

# **Role of Mutual funds in Capital market**

Arun Kumar.D

Associate Professor MBA, Department of Business Administration  
Bharath Institute of Higher Education and Research  
Selaiyur, Chennai, Tamil Nadu 600 073

## **ABSTRACT**

The Indian capital market has been increasing tremendously during last few years. With the reforms of economy, reforms of industrial policy, reforms of public sector and reforms of financial sector, the economy has been opened up and many developments have been taking place in the Indian money market and capital market. The Mutual funds is basically a risk reduction tool is achieved by diversification of the portfolio. The growth of any economy very much depends on the extent of promoting investments in the corporation sector. The savings of the investors or the public have to be mobilized for a productive use and this possible only by certain. Mutual funds have a significant role in channelizing savings in to the capital market. A mutual fund is a corporation that attracts savings. Which are then invested in money market debt market and capital market instruments such as shares & debentures. A Mutual fund acts as a link between the public and the capital market. The Main objectives of this paper is to Growth , Operation, Role and Recent Trends of Mutual funds are Future outlook and suggested for measures for make if a successful scheme in India.

## **1. INTRODUCTION**

The first mutual funds were established in Europe. One researcher credits a Dutch merchant with creating the first mutual fund in 1774. The first mutual fund outside the Netherlands was the Foreign & Colonial Government Trust, which was established in London in 1868. It is now the Foreign & Colonial Investment Trust and trades on the London stock exchange. Mutual funds were introduced into the United States in the 1890s. They became popular during the 1920s. These early funds were generally of the closed-end type with a fixed number of shares which often traded at prices above the value of the portfolio.

The first open-end mutual fund with redeemable shares was established on March 21, 1924. This fund, the Massachusetts Investors Trust, is now part of the MFS family of funds. However, closed-end funds remained more popular than open-end funds throughout the 1920s. By 1929, open-end funds accounted for only 5% of the industry's \$27 billion in total assets.

The modern mutual fund was first introduced in Belgium in 1822. This form of investment soon spread to Great Britain and France. Mutual funds became popular in the United States in the 1920s and continue to be popular since the 1930s, especially open-end mutual funds. Mutual funds experienced a period of tremendous growth after World War II, especially in the 1980s and 1990s.

At the end of 2010, there were 7,581 mutual funds in the United States with combined assets of \$11.8 trillion, according to the Investment Company Institute (ICI), a national trade association

of investment companies in the United States. The ICI reports that worldwide mutual fund assets were \$24.7 trillion on the same date.

## **2. WHAT IS MUTUAL FUND?**

“Many a drop make an ocean” A mutual fund is an investment instrument that pools money from many investors and invests this money in stocks, bonds, short-term money market instruments or other securities. The profit obtained on this investment is then returned to investors. Mutual fund keeps some part of the profit as a commission.

## **3. MUTUAL FUNDS & CAPITAL MARKET**

- Indian institute of capital market (IICM) aims is to educate and develop professionals for the securities industry in India and other developing countries, other objectives like to function on a centre for creating investors awareness through research & turning and to provide specialized consultancy related to the securities industry.
- Capital market play vital role for the growth of Mutual fund in India, capital market divided into the two parts one is the primary market and another is secondary market, primary market concern with issue management, as per the mutual fund concern the primary called as the NFO New Fund Offer, all the AMC (Assets Management Company) are issuing all the funds all the way through the NFO, Every NFO came with particularly investment objectives, style of investment and allocation of the funds all that thing depend on the fund manager style of investment. The other portion of the capital market is secondary market, as we have a discussion with reference with mutual fund secondary market means when the market bull stage the investors sole the units. Opposite when the bear stage the investor buy or some of the investor time wait for sale.

