# <u>MUTUAL FUNDS</u>

<u>A CHANGE IN INDIAN INVESTMENT PERSPECTIVE</u>

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Mutual Funds have become a new 'Mantra' for Indian Investors. Mutual Funds market plays a predominant role on par with other investment instruments. There has been a tremendous shift from traditional investment avenues like N.S.C. and P.P.F. etc to Mutual Funds and this trend is rapidly increasing day-by-day.

With in a span of 6 years, the total assets under management in Mutual Funds Industry have grown from Rs. 68,000 crores to Rs.1,50,000 crores and this clearly indicates the potential development and growth of Mutual Funds Industry.

Traditionally, Indian Investors invests in Bank Deposits, P.P.F, N.S.C and K.V.P. etc. The beginning era of market determined economy in 1990 started the decline in the highly assured returns and at present the interest rate remained constant at 8% on the instruments like N.S.C. and P.P.F. and other Postal Saving Schemes.

Though the aforesaid rate of return is completely free from any risk (which is suitable to risk averse investors), an investor with risk appetite may think this rate of return is far from that what has been yielded by the several schemes of Mutual Funds now-a-days. At present K.V.P. doubles the money in 8 years 7 months. But some Mutual Fund schemes witnessed that the money contributed was doubled in its value with in a span of 3 years. However, investments in Mutual Funds are subject to market risk.

With the formulation of Mutual Fund Regulations in 1996 and other stringent regulations, Mutual Fund Industry, being continuously monitored by SEBI and other Regulatory Authorities like Association of Mutual Funds in India (AMFI), became the leading platform for wealth generation, return yielding (in the form dividend and capital gains), financial and tax planning.

Mutual Funds are of several types like open-ended and close-ended funds, load and no-load funds, equity oriented and debt oriented funds, balanced funds, sector funds, Tax saving funds (popularly known as ELSS), opportunities funds, mid cap and small cap funds, index funds, fund of funds, Monthly Income Plans etc.,

Several schemes are being designed by Mutual Fund Companies to cater to the needs of different types of investors according to their level of income, risk profile, age group, tax benefits, liquidity requirements (i.e. lock-in period, if any) etc., One of the major reasons for the risk taking investor to get attracted into Mutual Fund Investment Avenues is the impressive return that has been yielded by several Mutual Fund Schemes especially diversified equity funds and tax saving funds (ELSS) with a CAGR (Compounded Annualized Growth Rate) ranging from 60% to 90%. Another benefit of investing in Mutual Funds is the risk diversification because Mutual Funds invest in well-diversified portfolio of securities.

If a person wants to invest in Securities Market like equity shares, he has to carefully calculate risk and build his portfolio in such a way that his risk is diversified to a maximum extent possible. But in this dynamic environment, an investor, who does not have much time to devote for this task and already preloaded with his assignments, can transfer this task by investing in Mutual Funds to a fund manager who got professional competence to handle this task.

Along with high returns, investors can also get tax benefits in the form of deduction under sec. 80C of the Income Tax Act by investing in ELSS. However, investment in ELSS Schemes will be kept in lock for a period of 3 years. Before going to invest in an ELSS Scheme, it is recommendable to compare the funds by appraising the returns for the last 3 years instead of going by 1 year. Also the measures of the risk such as SD (Standard Deviation) and ratios like Sharpe Ratio and Treynor Index can be used to evaluate different types of funds. Examples of some of the tax saving funds are SBI Magnum Tax Gain, HDFC Tax Saver, Sundaram Tax Saver, TATA Tax Saving Fund, Birla Equity Plan, PRU ICICI Tax Plan, HDFC LT Advantage Fund.

As the sectoral caps have been removed by Finance Act 2005 with the removal of rebate u/s 88 and introduction of deduction u/s 80C, investor has the opportunity to invest to avail the tax benefits to a maximum extent of Rs. 1 lakh in whatever tax saving funds he wants according his investment taste and risk-return profile. Also this favours a rational investor to follow the old saying "Don't put all eggs in one basket".

Generally, NFOs doen't charge any load so that investment of Rs.10,000/- by an investor will fetch him 1000 units at the @ 10/- per unit. An open-ended fund may charge load (entry or exit) as per the terms and conditions of the scheme subject to specified regulations. Some of the schemes may follow to charge the load on a differed basis known as CDSC (Contingent Differed Sales Charge).

One of the significant features of Mutual Fund is that the Mutual Fund offers greater flexibility in the minimum amount required to be invested. There are certain funds, which offer schemes with minimum amount of investment, as least as possible say Rs. 500/-. Example: DSP Merrill Lynch Tax Saver Fund.

With this flexibility even smaller and lower income people also can route their household savings into these types of funds and earn a reasonable rate of return along with tax benefits. So, if a Tax Payer estimates this his total income will be only Rs. 1,04,000/-, he can simply invest Rs. 4,000/- and get out of the tax net.

Even a risk averse investor can go for Mutual Funds by investing in lower risk funds which comprises a greater portion of it's portfolio in debt instruments. Example : Franklin India Capital Safety Fund.

At the time of investment investor has to choose one of the three options i.e., growth, dividend payout, dividend reinvestment. Those with higher risk appetite can opt for the growth option, which takes into account the benefit of effect of compounding. Dividend payout ensures the investors to get periodical dividends, which enable them to crystallize the profit so made by the fund. On the other hand dividend re-investment converts the dividend amounts into units calculated at the NAV prevailing on the relevant date. Switch over facility between the options will also be available to investor.

Systematic Investment Plan (SIP) and Systematic Withdrawal Plan (SWP) are also of important increasing trend in Mutual Fund Industry. SIP enforces discipline among the investors in saving the money for the future requirements and enables them to contribute to the fund in monthly installments instead of making one time payment of lump sum amount. This type of investment option gives greater flexibility to the investors especially salaried employees. In the similar way SWP enables an investor to systematically withdraw his money from the fund. SIP also takes in to account the effect of averaging.

So far as the tax considerations are taken into account, Long term Capital Gains on equity funds are exempt u/s 10(38) of the Income Tax Act. Short term Capital Gains are chargeable to tax at a lower rate of 10%. Whereas the debt funds are considered, Short term Capital Gains are chargeable to tax at the corresponding slab rate applicable to the taxpayer. Long term Capital Gains are taxable @ 10% without the benefit of indexation or 20% with the benefit of indexation.

For the purpose of advice with regard to the financial planning and information regarding Mutual Funds, investors can take the help of Mutual Fund advisors (AMFI Certified Mutual Fund advisors) who can provide them value added services. Fortunately, there are large number of registered Mutual Fund Advisors and Financial Planners in India.

In this view Mutual Fund plays a leading role in Indian Investment scenario and is becoming a strong and potential base for Indian Economy.