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Periodic Research

The World of Mutual Funds

Abstract

The mutual fund sectors are one of the fastest growing sectors in Indian Economy and have awesome potential for sustained future growth. Mutual funds make saving and investing simple, accessible, and affordable. Anybody with an investible surplus of as little as a few hundred rupees can invest in Mutual Funds. These investors buy units of a particular Mutual Fund scheme that has a defined investment objective and strategy. The money thus collected is then invested by the fund manager in different types of securities. SEBI is the regulatory body to control and regulate the securities market and Mutual Fund industry in India.

Objective of study: In this paper, I have undertaken a study on mutual funds. This paper focuses on the analysis of the mutual funds, its schemes, its benefits, and drawbacks and I have made a detailed summary on its various aspects. Keeping in mind the rise and fall in the money market it is better to invest in mutual funds for those investors who are risk adverse and for those who are risk taker it is better for them to invest in share market. This paper aims at exploring the potential of mutual funds in India.

Keyword: Mutual funds, NPV, securities, debenture, liquidity, risk, AMFI, funds.

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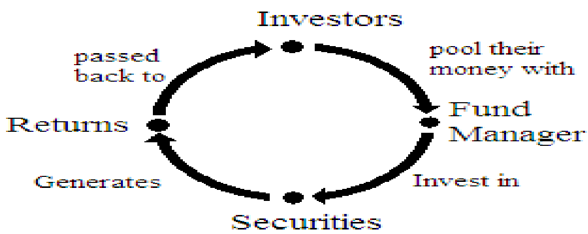
Introduction

With reforms in financial sector and the developments in the Indian financial markets, Mutual Funds (MFs) have emerged to be an important investment avenue for retail (small) investors. Investors' of mutual funds are known as unit holders. A fund is "mutual" as all of its returns, minus its expenses, are shared by the fund's investors. The Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 defines a



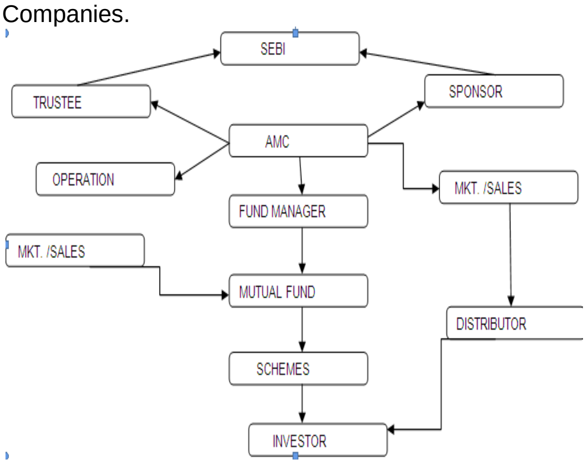
mutual fund as a 'a fund established in the form of a trust to raise money through the sale of units to the public or a section of the public under one or more schemes for investing in securities, including money market instruments'. The mutual funds normally come out with a number of schemes with different investment objectives which are launched from time to time.

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

Organization structure of mutual funds

Mutual funds have organization structure as per the Security Exchange Board of India guideline; Security Exchange Board of India specified authority and responsibility of Trustee and Asset Management Companies. The objective is to control, to promote, to regulate, to protect the investor's right and efficient trading of units.

The Mutual fund organization as per the SEBI formation and necessary formation is needed for sooth activities of the companies and achieved the desire objectives. Transfer agent and custodian play role for dematerialization of the fund and unit holders hold the account statement, but custody of the unit is on particular Asset Management Company. Custodian holds all the fund units on dematerialization form. Sponsor had decided the responsibility of custodian when investor to purchase the fund and to sell the unit. Application forms, transaction slip and other requests received by transfer agent, middle men between investors and Assts Management Companies.



Valuation of mutual fund

The net asset value of the Fund is the cumulative market value of the assets Fund net of its liabilities. In other words, if the Fund is dissolved or liquidated, by selling off all the assets in the Fund, this is the amount that the shareholders would collectively own. This gives rise to the concept of net asset value per unit, which is the value, represented by the ownership of one unit in the Fund. It is calculated simply by dividing the net asset value of the Fund by the number of units.

