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A Study On Performance Evaluation of Actively Managed And Passively Managed Mutual Fund

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ABSTRACT:

Mutual funds have long been a popular investment avenue, offering diversification, professional management, and liquidity to investors. This study aims to evaluate and compare the performance of actively managed and passively managed mutual funds. Actively managed funds seek to outperform market indices through strategic asset allocation and stock selection, whereas passively managed funds aim to replicate the performance of a benchmark index with minimal management intervention. Using performance metrics such as returns, risk-adjusted returns (Sharpe Ratio, Treynor Ratio, and Jensen's Alpha), and expense ratios, this research analyzes a selected sample of mutual funds over a defined period. The study further explores whether active fund managers can consistently generate superior returns after accounting for costs, compared to their passive counterparts. Findings from this study offer insights for investors in making informed investment decisions and contribute to the ongoing debate between active and passive investment strategies.

Keywords: Mutual Funds, Actively Managed Funds, Passively Managed Funds, Performance Evaluation, Sharpe Ratio, Treynor Ratio, Jensen's Alpha, Risk-Adjusted Returns, Investment Strategies.

Introduction

Mutual funds have become a go-to investment option for individuals and institutions looking to diversify their portfolios and tap into the financial markets. Over time, the mutual fund industry has grown and evolved, offering a wide range of products that cater to different risk appetites and investment goals. When it comes to mutual funds, there are two main approaches: active management and passive management. Actively managed funds are run by experienced fund managers who actively make investment decisions, trying to beat the market average. They rely on research, market forecasting, and their own judgment to pick securities that they think will perform well.

On the other hand, passively managed funds, like index funds and ETFs, take a different approach. They aim to mirror the performance of a specific index, like the S&P 500, by holding the same securities in the same proportions. The idea behind passive management is that markets are generally efficient, and it's hard to consistently beat the market over the long term.

In recent years, there's been a growing debate about whether active or passive management is more effective. Many actively managed funds have struggled to beat their benchmarks, and investors are starting to wonder if the higher costs associated with active management are worth it.

This research paper aims to compare the performance of actively managed and passively managed mutual funds, looking at their returns, risk profiles, and cost structures. By understanding the pros and cons of each approach, investors can make more informed decisions that align with their financial goals."

Objectives of the Study

The primary objective of this research is to evaluate and compare the performance of actively managed and passively managed mutual funds based on primary data collected from investors, financial advisors, and fund managers. The study aims to understand investor perceptions, preferences, and satisfaction levels regarding both types of mutual funds.

The specific objectives are:

- To analyze the investment behavior and preferences of mutual fund investors towards active and passive funds.
- To assess the performance satisfaction of investors with actively managed and passively managed mutual funds.
- To evaluate the awareness level among investors regarding the cost structure, risk, and returns of active versus passive funds.

Literature Review

The performance evaluation of actively managed and passively managed mutual funds has been widely studied by various researchers and scholars. This literature review provides a comprehensive understanding of the key studies, concepts, and findings that form the foundation of the present research.

Gupta (2000) in his book Mutual Funds and Asset Management in India provides a detailed analysis of the evolution, regulatory framework, and performance trends of mutual funds in India. His study highlights that actively managed funds initially dominated the Indian market, although the rise of passive investing is gradually reshaping investor preferences.

Kothari (2004) in Research Methodology: Methods and Techniques emphasizes the importance of systematic data collection and analysis in financial research. His insights have been valuable in shaping the methodological approach used in this study, particularly for conducting primary research on investor perceptions.

Singh (2016) in her work Investment Management: Security Analysis and Portfolio Management discusses how mutual fund performance is influenced by various factors such as fund management strategies, market conditions, and investor behavior. She also highlights the difference in expense structures and risk profiles between active and passive funds, which directly relates to the objectives of this study.

Tripathi (2008) in her research paper Performance Evaluation of Mutual Funds in India: A Study of Selected Schemes provides empirical evidence on the performance of mutual funds in the Indian context. Her findings suggest that although actively managed funds sometimes outperform benchmarks, passive funds often deliver more consistent returns after adjusting for costs.

John C. Bogle (2017) in The Little Book of Common Sense Investing strongly advocates for passive investing. He argues that due to lower expense ratios and minimal management intervention, index funds often outperform actively managed funds over the long term. His work has been instrumental in understanding the cost-benefit dynamics between active and passive investment strategies.

Websites such as AMFI (www.amfiindia.com), SEBI (www.sebi.gov.in), Moneycontrol (www.moneycontrol.com), and Investopedia (www.investopedia.com) have been referred to for gathering current statistics, definitions, regulations, and recent trends regarding mutual fund investments in India.

