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Significant Insights, Value Orientation and Differences Between the Mutual Fund Investment Flow and Indian Stock Market Returns – A Theoretical Assimilation

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ABSTRACT:

Researchers and academicians from all over the world have become interested in the study of the causal relationship between mutual fund investment flow and stock market returns in recent years. But there is currently a contradictory body of empirical data on this matter. Additionally, there are a few studies that take the case of India into account. In order to better understand the dynamics of the relationship between mutual fund investment flow and stock market returns in India from January 2000 to May 2010, the following article will do just that. The Granger causality tests are applied using the Toda and Yamamoto approach, which yields evidence of a one-way causal relationship between stock market returns and mutual fund investment flow. This suggests that the expansion of stock market activity in India draws mutual funds to the stock market. Therefore, the government and monetary authorities should take the necessary actions to reduce the volatility and increase the efficiency of the capital market. By gathering money from households and investing it in the stock and debt markets, mutual funds enable portfolio diversification and relative risk aversion. In India, a specific type of mutual fund called fixed-income funds invests in debt securities that have been issued by businesses, banks, or the government. In India, fixed-income funds are also referred to as debt funds and income funds. The goal of the current study is to assess the performance of a few selected debt or income mutual fund schemes in India based on their daily NAV using various statistical measures. In the past ten years, income schemes have become more and more popular. The securities that were purchased are referred to as the fund's portfolio. There may have been restrictions on rival products, which led to the emergence of money market and (short-term) bond funds. In this study, the performance of several mutual fund types in India was compared and studied. The results showed that equities funds outperformed income funds. The study also found that institutional fund managers can time their investments and that equity fund managers have significant market timing ability, but broker operated funds did not demonstrate this ability. Additionally, empirical research has shown that fund managers possess significant timing ability and can time their investments to match market conditions.

Keywords: Mutual funds, Stock Market Returns, Investment, Debt Markets, Portfolio Diversifications

Introduction:

In recent years, investors' preference for mutual funds as a source of investment has grown significantly. However, the Mutual Fund Industry is also contributing significantly to the expansion and improvement of the Economy. Mutual funds are professionally managed funds that pool the savings of many different investors and invest those funds in a variety of investment options, including government securities, debt, and equities. Due to their unique characteristics like diversification, low transaction costs, liquidity, and expert knowledge, mutual funds have become very popular. Due to their superior returns and capital growth compared to other investment options, equity funds are very well-liked by Indian investors. When compared to other fund schemes, equity funds likely offer a higher return, but they also come with a higher risk. The risk-return analysis of the funds is crucial because investors are now very concerned about their investments. A managed collection of securities from various corporations is referred to as a mutual fund. On the shares they own, these corporations receive dividends, and when their securities are traded, they experience capital gains or losses. Investors purchase mutual fund shares similarly to how they would any other type of individual security. After operational expenses have been paid, the mutual fund distributes its earnings (dividends, capital gains or losses) to the investors in proportion to the amount invested. Investors believe that a gain on one investment wills more than make up for a loss on another. Owners of mutual fund shares might collectively profit by diversifying their assets, which may be outside of their individual financial capabilities, by adhering to the maxim "Don't put all your eggs in one basket." Mutual funds come in two varieties: open-end and closed-end. Due to the fact that its shares are not fixed, an open-end mutual fund is a sort of fluid capital stock. The total number of shares fluctuates when shareholders buy and sell shares. Investors have access to a market at any time to buy and sell firm shares.

Model portfolio for 60:40 Asset Allocation with 80:20 Core-Satellite mix			
Investment	**Asset class**	**Core/Satellite**	**% of Portfolio**
Largecap ETF	Equity	Core	10
Largecap active fund	Equity	Core	20
Midcap active fund	Equity	Core	20
Ultra-short term debt funds	Debt	Core	10
EPF and Bank deposit	Debt	Core	20
International fund	Equity	Satellite	5
Stocks	Equity	Satellite	5
Long-term gilt funds (constant duration)	Debt	Satellite	10

Above image showing model portfolio for 60:40 asset allocation with 80:20 core satellite mix

Review of Literature:

AlkaSolanki (2016) According to "A Study of Performance Evaluation of Mutual Funds," all of the mutual fund schemes taken into consideration for the study beat the benchmark return, with the exception of one fund, the Reliance Focused Large Cap fund.