Calculation of NAV

The net asset value of a fund is the market value of the assets minus the liabilities on the day of valuation. In other words, it is the amount which the shareholders will collectively get if the fund is dissolved or liquidated. The net asset value of a unit is the net asset value of fund divided by the number of outstanding units. Thus NAV = Market Price o f Securities + Other Assets – Total Liabilities + Units Outstanding as at the NAV date. NAV = Net Assets of the Scheme + Number of units outstanding, that is, Market value of investments + Receivables + Other Accrued Income + Other Assets - Accrued Expenses - Other Payables - Other Liabilities + No. of units outstanding as at the NAV date. 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. Mutual funds are required to declare their NAVs and sale repurchase prices of all schemes updated daily on regular basis on the AMFI website by 8.00 p.m. and declare NAVs of their close-ended schemes on every Wednesday. For most funds, the NAV is determined daily, after the close of trading on some specified financial exchange, but some funds update their NAV multiple times during the trading day. Open-end funds sell and redeem their shares at the NAV, and so process orders only after the NAV are determined. Closed-end funds (the shares of which are traded by investors') may trade at a higher or lower price than their NAV; this is known as a premium or discount, respectively. If a fund is divided into multiple classes of shares, each class will typically have its own NAV, reflecting differences in fees and expenses paid by the different classes.

Types of mutual funds

The objectives of mutual funds are to provide continuous liquidity and higher yields with high degree of safety to investors. Based on these objectives, different types of mutual fund schemes have evolved.

- **Functional Classification of Mutual Funds**

1. **Open-ended schemes**: In case of open-ended schemes, the mutual fund continuously offers to sell and repurchase its units at net asset value (NAV). Unlike close-ended schemes, open-ended ones do not have to be listed on the stock exchange. Investors can enter and exit the scheme any time during the life of the fund. There is no fixed redemption period in open-ended schemes, which can be terminated whenever the need arises. The fund offers a redemption price at which the holder can sell units to the fund and exit. Besides, an investor can enter the fund again by buying units from the fund at its offer price. Such funds announce sale and repurchase prices from time-to-time. UTI's US-64 scheme is an example of such a fund. The key feature of open-ended funds is liquidity. They increase liquidity of the investors as the units can be continuously bought and sold.
2. **Close-ended schemes**: Close-ended schemes have a fixed corpus and a stipulated maturity period ranging between 2 to 5 years. Investors can invest in the scheme when it is launched. The scheme remains open for a period not exceeding 45 days. Investors in close-ended schemes can buy units only from the market, once initial subscriptions are over and thereafter the units are listed on the stock exchanges where they can be bought and sold. The fund has no interaction with investors till redemption except for paying dividend/bonus. Some close-ended funds give an option of selling back the units to the mutual fund through periodic repurchase at NAV related prices. If an investor sells units directly to the fund, he cannot enter the fund again, as units bought back by the fund cannot be reissued. The close-ended scheme can be converted into an open-ended one.

3. **Interval scheme**: Interval scheme combines the features of open-ended and close-ended schemes.
   They are open for sale or redemption during predetermined intervals at NAV related prices.

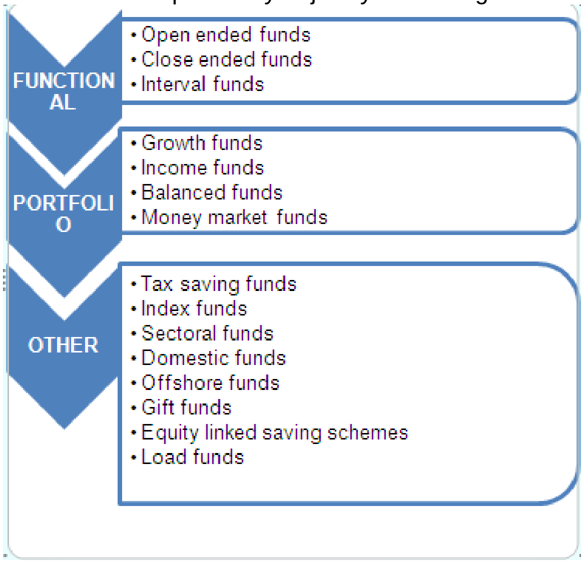
- **Portfolio Classification of Mutual Funds**

Here, classification is on the basis of nature and types of securities and objective of investment.