## **4. THE INDIAN MUTUAL FUND INDUSTRY HAS PASSED THROUGH THREE PHASES**

- The first phase was between 1964 and 1987 when Unit Trust of India was the only player. By the end of 1988, UTI had total assets worth Rs.6,700 crores.
- The second phase was between 1987 and 1993, during which period, 8 funds were established (6 by banks and one each by LIC and GIC). The total number of schemes went up to 167 and Assets Under Management saw the figures improving to over 61,000 crores.
- The third phase was marked by the entry of private and foreign sectors in the Mutual fund industry in 1993. The first entrant was Kothari Pioneer Mutual fund, launched in association with a foreign fund. The Securities and Exchange Board of India (SEBI) formulated the Mutual Fund Regulation in 1996, which for the first time established a comprehensive regulatory framework for the mutual fund industry. Since then several mutual funds have been set up by the private and joint sectors. Currently there are 34 Mutual Fund organizations in India.
- Today the AUM of the Mutual Fund Industry stands at over Rs.2 lakh crores, a growth of over 1 lakh crores since the last 5 years. Also the percentage of Equity assets in the overall AUM has increased from a shade under 5% to over 30% in the same period.

## **5. TYPES OF MUTUAL FUNDS**

- Close – ended mutual funds are created for a specific duration which is specified at the start of the funds. They have fixed number of shares or units outstanding. The net asset value per share or unit is determined based on the total value of investment.
- Open – ended mutual funds Open – ended mutual funds continue to operate for unlimited period of time. Investors can join and leave the funds any time. There is no fixed number of shares or units.
- Income funds income funds have the primary objective of a high current return, and investment is made in portfolios of high yielding shares.
- Growth funds they aim for capital gains and hence invest large proportion of their funds in equity shares with high growth potential.
- Balanced funds Balanced funds combine the objectives of earning current income and capital appreciation. So their portfolio consist of both equities and bonds.
- Tax saving fund tax saving funds are targeted to investors in high tax brackets. Income for these funds is tax – exempt.
- Sector – based funds Mutual funds may offer opportunities to investors to invest in the securities of specific sector.

## **6. ADVANTAGES OF MUTUAL FUNDS**

- Simplicity Mutual funds are the simplest means of investing in the stock market securities for small investors and those investors who have no understanding of stock market or who do not have time or liking to actively trade in stock.
- Flexibility Investors do not want waste time visiting the mutual funds for buying and selling shares. These days, most mutual funds facilitate buying, selling and transfer of shares by phone.
- Professional Management Mutual funds employ expert managers the investor's investments. Thus, small investors are able to avail services of professional fund managers without a heavy cost
- Diversification Small investors may not be able to invest in many securities as they may have limited savings. Mutual funds invest in large number of shares and other type s of securities like govt. bonds, corporate bonds etc.
- Affordability most mutual funds offer a variety of investment scheme with different investment goals and they specify low amount as the minimum investment.

## **7. DISADVANTAGES OF MUTUAL FUNDS**

- High fees and expenses the high fees and expenses of mutual funds include sales fee, management fee and funds expenses. Management fees include charges for managerial service and typically range from .25 to 2 percent.
- Brokerage fees Investors are required to pay brokerage fees in addition to the high fees and expenses of mutual funds.
- Hidden cost there is soft money or hidden brokerage fees that the mutual funds use research.
- Risk of ownership the mutual funds investors suffer the usual ownership risk.

- Cost of diversification the diversification advantages provided by the mutual funds might become a disadvantages as they curb the possibility for large gains from individual shares.

**8. GROWTH OF MUTUAL FUNDS**

- By the year 1970, the industry had 361 Funds with combined total assets of 47.6 billion dollars in 10.7 million shareholder’s account.
- However, from 1970 and on wards rising interest rates, stock market stagnation, inflation and investors some other reservations about the profitability of Mutual Funds, Adversely affected the growth of mutual funds.
- Hence Mutual Funds realized the need to introduce new types of Mutual Funds, which were in tune with changing requirements and interests of the investors.
- The 1970’s saw a new kind of fund innovation; Funds with no sales commissions called “ no load “ funds. The largest and most successful no load family of funds is the Vanguard Funds, created by John Bogle in 1977.
- In the series of new product, the First Money Market Mutual Fund ( MMMF)i.g. The Reserve Fund” was started in November 1971. This new concept signaled a dramatic change in Mutual Fund Industry.
- Most importantly, it attracted new small and individual investors to mutual fund concept and sparked a surge of creativity in the industry.