Reports from AMFI and SEBI have provided updated insights on investor trends, regulatory changes, and the growing interest in index-based investment products in India.

Thus, the literature reveals that while actively managed mutual funds may offer the potential for higher returns through professional management, passively managed funds attract investors looking for lower costs and stable, market-matching returns. This study builds on these existing works to further explore the preferences, satisfaction levels, and awareness among Indian investors.

Research Methodology

This section outlines the research approach, design, data collection methods, and tools used for evaluating and comparing the performance of actively managed and passively managed mutual funds. The research methodology adopted for this study is based on primary data collected from mutual fund investors, financial advisors, and fund managers. The study utilizes both qualitative and quantitative research techniques to achieve the objectives of the research.

1. Research Design

The research design for this study is descriptive in nature, as it aims to describe and analyze the perceptions, preferences, and satisfaction levels of mutual fund investors regarding actively and passively managed funds. The study also seeks to evaluate the awareness and knowledge of investors on various factors such as cost structures, returns, and risk associated with these two types of funds.

2. Research Approach

A quantitative research approach is employed for this study. The primary data collection involves structured questionnaires distributed to a sample of mutual fund investors. The responses are analyzed using statistical methods to draw meaningful insights regarding the investment behavior, preferences, and performance perceptions of investors.

3. Sampling Technique

The study uses a convenience sampling technique. The sample consists of 100 respondents, including individual investors, financial advisors, and fund managers. The sample is chosen based on their familiarity with mutual fund investments and their willingness to participate in the study.

4. Data Collection Methods

The primary data for this research is collected through a structured questionnaire. The questionnaire includes both closed-ended and open-ended questions to capture both quantitative and qualitative data. The questions are designed to align with the objectives of the study, which include:

- Understanding the preferences of investors between actively managed and passively managed mutual funds.
- Evaluating the satisfaction levels of investors regarding the performance and returns of their investments.
- Assessing the awareness levels of investors about costs, risk, and returns associated with different types of funds.

The survey is distributed to respondents through an online survey tool, ensuring a wide reach and ease of response collection.

5. Data Analysis

The collected data is analyzed using descriptive statistics such as frequencies, percentages, and mean scores to provide insights into the preferences and satisfaction levels of the respondents. In addition, the data is presented in tabular form, followed by data interpretation and insights.