1. **Growth funds:** The main objective of growth funds is capital appreciation over the medium-to-long- term. They invest most of the corpus in equity shares with significant growth potential and they offer higher return to investors in the long-term. They assume the risks associated with equity investments. There is no guarantee or assurance of returns. These schemes are usually close-ended and listed on stock exchanges.
2. **Income funds**: The aim of income funds is to provide safety of investments and regular income to investors. Such schemes invest predominantly in income-bearing instruments like bonds, debentures, government equities, and commercial paper. The return as well as the risk are lower in income funds as compared to growth funds.
3. **Balanced funds**: The aim of balanced scheme is to provide both capital appreciation and regular income. They divide their investment between equity shares and fixed nice bearing instruments in such a proportion that, the portfolio is balanced. The portfolio of such funds usually comprises of companies with good profit and dividend track records. Their exposure to risk is moderate and they offer a reasonable rate of return.
4. **Money market mutual funds**: They specialise in investing in short-term money market instruments like treasury bills, and certificate of deposits. The objective of such funds is high liquidity with low rate of return.

- **Other Classification of Mutual Funds**

1. **Tax saving schemes:** Tax-saving schemes are designed on the basis of tax policy with special tax incentives to investors. Mutual funds have introduced a number of tax saving schemes. These are close--ended schemes and investments are made for ten years, although investors can avail of encashment facilities after 3 years. These schemes contain various options like income, growth or capital application.
2. **Index funds:** An index fund is a mutual fund which invests in securities in the index on which it is based BSE Sensex or S&P CNX Nifty. It invests only in those shares which comprise the market index and in exactly the same proportion as the companies/weightage in the index so that the value of such index funds varies with the market index. An index fund follows a passive investment strategy as no effort is made by the fund manager to identify stocks for investment/dis-investment. The fund manager has to merely track the index on which it is based. His portfolio will need an adjustment in case there is a revision in the underlying index. In other words, the fund manager has to buy stocks which are added to the index and sell stocks which are deleted from the index. Internationally, index funds are very popular. Around onethird of professionally run portfolios in the US are index funds. Empirical evidence points out that active fund managers have not been able to perform well. Only 20-25% of actively managed equity mutual funds out-perform benchmark indices in the long-term. These active fund managers park 80% of their money in an index and do active management on the remaining 20%. Moreover, risk averse investors like provident funds and pension funds prefer investment in passively managed funds like index funds.
3. **Sectoral:** These funds invest in specific core sectors like energy, telecommunications, IT, construction, transportation, and financial services. Some of these newly opened-up sectors offer good investment potential.
4. **Domestic funds**: Funds which mobilise resources from a particular geographical locality like a country or region are domestic funds. The market is limited and confined to the boundaries of a nation in which the fund operates. They can invest only in the securities which are issued and traded in the domestic financial markets.
5. **Offshore funds**: Offshore funds attract foreign capital for investment in the country of the issuing company. They facilitate cross-border fund flow which leads to an increase in foreign currency and foreign exchange reserves. Such mutual funds can invest in securities of foreign companies. They open domestic capital market to international investors. Many mutual funds in India have launched a number of offshore funds, either independently or jointly with foreign



funds, either independently or jointly with foreign investment management companies. The first offshore fund, the India Fund, was launched by

Unit Trust of India in July 1986 in collaboration with the US fund manager, Merril Lynch.

6. **Gilt funds:** Mutual funds which deal exclusively in gilts are called gilt funds. With a view to creating a wider investor base for government securities, the Reserve Bank of India encouraged setting up of gilt funds. These funds are provided liquidity support by the Reserve Bank.
7. **Equity-linked savings scheme (ELSS):** In order to encourage investors to invest in equity market, the government has given tax-concessions through special schemes. Investment in these schemes entitles the investor to claim an income tax rebate, but these schemes carry a lock-in period before the end of which funds cannot be withdrawn.