Md.Qamruzzaman ACMA (2014) the authors came to the conclusion that growth-oriented mutual funds have not outperformed their volatility-relative performance.

Dr.Vikas Choudhary & Preeti Sehgal Chawla (2014) the performance of equity-diversified mutual funds was compared by the authors. In other words, 75% of the funds have performed better than average in terms of returns. 62% of the funds are less hazardous than the market in terms of SD.

MohamedZaheeruddin,Pinninti Sivakumar &K.Srinivas Reddy (2013) the aforementioned study found that, among the intermediaries chosen for the study's purposes, investors should choose ICICI mutual funds since they carry the lowest risk compared to those of other intermediaries.

Poonam M Lohara (2013) her research came to the conclusion that all fund returns exceeded market index returns. Across the board, the Reliance Banking Fund scored poorly on all three performance metrics. The market benchmark was exceeded by the IDBI fixed maturity funds and the Kotak Gold Fund.

M.S.Annapoorna &Pradeep Gupta (2013) The CRISIL-ranked #1 mutual fund schemes were subjected to evaluation by the authors. It was discovered that all of the schemes' performance appeared erratic during the study period, and it was challenging to identify a single one that consistently outperformed the others.

Dr. K. Mallikarjuna Rao and Ranjeeta Rani (2013)the authors' study used mean return beta, Sharpe, Treynor, Jensen, and Fama Ratio to evaluate the risk-adjusted performance of a few balance schemes. In other words, the study found that most of the schemes outperformed the market; had low average beta, disproportionate unsystematic risk, and some schemes had a mismatch between risk and return. These are primarily caused by a lack of professional management skills, including inadequate diversification, stock selection, and security analysis.

Dietze,Oliver and Macro (2009) the purpose of the study was to assess the risk-adjusted performance of mutual funds that invest in European investment-grade corporate bonds. For a five-year period, 19 investment grade corporate bond funds were assessed. Utilizing multi-index and asset class factor models, these funds were assessed. The findings showed that no fund had a positive return, and corporate funds generally underperformed the benchmark portfolio.

Boudreauxand Suzanne (2007) the authors carried out research to assess the risk-adjusted returns of global mutual funds from 2000 to 2006. Using Sharpe's performance index, ten international mutual fund portfolios were examined. Benchmark was established using the US mutual fund market. Nine out of ten funds, according to the findings, outperformed the market.

Mutual Funds can be categorized according to their nature as below:-

Equity funds:

Stocks of publicly traded companies are purchased by equity mutual funds with pooled money. When choosing stocks for their portfolios, equity fund managers use a variety of stock picking techniques. Some fund managers take a value approach to stock selection, looking for undervalued stocks compared to those of competing companies. Another strategy is to focus on growth, looking for stocks that are expanding more quickly than their rivals or the market as a whole. Some managers build a portfolio of both growth and value stocks by purchasing both varieties of stocks.

Debt funds:

Debt mutual funds are a particular kind of mutual fund that are created for low risk investors whose primary goal is capital appreciation along with respectable returns on investment. These are for investors who favor less volatile investments and seek a steady stream of income.

Debt funds can give:

- ✓ Capital Appreciation
- ✓ Regular Income

Balanced funds:

They are a combination of both equity and debt funds, as their name suggests. They follow the pre-established investment aim of the scheme by investing in both fixed income and equity instruments. Growth is provided by equity, while return stability is provided by debt. These funds are designed to maintain reasonable returns while reducing some of the equity risk through exposure to debt while this means less upside during a bull market, some investors prefer to stick with a single investment that offers a reasonable possibility of a solid return on their money and that is more likely to avoid major volatility when the economy slows down. The best chance of accomplishing so is with a well-managed balanced fund because bonds often keep their value better during stock market downturns and has lower yields during stock market upturns. A criterion for selecting a mutual fund for investing includes a successful past is not a guarantee of future success. Investors should consider several quantitative metrics when determining which fund is best for them.