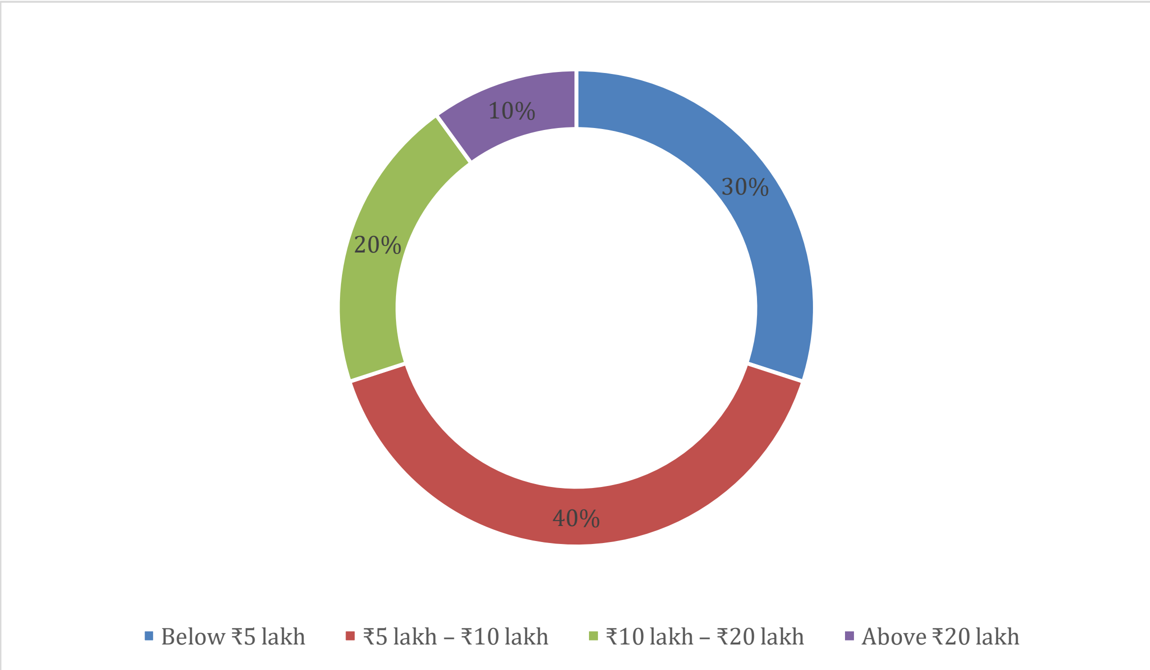
6. Limitations of the Study

While the research methodology provides comprehensive insights into the performance evaluation of mutual funds, the following limitations should be considered:
Sampling Bias: Since a convenience sampling technique is used, the sample may not be entirely representative of the broader investor population.
Geographical Limitations: The sample may be biased toward a particular geographic region, affecting the generalizability of the findings.
Response Bias: The survey relies on self-reported data, which may be subject to biases such as social desirability or misrepresentation of investment behavior.

Data Analysis and Interpretation

Table 1: Annual Income

Particular	No. of Respondents	Percentage
Below ₹5 lakh	30	30%
₹5 lakh – ₹10 lakh	40	40%
₹10 lakh – ₹20 lakh	20	20%
Above ₹20 lakh	10	10%



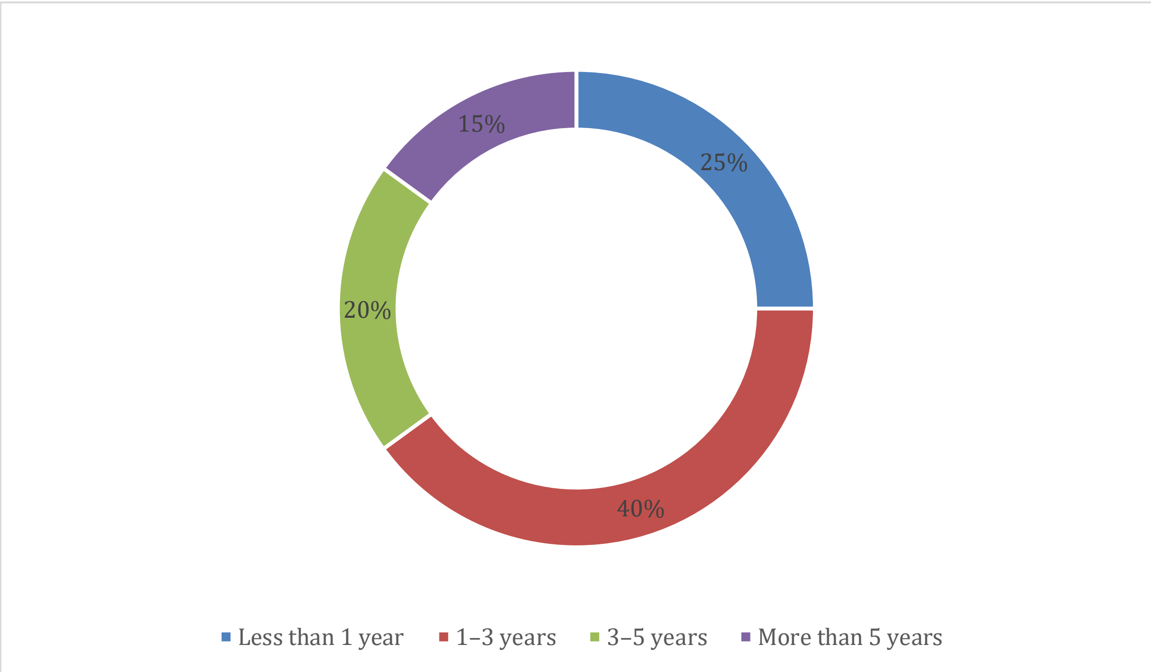
Graph : 1

Interpretation:

The majority of the respondents (40%) fall within the ₹5 lakh – ₹10 lakh annual income bracket, indicating a middle-income group as the dominant segment investing in mutual funds.

Table 2: How long have you been investing in mutual funds?

Particular	No. of Respondents	Percentage
Less than 1 year	**25**	**25%**
1–3 years	**40**	**40%**
3–5 years	**20**	**20%**
More than 5 years	**15**	**15%**