Load funds

Mutual funds incur certain expenses such as brokerage, marketing expenses, and communication expenses. These expenses are known as 'load' and are recovered by the fund when it sells the units to investors or repurchases the units from withholders. Loads can be of two types-Front-end-load and back-end-load. Front-end-load, or sale load, is a charge collected at the time when an investor enters into the scheme. Back-end, or repurchase, load is a charge collected when the investor gets out of the scheme. Schemes that do not charge a load are called 'No load' schemes.

How to choose a mutual fund

Step 1
Determine the investment objectives and time frame. the longer the time horizon, more will be the risk.

Step 2
Identify which type of funds match your goals and risk tolerance.

Step 3
Once appropriate category is decided, now choose an individual fund.bear in mind that the past performance doesn't guarantee future returns.

Various schemes of mutual funds

They can be broadly classified into Government securities and Industrial securities. The **Government securities** are fixed income securities backed by the government and there is no risk of default. The Major Instruments that fall under **Industrial Securities** are Debentures, Preference Shares and Equity Shares. In other words, the industrial securities are about the stock market and mutual funds.

- **Government securities(G-SEC)**

In India G-Secs are issued by the Central Government, State Governments and Semi Government Authorities such as municipalities, port trusts, state electricity boards and public sector corporations. The Central and State Governments raise money through these securities to finance the creation of new infrastructure as well as to meet their current cash needs. The risk of default is minimal. These securities may have maturities ranging from five to twenty years. These are fixed income securities, which pay interest every six months. The Reserve Bank of India manages the issues of the securities. These securities are sold in the primary market mainly through the auction mechanism. Prospective buyers submit their bids. The RBI decides to accept bids based on a cut off price.

- **Call money market**

The loans made in this market are of a short term nature – overnight to a fortnight. This is mostly inter-bank market. Those banks which are facing a short term cash deficit, borrow funds from the cash surplus banks. The rate of interest is market driven and depends on the liquidity position in the banking system.

- **Commercial paper(CP) and Certificate of deposits(CD)**

These are issued for short term maturities. These are issued at a discount and redeemed at face value. These are unsecured and therefore only those companies who have a good credit standing are able to access funds through this instrument. The rate of interest is market driven and depends on the current liquidity position and the creditworthiness of the issuing company.

- **Industrial securities**

These are securities issued by the corporate sector to finance their long term and working capital requirements. The Major Instruments that fall under Industrial Securities are: Debentures, Preference Shares And Equity Shares.

- **Debentures**

Debentures have a fixed maturity and pay a fixed or a floating rate of interest during their lifetime. The company has an obligation to pay interest and the principal amount on the due dates regardless of its profitability position. Since these carry a predefined rate of return, there is no scope for any major capital appreciation. However, in case of fixed rate debentures, their market price moves inversely with the direction of interest rates.

- **Preference shares**

Preference Shares carry a fixed rate of dividends. These carry a preferential right to dividends over the equity shareholders. Similarly on the winding up of the company, the preference share holders get back their capital before the equity share holders. In case of cumulative preference shares, any dividend unpaid in past years accumulates and is paid later when the company has sufficient profits. Now all preference shares in India are `redeemable', i.e. they have a fixed maturity period. Thus, preference shares are sometimes called a `hybrid variety' – incorporating features of debt as well as equity.

- **Equity shares**

Equity Shares are regarded as high return high risk instruments. These do not carry any fixed rate of return and there is no maturity period. The company may or may not declare dividend on equity shares. The major component of return to equity holders usually consists of market appreciation.

- **Equity or growth scheme**

These schemes seek to invest a majority of their funds in equities and a small portion in money market instruments. Such schemes have the potential to deliver superior returns over the long term. However, because they invest in equities, these schemes are exposed to fluctuations in value especially in the short term.

- **Balanced scheme**

The aim of Balanced Funds is to provide both growth and regular income. Such schemes periodically distribute a part of their earning and invest both in equities and fixed income securities in the proportion indicated in their offer documents. This proportion affects the risks and the returns associated with the balanced fund - in case equities are allocated a higher proportion, investors would be exposed to risks similar to that of the equity market. Balanced funds with equal allocation to equities and fixed income securities are ideal for investors looking for a combination of income and moderate growth.