Expense Ratio: Indicates the funds' annual costs, which include management and administrative costs. Better is a low expense ratio. The percentage of total assets used to manage a mutual fund that is known as the expense ratio. Expenses play a significant role when comparing bond funds because bond fund returns frequently have similar characteristics. A fund's chargeable maximum has been set by SEBI. In terms of expense ratio, management and advisory fees make up the majority of the total. It's not always true that a fund with a lower expense ratio is one that is better managed. A good fund is one that generates a good return while incurring few costs.

Standard Deviation (SD): A mutual fund's overall risk (market risk, security-specific risk, and portfolio risk) is quantified by its "Standard Deviation" (SD). The standard deviation of mutual fund returns shows how far they deviate from expected returns based on past performance. In other words, it assesses the fund's volatility. The degree to which a fund fluctuates in relation to its average return over a period of time is how the standard deviation of a fund gauges this risk. A mutual fund with a higher SD number has a higher risk profile and more volatile net asset value (NAV) than one with a lower SD.

Sharpe Ratio: A telltale sign of whether excessive risk or wise investment choices are to blame for the return on an investment. Better is a higher Sharpe Ratio. Another crucial metric, the Sharpe ratio (SR), assesses how well a fund has performed in relation to the risk it has taken. An investor can use this ratio to determine whether it is safe to invest in this fund while assuming certain level of risk.

HISTORY OF MUTUAL FUNDS:

Belgium was the first nation to provide the modern mutual fund in 1822. The popularity of this kind of investment spread quickly to France and Great Britain. Particularly since their initial uptake in the 1920s, open-end mutual funds have continued to enjoy popularity in the United States since the 1930s. Mutual funds experienced significant growth after World War II, especially in the 1980s and 1990s. While LIC launched its mutual fund in June 1989, GIC did so in December 1990. Private sector funds' entry into the Indian mutual fund market in 1993 marked the start of a new era and provided investors with more fund families to choose from. In addition, the initial Mutual Fund Regulations were established in 1993 and mandated that all mutual funds, with the exception of UTI, be registered and governed. The Kothari Pioneer mutual fund, which later merged with Franklin Templeton, was the first one to be registered in the private sector. It was established in July 1993. The number of mutual fund houses increased as more foreign mutual funds opened funds in India. The industry has also experienced a number of mergers and acquisitions. As of the end of January 2003, there were 33 mutual funds with a total asset value of Rs. 1,21,805 crores. The Unit Trust of India was far ahead of other mutual funds with assets under management totaling Rs. 44,541 crores. Following the repeal of the Unit Trust of India Act of 1963 in February 2003, UTI was split into two separate entities. One is the Specified Undertaking of the Unit Trust of India, which is governed by an administrator and is exempt from the Mutual Fund Regulations, and which as of the end of January 2003 had assets under management totaling Rs. 29, 835 crores, roughly equivalent to the assets of the US 64 scheme, assured return, and a few other schemes.

MUTUAL FUND PROSPECTUS:

A legal document called a prospectus contains details about the mutual fund. You can learn more about the offer's conditions, the issuer, and its goals in this document. The Securities Act of 1933, passed by the federal government in the wake of the 1929 stock market crash, mandated that security companies publish prospectuses. A prospectus might appear overwhelming at first. The prospectus typically contains a lot of information, is written in technical and legal language, and is lengthy and full of tables and graphs. Before you invest in a mutual fund, use the information in this document to

