INVESTMENT STRATEGIES OF POTENTIAL INVESTORS IN MUTUAL FUNDS

Iqbal, Naila

Dept. of Management, Rajiv Gandhi College , Bhopal (M.P),INDIA

ABSTRACT

Mutual funds provide access to expert managers who make and monitor the investment selections as dictated by the fund's strategy. Strategies can range from a defined financial objective, such as growth or income, to an investment theme like global or health care investing. Because mutual fund investors also share the costs of managing the fund, even new investors can access the same caliber of expert money management and portfolio diversification that larger investors and institutions obtain when they assemble their own portfolios of individual securities.

Growth and development of various mutual fund products in Indian capital market has proved to be one of the most catalytic instruments in generating momentous investment growth in the capital market. There is a substantial growth in the mutual fund market due to a high level of precision in the design and marketing of variety of mutual fund products by banks and other financial institution providing growth, liquidity and return.

KEYWORDS: Investment strategies, NAV, Association of Mutual Funds, potential investors, Systematic investment plan, Value added services and Offer document.

INTRODUCTION

Mutual Funds can provide investors with access to the expertise of professional money managers, sophisticated strategies and well-diversified portfolios. A mutual fund Product is a group of stocks, bonds or other securities that has been pooled together and is then sold in pieces called shares. The entire product line offered by a mutual fund company is considered its family. The significant outcome of the government policy of liberalization in industrial and financial sector has been the development of new financial instruments like Mutual Funds. These new instruments are expected to impart greater competitiveness flexibility and efficiency to the financial sector.

In this context, prioritization, preference building and close monitoring of mutual funds are essentials for fund managers to make this the strongest and most preferred instrument in Indian capital market for the coming years. With the decline in the bank interest rates, frequent fluctuations in the secondary market and the inherent attitude of Indian small investors to avoid risk, it is important on the part of fund managers and mutual fund product designers to combine various elements of liquidity, return and security in making mutual fund products the best possible alternative for the small investors in Indian market.

INVSETMENT STRATEGIES OF POTENTIAL INVESTORS

Investors' insight into an offer document an abridged offer document, which contains very useful information, is required to be given to the prospective investor by the mutual fund. The application form for subscription to a scheme is an integral part of the offer document. SEBI has prescribed minimum disclosures in the offer document. An investor, before investing in a scheme, should carefully read the offer document. Due care must be given to portions relating to main features of the scheme, risk factors, initial issue expenses and recurring expenses to be charged to the scheme, entry or exit loads, sponsor's track record, educational qualification and work experience of key personnel including fund managers, performance of other schemes launched by the mutual fund in the past, pending litigations and penalties imposed, etc. Mutual funds are required to dispatch certificates or statements of accounts within six weeks from the date of closure of the initial subscription of the scheme. In case of close-ended schemes, the investors would get either a Demat account statement or unit certificates as these are traded in the stock exchanges. In case of open-ended schemes, a statement of account is issued by the mutual fund within 30 days from the date of closure of initial public offer of the scheme. The procedure of repurchase is mentioned in the offer document.

According to SEBI Regulations, transfer of units is required to be done within thirty days from the date of lodgment of certificates with the mutual fund. A mutual fund is required to dispatch to the unit holders the dividend warrants within 30 days of the declaration of the dividend and the redemption or repurchase proceeds within 10 working days from the date of redemption or repurchase request made by the unit holder. In case of failures to dispatch the redemption/repurchase proceeds within the stipulated time period, Asset Management Company is liable to pay interest as specified by SEBI from time to time (15% at present). There may be changes from time to time in a mutual fund. The mutual funds are required to inform any material changes to their unit holders. Apart from it, many mutual funds send quarterly newsletters to their investors. At present, offer documents are required to be revised and updated at least once in two years. In the meantime, new investors are informed about the material changes by way of addendum to the offer document till the time offer document is revised and reprinted.

The performance of a scheme is reflected in its net asset value (NAV) which is disclosed on daily basis in case of open-ended schemes and on weekly basis in case of close-ended schemes. The NAVs of mutual funds are required to be published in newspapers. The NAVs are also available on the web sites of mutual funds. All mutual funds are also required to put their NAVs on the web site of Association of Mutual Funds in India (AMFI) and thus the investors can access NAVs of all mutual funds at one place. The mutual funds are also required to publish their performance in the form of half-yearly results which also include their returns/yields over a period of time i.e. last six months, 1 year, 3 years, 5 years and since inception of schemes. Investors can also look into other details like percentage of expenses of total assets as these have an effect on the yield and other useful information in the same half-yearly format.