Before the launching of schemes:

Before the launching of different schemes, a scheme has to be approved by the trustees and a copy of its offer documents filed with the SEBI. Every application form for units of a scheme is to be accompanies by a memorandum containing key information about the scheme. The offer document needs to contain adequate information to enable the investors to make informed investments decisions. All advertisements for a scheme have to be submitted to SEBI within seven days from the issue date. The advertisements for a scheme have to disclose its investment objective. The offer documents and advertisements could not contain any misleading information or any incorrect statement or opinion. The initial offering period for any mutual fund schemes could not exceed 45 days, the only exception being the equity linked saving schemes. No advertisements can contain information whose accuracy is dependent on assumption. An advertisement cannot carry a comparison between two schemes unless the schemes are comparable and all the relevant information about the schemes is given. All advertisements need to carry the name of the sponsor, the trustees, the AMC of the fund. All advertisements need to clarify that investment in mutual funds is subject to market risk and the achievement of the fund's objectives cannot be assured. When a scheme is open for subscription, no advertisement can be issued stating that the scheme has been subscribed or over subscription.

Role of SEBI

A mutual fund may enter into short selling transactions on a recognized stock exchange, subject to the framework relating to short selling and securities lending and borrowing specified by the Board. SEBI Regulation Act 1996 Establishment of a Mutual Fund: In India mutual fund play the role as investment with trust, some of the formalities laid down by the SEBI for setting up a mutual fund. As the part of trustee sponsor the mutual fund, under the Indian Trust Act, 1882, under the trustee company are represented by a board of directors. Board of Directors appoints the AMC and custodians. The board of trustees made relevant agreement with AMC and custodian. The launch of each scheme involves inviting the public to invest in it, through an offer documents. Depending on the particular objective of scheme, it may open for further sale and repurchase of units, again in accordance with the particular of the scheme, the scheme may be wound up after the particular time period.

1. The sponsor has to register the mutual fund with SEBI
2. To be eligible to be a sponsor, the body corporate should have a sound track record and a general reputation of fairness and integrity in all his business transactions.

   Sound Track Records means:

- The body corporate being in the financial services business for at least five years.
- Having a positive net worth in the five years immediately preceding the application of registration.
- Net worth in the immediately preceding year more than its contribution to the capital of the AMC.
- Earning a profit in the three out of the five preceding years, including the fifth year.

3. The sponsor should hold at least 40% of the net worth of the AMC.
4. A party which is not eligible to be a sponsor shall not hold 40% or more of the net worth of the AMC.
5. The sponsor has to appoint the trustees, the AMC and the custodian.
6. An AMC or its officers or employees can not be appointed as trustees of the mutual fund.
7. At least two thirds of the business should be independent of the sponsor.
8. Only an independent trustee can be appointed as a trustee of more than one mutual fund, such appointment can be made only with the prior approval of the fund of which the person is already acting as a trustees.

Role of AMFI (Association Mutual Fund in India)

The Association of Mutual Funds in India (AMFI) is dedicated to developing the Indian Mutual Fund Industry on professional, healthy and ethical lines and to enhance and maintain standards in all areas with a view to protecting and promoting the interests of mutual funds and their unit holders. AMFI, the association of SEBI registered mutual funds in India of all the registered management companies was incorporated on august 22, 1995; as a non profit organization.

Following are Assets Management Companies under India: AEGON Asset Management Company Pvt. Ltd., Axis Asset Management Company Ltd., Benchmark Asset Management Company Pvt. Ltd., Escorts Asset Management Ltd., HDFC Asset Management Company Ltd., ICICI Prudential Asset Management Company Ltd., LIC Mutual Fund Asset Management Company Ltd. etc.

Comparison between investment in banks and mutual funds

If someone wants to invest for the future, he will generally have two options i.e. Mutual fund and banks. He has to choose between the two. Both carry inherent advantages and risks at the same time. Thus the differences between these two are very important

If any new investor is looking to invest in Mutual Fund financial position, risk tolerance and return expectations etc. of the various schemes are to be essentially studied. He has to opt for such a scheme that minimizes risk and maximizes returns.