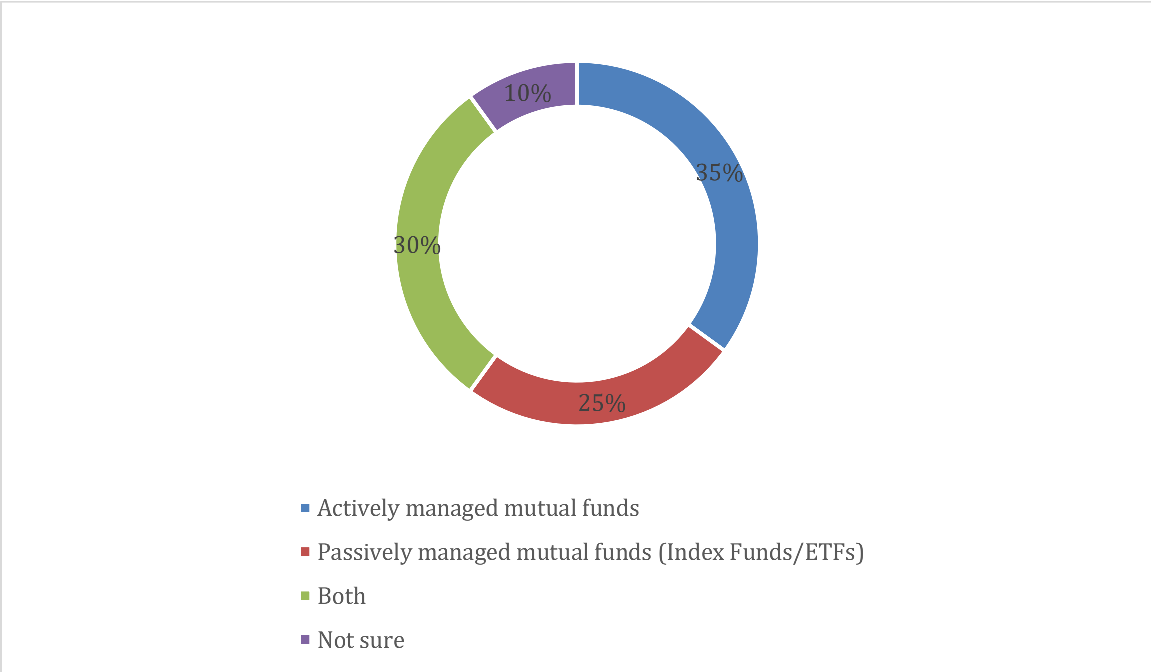
Graph : 2

Interpretation:

Most respondents (40%) have been investing in mutual funds for 1–3 years, showing that a large portion of investors are relatively new to mutual fund investments.

Table 3: Which type of mutual fund do you prefer to invest in?

Particular	No. of Respondents	Percentage
Actively managed mutual funds	**35**	**35%**
Passively managed mutual funds (Index Funds/ETFs)	**25**	**25%**
Both	**30**	**30%**
Not sure	**10**	**10%**



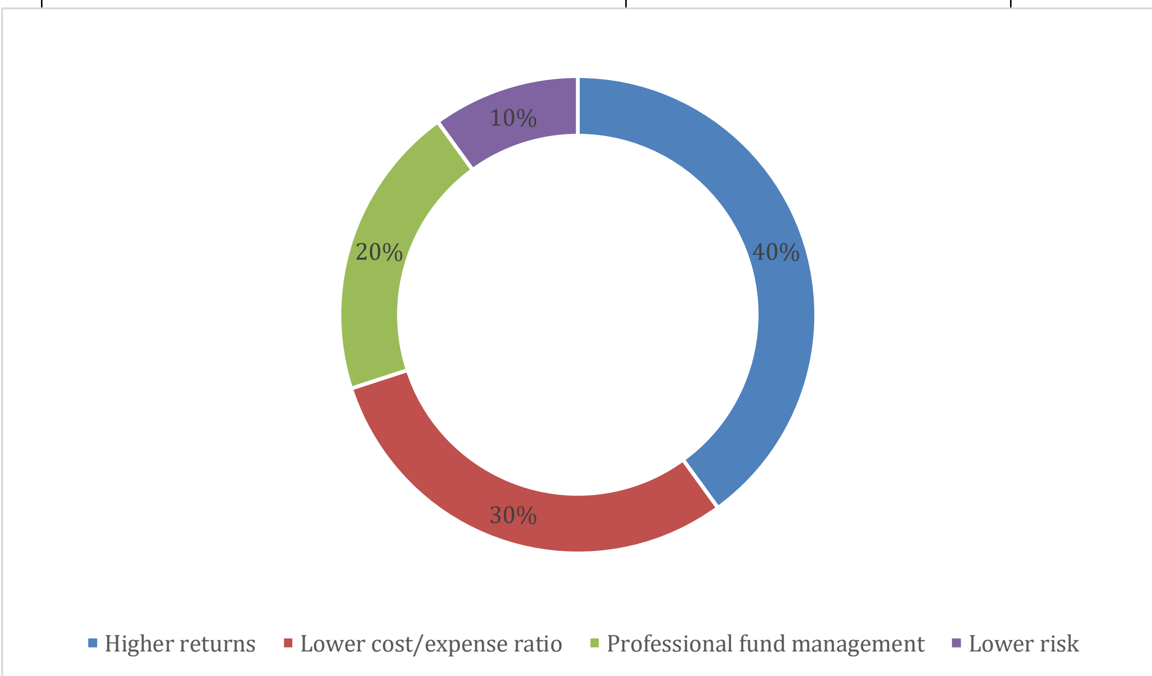
Graph : 3

Interpretation:

35% of investors prefer actively managed funds, followed closely by 30% preferring both active and passive investments, showing a balanced interest in both types of funds.