The mutual funds are also required to send annual report or abridged annual report to the unit holders at the end of the year. Various studies on mutual fund schemes including yields of different schemes are being published by the financial newspapers on a weekly basis. Apart from these, many research agencies also publish research reports on performance of mutual funds including the ranking of various schemes in terms of their performance. Investors should study these reports and keep themselves informed about the performance of various schemes of different mutual funds. Investors can compare the performance of their schemes with those of other mutual funds under the same category. They can also compare the performance of equity oriented schemes with the benchmarks like BSE Sensitive Index, S&P CNX Nifty, etc. On the basis of performance of the mutual funds, the investors should decide when to enter or exit from a mutual fund scheme.

1.1 Choosing a Scheme by a Small Investor for Investment:

The investors must read the offer document of the mutual fund scheme very carefully. They may also look into the past track record of performance of the scheme or other schemes of the same mutual fund. They may also compare the performance with other schemes having similar investment objectives. Though past performance of a scheme is not an indicator of its future performance and good performance in the past may or may not be sustained in the future, this is one of the important factors for making investment decision. In case of debt oriented schemes, apart from looking into past returns, the investors should also see the quality of debt instruments which is reflected in their rating. A scheme with lower rate of return but having investments in better rated instruments may be safer. Similarly, in equities schemes also, investors may look for quality of portfolio. They may also seek advice of experts. Investors should not assume some companies having the name "mutual benefit" as mutual funds. These companies do not come under the purview of SEBI. On the other hand, mutual funds can mobilize funds from the investors by launching schemes only after getting registered with SEBI as mutual funds.

In the offer document of any mutual fund scheme, financial performance including the net worth of the sponsor for a period of three years is required to be given. The only purpose is that the investors should know the track record of the company which has sponsored the mutual fund. However, higher net worth of the sponsor does not mean that the scheme would give better returns or the sponsor would compensate in case the NAV falls.

In case of winding up of a scheme, the mutual funds pay a sum based on prevailing NAV after adjustment of expenses. Unit holders are entitled to receive a report on winding up from the mutual funds which gives all necessary details.

Investors would find the name of contact person in the offer document of the mutual fund scheme that they may approach in case of any query, complaints or grievances. Trustees of a mutual fund monitor the activities of the mutual fund. The names of the directors of asset Management Company and trustees are also given in the offer documents. Investors can also approach SEBI for redressal of their complaints. On receipt of complaints, SEBI takes up the matter with the concerned mutual fund and follows up with them till the matter is resolved.

1.2 Investor’s Rights and Obligations:

Some of the Rights and Obligations of investors are:-

a) Investors are mutual, beneficial and proportional owners of the scheme’s assets. The investments are held by the trust in fiduciary capacity (The fiduciary duty is a legal relationship of confidence or trust between two or more parties).

b) In case of dividend declaration, investors have a right to receive the dividend within 30 days of declaration.

c) On redemption request by investors, the AMC must dispatch the redemption proceeds within 10 working days of the request. In case the AMC fails to do so, it has to pay an interest @ 15 %. This rate may change from time to time subject to regulations

d) In case the investor fails to claim the redemption proceeds immediately, then the applicable NAV depends upon when the investor claims the redemption proceeds.

e) Investors can obtain relevant information from the trustees and inspect documents like trust deed, investment management agreement, annual reports, offer documents, etc. They must receive audited annual reports within 6 months from the financial year end.

f) Investors can wind up a scheme or even terminate the AMC if unit holders representing 75 % of scheme’s assets pass a resolution to that respect.

g) Investors have a right to be informed about changes in the fundamental attributes of a scheme. Fundamental attributes include type of scheme, investment objectives and policies and terms of issue.

h) Lastly, investors can approach the investor relations officer for grievance redressal. In case the investor does not get appropriate solution, he can approach the investor grievance cell of SEBI. The investor can also sue the trustees.

The OD (offer document) is a legal document and it is the investor's obligation to read the OD carefully before investing. The OD contains all the material information that the investor would require to make an informed decision. It contains the risk factors, dividend policy, investment objective, expenses expected to be incurred by the proposed scheme, fund manager's experience, historical performance of other schemes of the fund and a lot of other vital information. It is not mandatory for the fund house to distribute the OD with each application form but if the investor asks for it, the fund house has to give it to the investor. However, an abridged version of the OD, known as the Key Information Memorandum (KIM) has to be provided with the application form.