Particulars	**Banks**	**Mutual funds**
Liquidity	At a cost	Better
Risk	Low	Moderate
Returns	Low	Better
Interest calculation	Minimum balance between 10th and 30th of every month	Everyday
Assets	Not transparent	Transparent
Administrative expenses	High	Low
Investment options	Less	more

Mutual fund investors

Mutual funds in India are open to investment by residents, Non-Residents and Foreign entities. Foreign citizens/ entities are however not allowed to invest in mutual funds in India.

RESIDENTS

- Individuals
- Indian companies
- Indian trusts
- Banks
- Insurance companies
- Provident funds
- Non banking finance companies

NON-RESIDENTS

- Non-resident indians
- Other corporate bodies

FOREIGN ENTITIES

- Foreign institutional investors registered with SEBI

Growth of Mutual Funds in India

The growth of the mutual fund industry in India can be divided into four phases: Phase I (1964-87), Phase II (1987-92), Phase III (1992-97), and Phase IV (beyond 1997).

Phase I

The Unit Trust of India (UTI) was the first mutual fund set up under the UTI Act, 1963. It became operational in 1964 with a major objective of mobilising savings through the sale of units and investing them in corporate securities for maximising yield and capital appreciation. UTI's investible funds, at market value (and including the book value of fixed assets) grew from Rs 49 crore in1965 to Rs 219 crore in 1970-71 to Rs 1,126 crore in 1980-81 and further to Rs 5,068 crore by June 1987. Its investor base had also grown to about 2 million investors. Master share, the equity growth fund launched in 1986, proved to be a grand marketing success. Master share was the first real close-ended scheme floated by UTI.

Phase II

In 1987, SBI Mutual Fund and Canbank Mutual Fund were set up as trusts under the Indian Trust Act, 1882. By 1990, the two nationalised insurance giants, LIC and GIC, and nationalised banks, namely, Indian Bank, Bank of India, and Punjab National Bank had started operations of wholly-owned mutual fund subsidiaries. With the entry of public sector funds, there was a tremendous growth in the size of the mutual fund industry with investible funds, at market value, increasing to Rs 53,462 crore and the number of investors increasing to over 23 million.

Phase III

The year 1993 marked a turning point in the history of mutual funds in India. Private domestic and foreign players were allowed entry in the mutual fund industry. Kothari group of companies, in joint venture with Pioneer, a US fund company, set up the first private mutual fund the Kothari Pioneer Mutual Fund, in 1993. Several other private sector mutual funds were set up during this phase. UTI launched a new scheme, Master-gain, in May 1992, which was a phenomenal success with a subscription of Rs 4,700 crore from 631akh applicants. A lack of performance of the public sector funds and miserable failure of foreign funds like Morgan Stanley eroded the confidence of investors in fund managers. The average annual sales declined from about Rs 13,000 . crore in 1991-94 to about Rs 9,000 crore in 1995 and 1996.

Phase IV

During this phase Investible funds, at market value, of the industry rose by June 2000 to over Rs 1,10,000 crore with UTI having 68% of the market share. During 1999-2000 sales mobilisation reached a record level of Rs 73,000 crore as against Rs 31,420 crore in the preceding year. This trend was, however, sharply reversed in 2000-01. The Indian mutual fund industry has stagnated at around Rs 1,00,000 crore assets since 2000-01.

Vision- 2020 for mutual fund in India

This section contains a summary of the expected drivers for future growth, expected industry growth projections and overall future outlook across various dimensions customers, markets, products, distribution channels and regulatory frameworks. Although several macroeconomic and demographic factors affect the growth of the industry, the key underlying driver for all the categories of funds is the key economic indicator – the GDP growth rate. Increase in disposable incomes and household financial savings may result in households seeking alternate avenues for investments to yield higher returns with reasonable risk. Distribution innovations are expected to increased mutual fund penetration specifically in Tier 2 and Tier_3 towns thereby expanding the mutual fund customer base. Improved awareness levels and enhanced financial literacy is expected to aid the understanding of mutual fund products.

