mutual Funds came in India with the establishment of Unit Trust of India (UTI) in 1964. The UTI was set to mobilise the savings of the community and channelize them into productive ventures. The growth in the business of UTI, especially during the eighties has been spectacular. (Avadhani ,2009) With the view to provide a wider choice to small investor, the Government of India amended Banking Regulation Act in 1987 to permit commercial banks to launch mutual funds in India. Considering the fact that the household sector has a dominant share in the aggregate net savings of the economy, banks in their quest for mobilizing the community savings into productive avenues have found in mutual funds a lucrative opportunity. The State Bank of India (SBI) was the first Bank to launch a mutual fund called SBI Mutual Fund in July, 1987. (Srivastava, 2001) Commercial Banks are targeting those customers who have a good amounts of deposit in the Bank. Commercial Banks were giving emphasis on Cross-Selling business for Mutual Fund Products. Cross selling stands for being able to offer to the existing bank customer, some additional banking and non-banking products with a view to expand business, reduce the per customer cost of operations and provide more satisfaction and value to the customer. By adopting the crossselling techniques, the commercial banks are able to increase the resource mobilisation towards mutual fund at a lower cost (http://www.wisegeek.com/what-iscross-selling.htm).

After a quiet beginning in the mutual fund industry lay dormant till 1987 mainly because it was monopolized by one institution i.e. UTI and the nomenclature ' Mutual Fund ' had not really gained currency. However after the entry of five public sector banks and two insurance companies in the mutual fund business since 1987 the scenario has undergone a phenomenal change and mutual fund as a financial instrument is becoming popular and awareness of investors towards this investment outlet is gradually increasing.

In India, the mutual fund industry started with the setting up of the erstwhile Unit Trust of India in 1963. Public sector banks and financial institutions were allowed to establish mutual funds in 1987. Since 1993, private sector and foreign institutions were permitted to set upmutual funds.

In February 2003, following the repeal of the Unit Trust of India Act 1963 the erstwhile UTI was bifurcated into two separate entities viz. The Specified Undertaking of the Unit Trust of India, representing broadly, the assets of US 64 scheme, schemes with assured returns and certain other schemes and UTI Mutual Fund conforming to SEBI Mutual Fund Regulations.

As at the end of March 2008, there were 33 mutual funds, which managed assets of Rs. 5,05,152 crores (US $ 126 Billion)* under 956 schemes. This fast growing industry is regulated by the Securities and Exchange Board of India (SEBI).

CONCEPT OF MUTUAL FUND:

A mutual fund is a common pool of money into which investors place their contributions that arc to be invested in accordance with a stated objective. The ownership of the fund is thus joint or "mutual"; the

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fund belongs to all investors. A single investor's ownership of the fund is in the same proportion as the amount of the contribution made by him or her bears to the total amount of the fund Mutual Funds arc trusts, which accept savings from investors and invest the same in
diversified financial instruments in terms of objectives set out in the trusts deed with the view to reduce the nsk and maximize the income and capital appreciation for distribution for the members A Mutual Fund is a corporation and the fund manager's interest is to professionally manage the funds provided by the investors and provide a return on them after deducting reasonable management fees.

The objective sought to be achieved by Mutual Fund is to provide an opportunity for lower income groups to acquire without much difficulty financial assets. They cater mainly to the needs of the individual investor whose means are small and to manage investors portfolio in a manner that provides a regular income, growth, safety, liquidity and diversification opportunities.

Definition –

"Mutual funds art collective savings and investment vehicles where savings of small (or sometimes big) investors are pooled together to invest for their mutual benefit and returns distributed proportionately" "A mutual fund is an investment that pools your money with the money of an unlimited number of other investors. In return, you and the other investors each own shares of the fund.
The fund's assets are invested according to an investment objective into the fund's portfolio of investments. Aggressive growth funds seek long-term capital growth by investing primarily in stocks of fast-growing smaller companies or market segments Aggressive growth funds are also called capital appreciation funds".

INDIAN FINANCIAL SYSTEM AND MUTUAL FUNDS

The economic and financial scenario of India prior to 1991 was somehow not optimistic. Indian economy at that time was suffering from low savings, low GDP, high inflation, high unemployment, high rates of interest, low forex reserve, etc.. When India approached IMF for financial assistance in 1991, we were imposed certain conditions on the basis of which the financial assistance was sanctioned to India. These restrictions which we accepted under the pressure from IMF were actually the starting point of economic reforms popularly known as LPG process. The fruit of liberalisation reached their peak in 2007, when India recorded its highest GDP growth rate of 9%. With this, India became the second fastest growing major economy in the world, next only to China. The growth rate has slowed significantly in the first half of 2012. An Organisation for Economic Co-operation and Development (OECD) report states that the average growth rate 7.5% will double the average income in a decade, and more reforms would speed up the pace. India's Gross domestic product (GDP) growth rate became lowest in 2012-13 over a decade, growing merely at 5%, more criticism of India's economic reforms surfaced, as it apparently failed to address employment growth, nutritional values in terms of food intake in calories, and also exports growth – and thereby leading to a worsening level of current account deficit compared to the prior to the reform period.