Table 4: What is the primary reason for choosing your preferred fund type?

Particular	**No. of Respondents**	**Percentage**
Higher returns	**40**	**40%**
Lower cost/expense ratio	**30**	**30%**
Professional fund management	**20**	**20%**
Lower risk	**10**	**10%**



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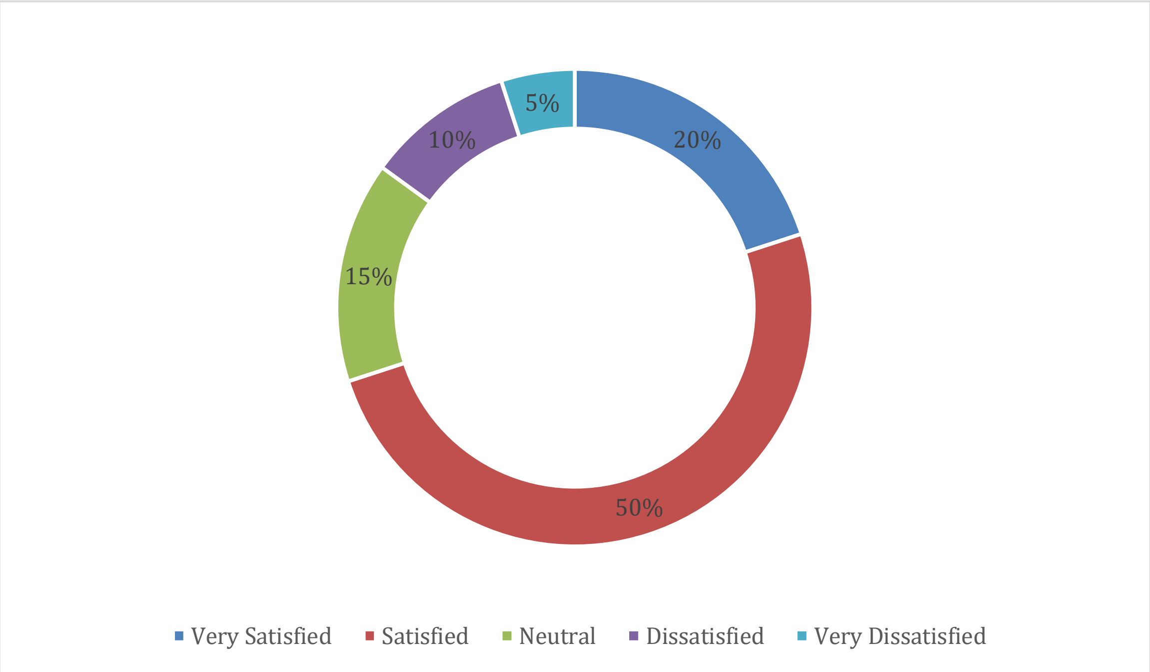
Interpretation:

Higher returns are the main reason (40%) why investors choose a particular fund type, highlighting that return potential remains the most critical factor in investment decisions.

Table 5: How satisfied are you with the returns from your mutual fund investments?

Particular	No. of Respondents	Percentage
Very Satisfied	**20**	**20%**
Satisfied	**50**	**50%**
Neutral	**15**	**15%**
Dissatisfied	**10**	**10%**
Very Dissatisfied	**5**	**5%**