Benefits of Mutual Funds

Mutual funds are currently the most popular investment vehicle and provide several advantages to investors. The advantages of mutual funds include professional management, diversification, variety, liquidity, affordability, convenience, strict government regulation and full disclosure. An investor can invest directly in individual securities or indirectly through a financial intermediary. Globally, mutual funds have established themselves as the means of investment for the retail investor. The benefits of mutual funds are as follows:

- **Portfolio diversification**: An investor undertakes risk if he invests all his funds in a single scrip. Mutual funds invest in a number of companies across various industries and sectors. This diversification reduces the riskiness of the investments. Mutual Funds invest in a well-diversified portfolio of securities which enables investor to hold a diversified investment portfolio (whether the amount of investment is big or small).
- **Dividend Reinvestment:** As dividends and other interest income is declared for the fund, it can be used to purchase additional shares in the mutual fund.
- **Convenience:** Mutual funds are common and easy to buy. Investing in mutual fund reduces paperwork, saves time and makes investment easy.
- **Risk Reduction (Safety):** Mutual Fund industry is part of a well-regulated investment environment where the interests of the investors are protected by the regulator. All funds are registered with SEBI and complete transparency is forced.
- **Professional management:** An average investor lacks the knowledge of capital market operations and does not have large resources to reap the benefits of investment. Hence, he requires the help of an expert. It, is not only expensive to 'hire the services' of an expert but it is more difficult to identify a real expert. Thus investors in mutual funds allow a qualified professional with advanced training and expertise to manage their money.They make possible an organised investment strategy, which is hardly possible for an individual investor. Fund manager undergoes through various research works and has better investment management skills which ensure higher returns to the investor than what he can manage on his own.
- **Low Transaction Costs**: Compared to direct investing in the capital market, investing through the funds is relatively less expensive. Due to the economies of scale (benefits of larger volumes), mutual funds pay lesser transaction costs. These benefits are passed on to the investors.
- **Liquidity:** An investor may not be able to sell some of the shares held by him very easily and quickly, while in case of mutual funds, they can easily encash their investment by selling their units to the fund if it is an open-ended scheme or selling them on a stock exchange if it is a close-ended scheme.
- **Choice of Schemes:** Mutual funds provide investors with various schemes with different investment objectives. Investors have the option of investing in a scheme having a correlation between its investment objectives and their own financial goals. These schemes further have different plans/options
- **Advanced Portfolio Management:** Investors pay management fee which is used to hire a professional portfolio manager who buys and sells stocks, bonds, etc. This is a relatively small price to pay for help in the management of an investment portfolio.
- **Transparency** Mutual funds transparently declare their portfolio every month. All material facts are disclosed to investors as required by the regulator. Thus an investor knows where his/her money is being deployed and in case they are not happy with the portfolio they can withdraw at a short notice.
- **Flexibility:** Investors also benefit from the convenience and flexibility offered by Mutual

Funds. Investors can switch their holdings from a debt scheme to an equity scheme and vice-versa. Option of systematic (at regular intervals) investment and withdrawal is also offered to the investors in most open-end schemes.

- **Stability to the stock market:** Mutual funds have a large amount of funds which provide them economies of scale by which they can absorb any losses in the stock market and continue investing in the stock market. In addition, mutual funds increase liquidity in the money and capital market.
- **Equity research** Mutual funds can afford information and data required for investments as they have large amount of funds and equity research teams available with them.

Drawbacks associated with mutual funds

The mutual fund not just advantage of investor but also has disadvantages for the funds. The fund manager not always made profits but might creates loss for not properly managed. The fund have own strategy for investment to hold, to sell, to purchase unit at particular time period. However, there are also disadvantages of mutual funds, such as the following:

- **High Expense Ratios and Sales Charges:** Investor has to pay investment management fees and fund distribution costs as a percentage of the value of his investments (as long as he holds the units), irrespective of the performance of the fund. If attention is not paid to mutual fund expense ratios and sales charges, they can get out of hand. He has to be very cautious when investing in funds with expense ratios higher than 1.20%, as they will be considered on the higher cost end.
- **Management Abuses:** Churning, turnover and window dressing may happen if manager is abusing his or her authority. This includes unnecessary trading, excessive replacement and selling the losers prior to quarter-end to fix the books.
- **Difficulty in Selecting a Suitable Fund Scheme**

Many investors find it difficult to select one option from the plethora of funds/schemes/plans available. For this, they may have to take advice from financial planners in order to invest in the right fund to achieve their objectives.