By 2008, India had established itself as one of the world's fastest growing economies. Growth significantly slowed to 6.8% in 2008–09, but subsequently recovered to 7.4% in 2009–10, while the fiscal deficit rose from 5.9% to a high 6.5% during the same period. India's current account deficit surged to 4.1% of GDP during Q2 FY11 against 3.2% the previous quarter. The unemployment rate for 2010–11, according to the state Labour Bureau, was 9.8% nationwide. As of 2011, India's public debt stood at 68.05% of GDP which is highest among the emerging economies. However, inflation remains stubbornly high with 7.55% in August 2012, the highest amotrade (counting exports and imports) stands at $606.7 billion 45 and is currently the 9th largest in the world. During 2011–12, India's foreign trade grew by an impressive 30.6% to reach $792.3 billion (Exports-38.33% & Imports-61.67%). The economy of India is the ninth-largest in the world by nominal GDP and the third-largest by purchasing power parity (PPP).

All these developments could have not been possible without the sound financial market.

It is the financial market which finances economic development. It is the financial market which channelizes the saving of the people into the investment. Indian financial markets are getting more and more institutionalized. Foreign investors, local institutions and mutual funds are now playing a bigger role. Mutual funds play a significant role in the development of the financial market and this has been proved in the developed countries like United States, United Kingdom and Japan. India is at its first stage of a revolution that has already peaked in United States. In United States, the asset base of mutual funds is much higher than its bank deposits. In India, mutual funds'assets are not even 10% of the bank deposits, but this trend is only at the beginning.

The mutual funds in India have emerged as strong financial intermediaries and are playing a very important role in bringing stability to the financial system and efficiency to resource allocation. Mutual funds help corporates in raising funds for their financial needs and provide an avenue of investment to investors by parking their savings. This leads to the overall growth of the economy. The major chunk of the household savings in India, which earlier went to bank deposit are now being taken by mutual funds. The active involvement of mutual funds in promoting economic development can be seen not only in terms of their participation in the savings market but also in their dominant presence in the money and the capital market.

A developed financial market is critical to build overall economic development and mutual funds play an active role in promoting an active healthy market. Mutual funds increase liquidity in the money market. The asset holding pattern of mutual fund in India indicates the dominant role of the mutual funds in the money and capital markets. The private corporate sector in India is a deficit sector and the gap between demand and supply of financial resources is met by funds raised through loans, advances and issuance of securities. However, the buoyancy in the capital market has increased the reliance of the corporate sector has more than doubled. The changing pattern of corporate financing indicates that the banking sector is losing its prominence vis-a-vis the other financial sector. Direct financing by mutual funds to the corporate sector has substantially increased after SEBI guidelines allowed 'the corporate sector to reserve 20% of the public issues for Indian mutual funds. Mutual funds have also widened the private placement market for corporate securities.

Mutual funds have enabled the corporate sector to raise capital at reduced costs and have opened an avenue for alternate source of capital. Mutual funds in India have merged as a critical institutional linkage among various financial segments like savings, capital market and the corporate sector. As various tax incentives and benefits on mutual fund investment are offered by the Government, their role in the mobilization of savings and the development of the economy will assume more significance. They provide much needed impetus to the money market and the stock markets; in addition to direct and indirect support to the corporate sector.‖ Above all mutual funds have given a new direction to the flow of personal savings and semi-urban areas to reap benefits of stock market investments. Indian mutual funds are thus playing a very crucial development role in allocating resources in the emerging market economy.

EMERGENCE OF MUTUAL FUND

Mutual funds now represent perhaps the most appropriate investment opportunity for most investors; as financial markets become more complicated and sophisticated; investors need a financial intermediary who provides the required knowledge and professional expertise on successful investing. It is no wonder then that in the birth place of mutual fund- the U.S.A. – the fund industry has already overtaken the banking industry, more funds being under mutual fund management than deposited with banks.

The Indian Mutual Fund industry has already started opening up many of the exciting investment opportunities to Indian investors. We have started witnessing the phenomenon of more savings now being entrusted to the funds than to the banks. Despite the continuous growth in the industry, mutual funds are still a new financial intermediary in India. Hence, it is important that the investors, the mutual fund agents/distributors, the investment advisors and even the fund employees acquire better knowledge of what mutual funds are, what they cannot, how the function differently from other intermediaries such as banks.

BANKING IN A GLOBAL MARKETPLACE

The Indian banking system will have to deal with mindboggling paradigm shifts in a complex global environment in the years ahead. With yet another year of high economic growth, the Indian economy continues on a sustained upwards trajectory. The GDP growth has averaged 8% over the past four years and is determined by three key macroeconomic factors.

1. Changing demographic profile- 60% of India's population is expected to be below the age of 40 years by 2015

2. Structural change in the GDP- with over 60% of the contribution coming from the service sector, the higher contribution from services, coupled with high growth in the industry sector and improved performance of the agriculture sector are de-risking India's economic model and building a strong foundation for continued growth.