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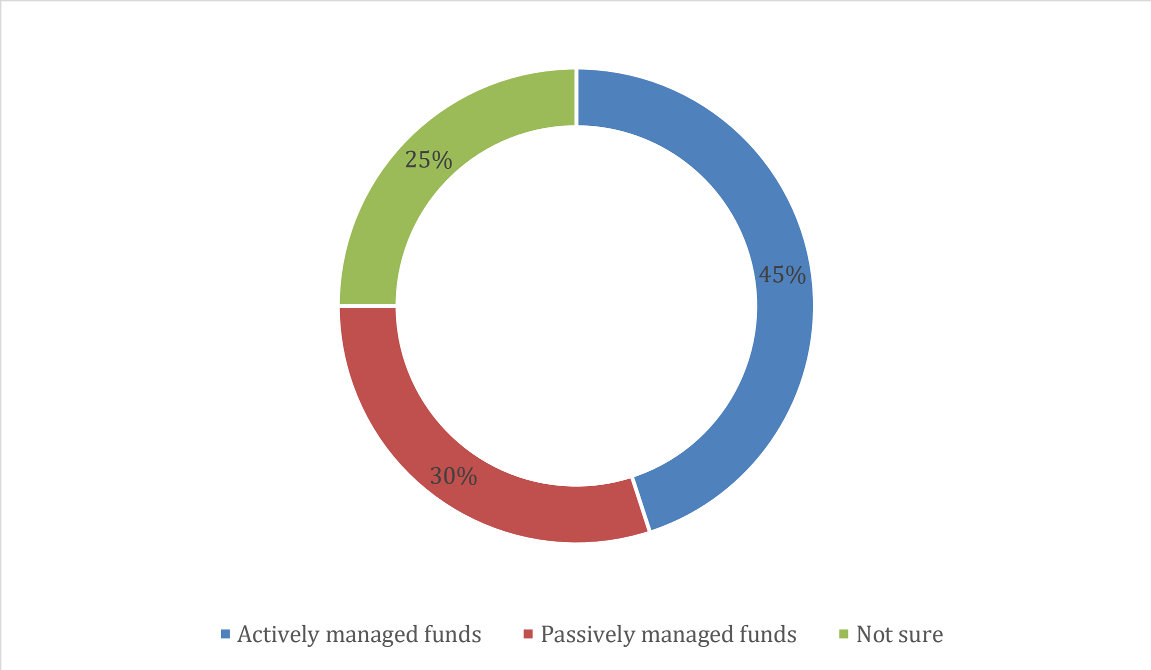
Interpretation:

Half of the respondents (50%) are satisfied with their mutual fund returns, suggesting that mutual funds are meeting the expectations of a large segment of investors.

Table 6: In your opinion, which type of fund provides better returns after costs?

Particular	No. of Respondents	Percentage
Actively managed funds	**45**	**45%**
Passively managed funds	**30**	**30%**
Not sure	**25**	**25%**



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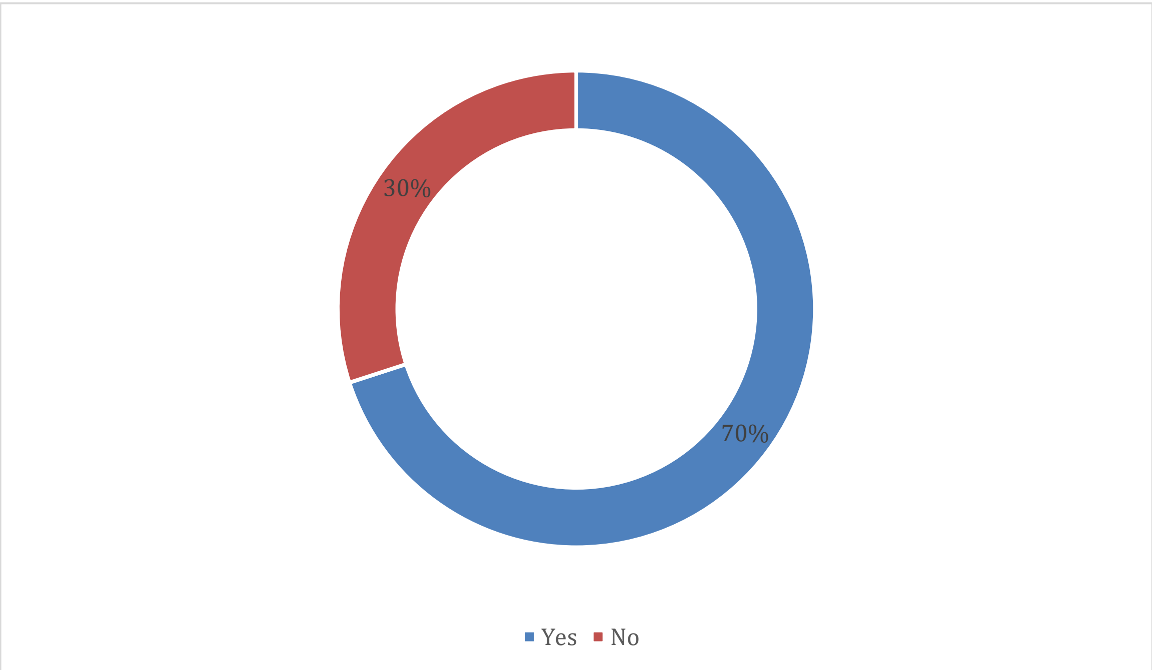
Interpretation:

45% of respondents believe that actively managed funds provide better returns after costs, indicating stronger confidence in fund manager strategies despite higher fees.