- **No Customized Portfolios**

The portfolio of securities in which a fund invests is a decision taken by the fund manager. Investors have no right to interfere in the decision making process of a fund manager.

- **Tax Inefficiency:** Due to the turnover, redemptions, gains and losses in security holdings throughout the year, investors typically receive distributions from the fund that are an uncontrollable tax event.
- **Trading Limitations**: Although mutual funds are highly liquid in general, most mutual funds (called open-ended funds) cannot be bought or sold in the middle of the trading day. You can only buy and sell them at the end of the day, after they've calculated the current value of their holdings.
- **Inefficiency of Cash Reserves**: Mutual funds usually maintain large cash reserves as protection against a large number of simultaneous withdrawals. Although this provides investors with liquidity, it means that some of the fund's money is invested in cash instead of assets, which tends to lower the investor's potential return.
- **Loss of Control**: The managers of mutual funds make all of the decisions about which securities to buy and sell and when to do so. This can make it difficult for you when trying to manage your portfolio. For example, the tax consequences of a decision by the manager to buy or sell an asset at a certain time might not be optimal for you. You also should remember that you are trusting someone else with your money when you invest in a mutual fund.
- **Poor Trade Execution:** If you place your mutual fund trade anytime before the cut-off time for same-day NAV, you'll receive the same closing price NAV for your buy or sell on the mutual fund. For investors looking for faster execution times, maybe because of short investment horizons, day trading, or timing the market, mutual funds provide a weak execution strategy.
- **No Insurance**: Mutual funds, although regulated by the government, are not insured against losses. The Federal Deposit Insurance Corporation (FDIC) only insures against certain losses at banks, credit unions, and savings and loans, not mutual funds. That means that despite the risk-reducing diversification benefits provided by mutual funds, losses can occur, and it is possible (although extremely unlikely) that you could even lose your entire investment.
- **Dilution**: Although diversification reduces the amount of risk involved in investing in mutual funds, it can also be a disadvantage due to dilution. For example, if a single security held by a mutual fund doubles in value, the mutual fund itself would not double in value because that security is only one small part of the fund's holdings. By holding a large number of different investments, mutual funds tend to do neither exceptionally well nor exceptionally poorly.

Conclusion

Mutual funds are the most preferred investment instruments. For middle income individuals, investing in mutual funds yields higher interest and comes with good principal amount at the end of the maturity period of the mutual fund investment. Another important fact is that mutual funds are safe, with close to zero risk. The mutual fund is run by a fund manager who is responsible for the buying and selling of investments in accord with the investment objectives of the fund. As far as the benefits provided by mutual funds are concerned, return potential and liquidity have been perceived to be most attractive by the invertors' followed by flexibility, transparency and affordability. Apart from the above, in India there is a lot of scope for the growth of mutual fund companies provided that the funds satisfy everybody's needs and sharp improvements in service standards and disclosure. Mutual funds have opened new vistas to millions of small investors by virtually taking investment to their doorstep. In India, a small investor generally goes for such kind of information, which do not provide hedge against inflation and often have negative real returns. Mutual funds have come, as a much needed help to these investors. But the study shows that most of respondents are still confused about the mutual funds and have not formed any attitude towards the mutual fund for investment purpose. It has been observed that most of the respondents having lack of awareness about the various function of mutual funds. Moreover, as far as the demographic factors are concerned, gender, income and level of education have significantly influence the investors' attitude towards mutual funds. On the other hand the other two demographic factors like age and occupation have not been found influencing the attitude of investors' towards mutual funds. Some steps should be taken to give information to the public about mutual funds.

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