make an educated investment decision. Pay close attention to the following crucial sections to obtain the information you require: Investment Purpose: a succinct description of the investment goals of the fund. While some funds may prioritize long-term stability, others may aim for short-term growth. Investment Strategy: The precise method by which the fund intends to achieve its goals. The types of assets that the fund purchases are described in this section. Fees and Expenses: While mutual funds aim to make money for their investors, their primary objective—as with any business—is to do so for their own financial benefit. The fees and costs that funds charge their shareholders in order to achieve this must all be disclosed in the prospectus. Each prospectus includes a table outlining the various fees and expenses, along with an estimation of how the fees would affect a $10,000 investment over a ten-year period. You can compare costs and fees among mutual funds as a result. Account Information: The very basic instructions for buying and selling shares, as well as other information pertaining to accounts, are provided in this section. The prospectus will explain how to withdraw your money from the fund in addition to how to put money into it. You can learn about your options for redemption in the prospectus. Risks: The prospectus's most crucial section deals with the fund's level of risk-taking and the risks connected to the particular investments the fund has made. Performance: Details regarding the fund's performance over the previous ten years are provided. Investors need to be aware that past performance does not guarantee future outcomes. The fund's historical performance in comparison to an index, like the S&P 500, is crucial. Performance of a fund is also influenced by turnover, dividend payments, and volatility of the fund. Management: The names of the managers are listed, along with some additional details about their backgrounds and credentials. To get a sense of their previous strategies and outcomes, it can be useful to know whether or not they have managed other funds in the past and whether or not they were successful.

A company with speculative growth should eventually develop into a top-tier organization. Aggressive Growth: Businesses with aggressive growth exhibit a little more maturity than those with speculative growth: They record rapid growth in profits as well as sales, which indicates greater tenacity. It's time to start earning some money at this point. Classic Growth: These companies are in the prime of their careers and don't have much to prove. The top traditional growers have developed into money-making machines, producing consistent growth, high capital returns, positive free cash flows, and rising dividends. The problem is that they are growing much more slowly than the group with aggressive growth. Slow Growth and High Yield: These companies' growth is now just a distant memory. Due to a lack of lucrative investment opportunities, the majority of them pay out the majority of their profits in dividends (high payout ratios) as opposed to reinvesting the money in their companies.

PROFESSIONAL MANAGEMENT & RANKING OF MUTUAL FUNDS

Professional management: Professional managers are used by mutual funds to decide which companies' securities should be purchased and sold. The managers of the mutual fund choose the investments for the combined funds. There are many complex investment opportunities available. Fund managers must be aware of what is available, the risks and potential rewards, the cost of buying and selling investments, and industry laws and regulations.

Ranking: FundsCompanies like Morningstar, which has an industry-recognized rating system for mutual funds, rank these funds based on their performance overall and performance relative to their peers. One to five stars are assigned, with five stars being the best. Typically, the quality of the fund increases with rank. For instance, Morningstar assigns mutual funds a star rating of 1 to 5 based on how well they've performed in comparison to other funds of a similar type (after adjusting for risk and sales charges). The top 10% of funds in each Morningstar Category receive 5 stars, while the bottom 10% receives 1 star. Three, five, and ten year ratings are given to funds, and these ratings are added together to produce an overall rating. Funds with a history of less than three years are not rated. Ratings are impartial and entirely determined by a mathematical analysis of prior performance. The ratings are a helpful tool for identifying investments that merit further investigation, but they shouldn't be interpreted as buy or sell signals.

MUTUAL FUND ANNUAL REPORT

Every year, mutual funds send an Annual Report to each investor. The fund's financial statements, a list of its securities, and an explanation from the management of the fund as to why the fund performed as it did the prior year are all included in the annual report.

CONCLUSION:

Without a doubt, the Indian economy is likely to return to a high growth path in a few years with the structural liberalization policies. Therefore, it is necessary for mutual fund organizations to upgrade their knowledge and equipment. However, the success of the mutual fund would depend on how well the suggestions were put into practice. Regarding the mutual fund investor, we believe that the investor must simultaneously develop two critical skills for successful investing: a sense of timing and investment discipline.Direct stock investments are an option for equity investors, or they can invest through mutual funds. Investments in stocks are risky and time-consuming for the individual investor. If you have a good understanding of the market, investing in stocks might be a rapid way to gain money. Mutual funds, on the other hand, are appropriate for investors with a longer time horizon.

Mutual funds are professionally managed by fund managers and less risky. Mutual funds are less prone to market swings and have the advantage of diversification.

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