**COMPARISON OF INVESTMENT IN BANKS V/S MUTUAL FUNDS**

<b>PARTICULAR</b>	<b>BANKS</b>	<b>MUTUAL FUNDS</b>
Returns	Low	Better
Administrative exp.	High	Low
Risk	Low	Moderate
Investment options	Less	More
Network	High penetration	Low but improving
Liquidity	At a cost	Better
Quality of assets	Not transparent	Transparent
Interest calculation	Minimum balance between 10th. & 30th. Of every month	Everyday
Guarantee	Maximum Rs.1 lakh on deposits	None

**TABLE No 1**

**9. ROLE OF MUTUAL FUNDS IN CAPITAL MARKET**

- As mutual fund has entered into the Indian Capital market, growing profitable enough to attract competitors into this cherished territory encouraging competition among all the mutual fund operators, there is need to take some strategy to bring more confidence among investors for which mutual fund would be able to project the image successfully.

- The recommendations of the Secondary Market Advisory Committee, the SEBI decided to permit the Mutual funds to participate in the Derivatives market at par with Foreign Institutional Investors (FII).
- The Mutual funds shall be treated at par with registered FII in respect of positions limits in Index futures, Index options, Stock options and Stock futures contracts. The Mutual funds will be considered as trading members like registered FIIs and the schemes of Mutual funds will be treated as clients like sub-accounts of FIIs.
- This revised policy will be applicable to all new schemes which are yet to be launched and for existing schemes, the Mutual funds are required to obtain positive consent from the majority unit holders for participation in the Derivatives segment while simultaneously allowing exit option to dissenting members without any load.

#### **RECENT TREND OF MUTUAL FUNDS**

- India is at the first stage of a revolution that has already peaked in the U.S. The U.S. boasts of an Asset base that is much higher than its bank deposits.
- In India, mutual fund assets are not even 10% of the bank deposits, but this trend is beginning to change.
- Recent figures indicate that in the first quarter of the current fiscal year mutual fund assets went up by 115% whereas bank deposits rose by only 17%. (Source: Thinktank, the Financial Express September, 99) This is forcing a large number of banks to adopt the concept of narrow banking wherein the deposits are kept in Gilts and some other assets which improves liquidity and reduces risk.
- The basic fact lies that banks cannot be ignored and they will not close down completely. Their role as intermediaries cannot be ignored.
- It is just that Mutual Funds are going to change the way banks do business in the future.

#### **FUTURE OUTLOOK AND SUGGESTION**

- As mutual fund has entered into the Indian Capital market, growing profitable enough to attract competitors into this cherished territory encouraging competition among all the mutual fund operators, there is need to take some strategy to bring more confidence among investors for which mutual fund would be able to project the image successfully.
- The mutual funds are operated in the public sector. Hence private sector may be Allowed to float mutual funds, intensifying competition in this industry.
- To operations of many mutual fund, there will be need for appropriate guidelines for self-regulation in respect of publicity/advertisement and inter scheme transactions within each mutual fund.
- The infrastructure bottlenecks will have to be removed and banking and postal systems will have to be taken place for growth of mutual funds.
- The mutual funds need to take advantage of modern technology like computer and tele-communications to render service to the investors.

#### **10. CONCLUSION**

The Indian economy is second largest economy in the world, but on 2008 and first quart of 2009 was international financial liquidity and global fund crisis. USA economy affect by sub-

prime crisis that creates problem of international financial market, commodity market and foreign exchange market. But Indian economy less affects due to fast moving for consumer durable, growth of capital expenditure projects and service sector, Indian government easily attract foreign investors. Foreign Institutional Investors invest on Indian capital market, it is continuous growing. With the structural liberalization policies no doubt Indian economy is likely to return to a high grow path in few years. Hence mutual fund organizations are needed to upgrade their skills and technology. Success of mutual fund however would bright depending upon the implementation of suggestions.

## **11. REFERENCES**

- [1] Financial Services – Mr.B.Santhanam.
- [2] Financial Services – Chand.
- [3] [www. Mutual funds.com](http://www.Mutualfunds.com)
- [4] [www.google.com](http://www.google.com)