Table 7: Are you aware that actively managed funds generally have higher expense ratios than passively managed funds?

Particular	No. of Respondents	Percentage
Yes	**70**	**70%**
No	**30**	**30%**



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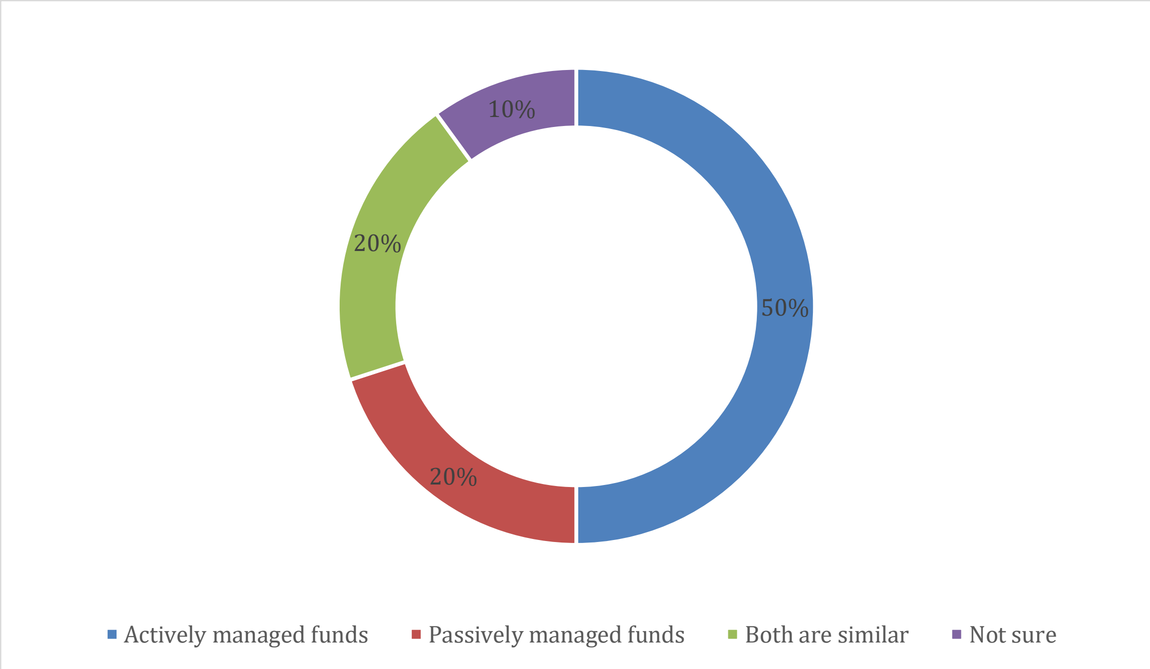
Interpretation:

A large majority (70%) of respondents are aware that actively managed funds have higher expense ratios, suggesting a reasonable level of cost-awareness among investors.

Table 8: In your opinion, which type of fund carries a higher risk?

Particular	No. of Respondents	Percentage
Actively managed funds	**50**	**50%**
Passively managed funds	**20**	**20%**
Both are similar	**20**	**20%**
Not sure	**10**	**10%**