3. Booming capital market and increased employment opportunities are resulting in higher disposable incomes, higher consumption and greater appetite for risk. The development of the debt market and the role of financial intermediaries in routing national savings to fund the massive requirements of the infrastructure segment will play a critical role in sustaining the growth momentum.

4. The sustained economic growth provides banks with significant business opportunities, rapid growth driven by player strategy choices. Some banks have aggressively focused on pure growth to create size and mass, others have focused on the quality of growth. These widely divergent strategic approaches are likely to establish leadership position for the future.

5. While growth brings greater opportunities, it also creates significant new challenges for the Indian banking system.

Challenges have the potential to fundamentally change the structure of the Indian financial service industry, particularly banking, with specific reference to three key impact areas:

a. Capital management challenge

b. Managing the convergence of financial services

c. Mastering the challenge of liabilities

METHODOLOGY

The study is an exploratory one and based on secondary data. The industry-level aggregate data published regularly by Securities and Exchange Board of India (SEBI), Reserve Bank of India (RBI), Association of Mutual Fund in India (AMFI), State Bank of India (SBI) and other commercial banks, and other prominent organization and associations has been taken.

Information regarding deposit mobilisation of commercial banks has been collected from the Press Releases, Annual Reports and other periodicals and publications of the commercial banks engaged in mutual fund business.

The financial newspaper particularly The Economic Times, the Business Standard and the bulletins, periodicals and other publications of various mutual fund associations has been consulted for the necessary data and information.

SAMPLE

Domestic banks: HDFC, ICICI, AXIS, SBI.

Foreign banks: UBS, Barclays, HSBC, ABN Amro.

Domestic Mutual Funds: HDFC, Kotak Mahindra Mutual fund, SBI, UTI, Reliance

Global mutual funds: DSP Merrillynch, Franklin Templeton, HSBC, FIDELITY.

To test the above objectives and used the weekly return data of equity mutual funds and their relevant benchmarks over the above said period. The return data of the mutual funds is taken from the Alpha database of CMIE. I also used popular websites for obtaining information about disclosed benchmarks for the funds in our sample. The week end values of the benchmarks were obtained from the PROWESS database of CMIE and were used to calculate the weekly returns from the benchmark.

DATA SOURCES

The main data sources are the mutual annual reports of the various Mutual Funds, the offer document of various Mutual Fund schemes, and the NAVs and repurchase prices announced by the funds from time to time. Data on market prices are collected from "*The Economic Times*" and the monthly economic reviews published by the Center for Monitoring Indian Economy (CMIE). The data of BSE National Index are collected from the index values published by The Stock Exchange, Mumbai and afterwards as available in '*The Economic Times*'. In addition to this, popular investment periodicals, such as Dalal Street and Capital Market have also been referred. Informational data are also collected from the various issues of RBI Bulletin and RBI reports on Currency and Finance. No primary data have been collected; however, interviews were conducted with the executives of Mutual Funds. During the interview, inquiries were made about the investment decision and organizational problems.

DATA ANALYSIS

Since the inception of mutual fund by the Unit Trust of India (UTI) and after showing growth in this business this has became a area of interest of commercial banks. Moreover, the profitability of banks has been very much affected due to too much restriction on their lending policies. They have been compelled to seek some other alternatives to increase their profits by means of diversifying their activities. Mutual funds offer an excellent outlet for diversification.

CONCLUSION

To sum up, one may note that Mutual funds in India have largely resorted to the retail markets and placed products through brokers and agents. The presence of these financial intermediaries along with the sheer size of the investment community of diverse background has complicated matters to a large extent. Lack of complete information about the clientele along with existing SEBI guidelines, that prohibits any sort of projections of return (so vital to investment decision making) has only compounded problem. For this, a concerted effort needs to be made to create a cost effective mechanism for communication. Disclosure standards need to be trimmed from a lengthy but sketchy set of rules, to an effective and meaningful one. Finally, increasing awareness through investor education is of paramount importance. A technically ill-equipped investor may not be able to reap full advantage from a system of complete information if he is not trained in how to process and optimally use it for valuation of assets.

Mutual funds in India has played significant role in mobilizing the savings from large number of public and channelizing to the development of capital market. Thus, now, it has been emerging as popular investment vehicle besides major source of finance for economic development of India. The nationalized banks were allowed to set up mutual funds in 1987. The doors were opened to private sector companies to set up mutual funds in 1993. Since then mutual funds have mobilized large savings.

From the above discussion it is observed that the banks and other financial companies have enormous opportunities in the mutual fund industry in India. But compare to the private mutual fund companies, performance of these banks and other financial companies are not satisfactory in spite of their huge customer base till the day. In this context, it is also true that the banks and other financial companies have to play a crucial role in the near future in the Indian mutual fund industry as now-a-days people wish to participate and invest in different mutual fund schemes.

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