1.3 Fund Selection by the Advisor:

It is very important for the asset management company to decide that in which of the available options the collected funds should be invested to provide the investors with higher returns .It affects not only the investment pattern as a whole but also the profitability of the products. An advisor has to decide on the amount to be invested in the basic categories of Equity, Debt, Balanced and Money Market Funds.

Selecting an Equity Fund

The Investor should classify the available equity schemes before investing or selecting a fund for convenience based on Growth, Value ,Equity Income ,Broad based specialty
Concentrated specialty funds .The investor should strategies based on mainstream growth or value funds, providing broad based diversification, Select either a differentiated growth or value fund, or a specialty fund whose risk return will vary from the overall market and also Evaluate pass returns of available funds

2.1Review the salient features of the scheme:

Fund size – smaller funds means higher expenses.

Fund age – the older the performing fund the better compared a new unproven fund. One must consider Portfolio manager's experience, Cost of investing, and Portfolio characteristics.

Cash position – Equity funds normally hold little cash; say 5%, more cash would mean less money is invested. A fund manager might sit on higher % of cash if he predicts a Bull or Bear run.

Portfolio concentration – if the funds 10 largest holdings account for over 50% of the net assets, it is a concentrated portfolio.

Market capitalization of funds – large caps funds are deemed safer to invest in compared to small cap funds.

Portfolio turnover – A steady holding of investments means long term orientation. Higher turnover could mean higher capital gain but it would also mean higher transaction cost.

Portfolio statistic – compare its performance with others.

2.2 Selecting a Debt/ Income/ Bond Fund:

Narrow down on choices- Debt funds have a larger variety to choose from. Short term – long term, government – corporate, high investment grade or low, domestic – global bonds.

Know investment objective- Younger investor needs retirement planning, hence long term bonds are appropriate, retired investors need money income schemes.

2.3 Selecting a Money Market or Liquid Fund:

While selecting a liquid fund the advisor has to keep in mind points like *Costs ,*
Quality ,Yields

3.1 Developing a Model Portfolio:

While investing and developing a portfolio for one self, there are many important points which one should remember. Jacob described these steps of investing in this manner:

Jacob's Four step program:

a) *Work with the investors to develop long term goals*
b) *Determine the asset allocation of the investment portfolio*
c) *Determine the sector distribution*
d) *Select specific fund managers & their schemes*

Jacob's Four different portfolios:

Young unmarried professional: 50% in aggressive equity funds, 25% in high yield bonds & growth & income funds, 25% in conservative money market funds.

Young couple with 2 kids: 10% in money market funds, 30% in aggressive equity funds, 25% in high yield bonds & long term growth funds & 35% municipal bond funds.

Older couple – single income: 30% in short municipal bond funds, 35% long term municipal bond funds, 25% moderately aggressive equity & 10% emerging growth equity.

Recently retired couple: 35% in conservative equity funds for capital preservation/ income, 25% moderately aggressive equity & 40% in money market funds.

4.1Mutual Fund Investment Strategies:

Systematic Investment Plan (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 mutual fund scheme the investor has chosen. For instance 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.

Systematic Withdrawal Plan (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 expenses.

Systematic Transfer Plan (STPs):

They allow the investors 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 units 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 investment actively to achieve his objectives. Many funds do not even charge even any transaction feed for this service an added advantage for the active investor.

5.1 Investment Procedure in Mutual Funds:

The Procedure Of investment in Mutual Fund can be summed up like this:

1) Identify the needs
2) Choose the Right Fund

3) Select the ideal mix of scheme
4) Invest Regularly
5) Keep taxes in mind
6) Start early

The Ground Rule of Mutual Fund Investing:

Before investing one must learn some basic rules of investing in Mutual funds, so that one should not make big losses. These Rules are simple and as follows:

1) Assess oneself: assessment of once need
2) Try to understand where money is going
3) Don't rush in picking funds, think first
4) Invest, Don't speculate
5) Don't put all the eggs in one basket
6) Be regular
7) Do the homework
8) Find the right Fund
9) Keep track of right information
10) Know when to sell the funds

These ground rules are inter connected to each other and they go hand in hand together.

6.FACILITIES AVAILABLE TO INVESTORS:

6.1Repurchase Facilities: The close-end schemes are required to be listed in recognized stock exchanges. These schemes are generally bought and sold at market prices. But listing in stock exchange is not mandatory for the open-ended schemes. So they have to be bought only from the fund. The fund reserves the right to buy back the units from its members. This process of buying back the units from the investors by the fund is called repurchase facility.