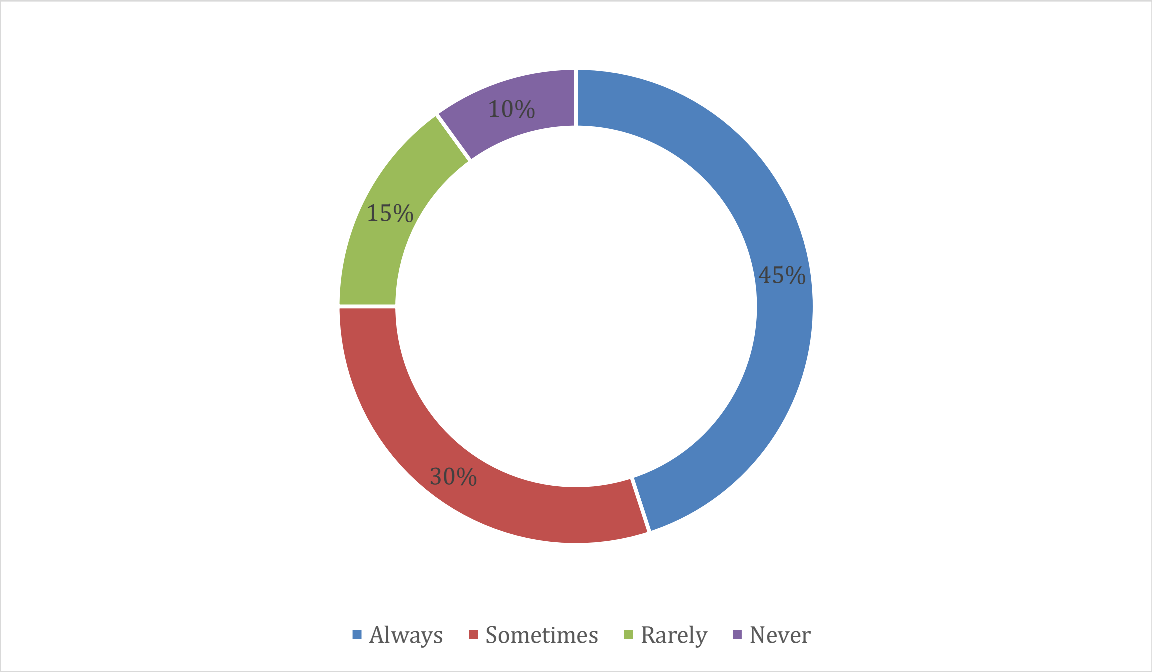
Graph : 8

Interpretation:

Half of the respondents (50%) believe actively managed funds carry higher risk, possibly due to the frequent buying and selling strategies employed by fund managers.

Table 9: Before investing, do you compare the fund's historical performance and expense ratio?

Particular	No. of Respondents	Percentage
Always	**45**	**45%**
Sometimes	**30**	**30%**
Rarely	**15**	**15%**
Never	**10**	**10%**



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Interpretation:

45% of respondents always compare historical performance and expense ratios before investing, showing that many investors are conducting due diligence before selecting funds.

Findings

- Based on the primary data collected and analyzed, the following key findings have emerged:
  Income Group of Investors: A majority of mutual fund investors (40%) belong to the ₹5 lakh – ₹10 lakh annual income bracket, indicating that middle-income individuals form the core segment investing in mutual funds.
- Investment Experience: Most respondents (40%) have been investing in mutual funds for a period of 1–3 years, suggesting that mutual fund investing is a relatively recent activity for many.
- Preference for Fund Type: 35% of the respondents prefer investing in actively managed mutual funds, while 30% prefer a balanced approach by investing in both actively and passively managed funds.
- Reason for Fund Selection: Higher returns (40%) were cited as the primary reason for fund selection, followed by lower costs and professional fund management.
- Satisfaction with Returns: Half of the respondents (50%) reported being satisfied with the returns generated from their mutual fund investments, while 20% reported being very satisfied.
- Perception of Better Returns after Costs: 45% of the respondents believe that actively managed funds deliver better returns after accounting for costs, although a considerable 30% feel passive funds are better in this aspect.
- Awareness of Expense Ratios: A significant 70% of investors are aware that actively managed funds generally have higher expense ratios compared to passively managed funds.
- Perception of Risk: Half of the respondents (50%) perceive that actively managed funds carry higher risk, whereas 20% believe passive funds also involve similar risk levels.
- Investment Analysis Behavior: 45% of investors reported that they always compare a fund’s historical performance and expense ratio before investing, showing a responsible and informed approach toward mutual fund selection.

Conclusion

"Our study set out to understand how investors perceive the performance of actively managed and passively managed mutual funds. We collected data from investors and found that while many still prefer actively managed funds for their potential to deliver higher returns, there's a growing interest in passively managed funds, especially among those who are cost-conscious and risk-averse.

Most of the investors we surveyed were relatively new to mutual fund investing, with most having invested for 1-3 years. When choosing a fund, investors are driven by the potential for higher returns, lower costs, and professional management. While many are satisfied with the returns, they're also keenly aware of the cost factor and its impact on their investments.

One encouraging finding is that investors are becoming more informed about the differences between active and passive funds, particularly when it comes to expense ratios. However, perceptions of risk vary, with many associating actively managed funds with higher risk.

What's heartening is that many investors are taking a thoughtful approach to investing, comparing historical performance and expense ratios before making decisions. This suggests that investors are becoming more mature and informed in their investment choices.

Overall, our study suggests that while actively managed funds remain popular, passively managed funds are gaining traction due to their cost-efficiency and stable returns. To help investors make informed decisions, it's essential to provide ongoing education and transparent performance reporting. By doing so, we can empower investors to make choices that align with their financial goals and risk tolerance."

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