6.2 Re-issue *Facilities:* The units /schemes /funds purchased from the investors are again reissued to the interested investors. The price for this purchase is called re-issue price.

6.3 Roll-*Over Facilities:* At the time of redemption, investors are given an option to reinvest this entire amount once again for another term. An investor can overcome the adverse market conditions at the time of redemption by resorting to roll over facility. This is cited in the close-ended scheme.

6.4 Lateral Shifting Facilities: Some mutual funds permit investors to shift from one scheme to another on the basis of the NAV with a view to provide total flexibility in their operations. This shifting is called "lateral shifting".

6.5 OPTIONS AND VALUE-ADDED SERVICES:

Thanks to the heightened competition in the mutual fund industry, mutual funds now offer various options and value-added services to attract and retain customers.

Options:

With respect to a number of schemes, Mutual Funds offer the following:

Dividend and growth options, systematic investment plan, and systematic withdrawal plan.

i. **Dividend and growth options:** When any investor joins a scheme, he can choose the dividend option or the growth option. Under the dividend option, the gains of the scheme are paid out at regular intervals in the form of dividends. Funds may offer daily, weekly, monthly, quarterly, half-yearly, and annual dividend options.

Under the growth option, investment gains are ploughed back into the scheme and no dividends are declared. Though the returns from both the dividend and growth options will be the same, the tax implications may be different.

ii. **Systematic investment plan:** Under the systematic investment plan (SIP), the investor can invest regular sums of money every month to buy units of a Mutual Fund scheme. As the investment is made regularly, the investor buys more units when the price is low and fewer units when the price is high.

ii. **Systematic withdrawal plan:** A Systematic Withdrawal Plan (SWP) works like a systematic investment plan in the opposite direction. The SWP allows the investor to withdraw a fixed amount every month.

Value-Added Services:

Mutual funds offer value-added services like redemption over phone, triggers and alerts, cheque book facility, and new points of purchase.

i. **Redemption over phone:** many companies for example, Prudential ICICI offers investors, the facility of making a redemption request or switch between schemes over the phone.

ii. **Cheque book facility:** Fund houses take few days to process a redemption request and then further time is lost when the redemption cheque is in transit. To cut down this delay, some fund houses give investors in certain schemes (typically debt schemes), some limit, at the time of investment itself. Encashment of the cheque is deemed as withdrawal, at the scheme's NAV on the day the cheque is deposited.

CONCLUSION

Savings form an important part of the economy of any nation. With the savings invested in various options available to the people, the money acts as the driver for growth of the country. Indian financial scene too presents a plethora of avenues to the investors. Though certainly not the best or deepest of markets in the world, it has reasonable options for an ordinary man to invest his savings.

An investment can be described as perfect if it satisfies all the needs of all investors. So, the starting point in searching for the perfect investment would be to examine investor needs. If all those needs are met by the investment, then that investment can be termed the perfect investment.

Most investors and advisors spend a great deal of time understanding the merits of the thousands of investments available in India. Little time, however, is spent understanding the needs of the investor and ensuring that the most appropriate investments are selected for him.

The Investment Needs of an Investor are very important.

1. Security of original capital: The chance of losing some capital has been a primary need. This is perhaps the strongest need among investors in India, who have suffered regularly due to failures of the financial system.

2. Wealth accumulation: This is largely a factor of investment performance, including both short-term performance of an investment and long-term performance of a portfolio. Wealth accumulation is the ultimate measure of the success of an investment decision.

3. Comfort factor: This refers to the peace of mind associated with an investment. Avoiding discomfort is probably a greater need than receiving comfort. Reputation plays an important part in delivering the comfort factor.

4. Tax efficiency: Legitimate reduction in the amount of tax payable is an important part of the Indian psyche. Every rupee saved in taxes goes towards wealth accumulation.

5. Life Cover: Many investors look for investments that offer good return with adequate life cover to manage the situations in case of any eventualities.

6. Income: This refers to money distributed at intervals by an investment, which are usually used by the investor for meeting regular expenses. Income needs tend to be fairly constant because they are related to lifestyle and are well understood by investors.

7. Simplicity: Investment instruments are complex, but investors need to understand what is being done with their money. A planner should also deliver simplicity to investors.

8. Ease of withdrawal: This refers to the ability to invest long term but withdraw funds when desired. This is strongly linked to a sense of ownership.

9. Communication: This is to educating and informing the investors about their investment

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