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An Analysis of Gap between the Public and Private Sector Mutual Funds in India

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Abstract

The mutual fund industry has become extremely popular in Indian financial system. A mutual fund works on the principle of collective investment and is expected to provide the benefits of diversification and professional management. Mutual fund is an investment avenue designed primarily for the investors having small and infrequent savings and lacking requisite skills for investment management. Thus, the mutual funds are significant financial intermediary collecting funds mainly from small investors and investing them in financial market securities. The paper tries to establish the gap between the public and private sector mutual funds in India with the help of Gap Index Analysis. The study covers the period from the year 1998-99 to 2009-10. The study based on the secondary data which has been collected from the fact books and published annual reports of both types of mutual funds for the twelve years. The paper found that the private sector mutual funds are gaining more in terms of magnitude of mobilization of funds compared to that of public sector mutual funds. Further, the study also found that there is a strong evidence of relationship between the pattern of the gap movement between mobilization of funds and redemption / repurchase of public and private sector mutual funds.

Keywords: Mobilization of funds, Redemption, Repurchase, Public and Private Sector Mutual Funds and Gap Index, Net in / out flow.

1. Introduction

Mutual funds play an extremely crucial role in Indian economy. Mutual fund industry today is one of the most attractive investment avenues in India. Mutual fund is a good investment option for the medium and small investors who have the limited resources and do not have a professional knowledge about the stock market and other investment opportunities. Mutual funds are the significant financial intermediary collecting funds mainly from small investors and investing them in financial market securities. A mutual fund is an investment company or trust that pools the resources of thousands of its shareholders or unit holders and investment on behalf of these diversified securities and a cross section of companies to attain the objectives of the investors, which in turn achieve income or growth or both i.e. steady return or capital appreciation or both along with low risk. Thus, mutual funds offer several benefits to the investors like diversification, professional management, tax benefits, transparency, liquidity, flexibility, choice of schemes and low cost etc.

The mutual funds has serve as a concept to intermediate for the convenience of investing comparatively with a small amount portfolio-management and some other such facilities to increase the investors attraction towards the capital markets of the country. Although the concept of mutual funds in India is not so old as it have been evolved in the rest of globe. It was first adopted in Netherlands (1822) by King William 1, while some others have opinion that this concept has been first started by Dutch merchant adriaan van ketwich who created his investment trust in 1774. Ketwich has given the theory that diversification may increase the appeal of investments to smaller investors with minimal capital. The name of Ketwich fund was Eendragt Maakt Magt, which means “unity creates strength”.

Modern mutual fund has been first created in 1924 in Massachusetts, as Massachusetts in Boston. In India the mutual funds industry has been pioneered with the enactment of unit trust of India act 1963, which started its operations in 1964. The encouraging trend has been observed since 1964, which may be discussed in the form of some phases. Resource mobilization in an economics’ context may be defined as movement of money or money-equals from the non/less productive section to productive section. In Indian mutual funds industry the growth in the form of assets under management (AUM) in sept.2004 ₹ 153108cr which was ₹ 121805cr in Jan 2003 and ₹ 4564cr in March 1987.

Mutual funds are the associations or trusts of members for the mutual benefit of its members, who are willing to invest in the corporate sector in their financial instruments or financial assets of those companies or business firms. The funds collect the savings of the members and then invest them in a diversified and managed portfolio, in order to maximize the returns and minimize the risk, so that the members get capital-appreciation and a portion of income. The motivating part behind evolution of such funds is economies of scale, diversified portfolio, portfolio management and large investment avenues in the form of various schemes etc.

Mutual funds increase the mobilization of invertible funds of the community by pooling the interest of a great number of small savers towards the financial system of the country. In India, development of such mutual funds can well grow the rural economy of the country. Mutual funds, in India, are being regulated with the supervision of “Securities and Exchange Board of India” and the apex bank in the country, “Reserve Bank of India”. Mutual funds are authorized to work as a mutual fund, by the guidelines of securities exchange board of India (SEBI).

According to Department of Public Enterprises (DPE), “The mutual-funds registered with and regulated by SEBI, where the Government, its financial institutions and public sector banks holds/hold individually or collectively more than 50% of equity in the Asset Management Company of that mutual funds”. On the contrary the Asset Management Company (AMC), who’s more than 50% of equity paid-up capital is being held by private company/ies or private sector business houses, is known as Private Sector Mutual Funds. In India the public sector mutual funds have been set-up first, by the State Bank of India (SBI) as MRIS (Magnum Regular Income Scheme), 1987.

2. Review of Literature

Gali (1995) evaluated the past performance of the mutual funds and assessed the factors that have an influence on the performance. The factors considered were portfolio turnover, size and expenses charged to the fund. He further found that mutual funds in general do not provide risk adjusted returns. It was also found that mutual funds do not have market timing ability. **Gupta and Sehgal (1998)** tried to find out the investment performance of 80 schemes managed by 25 mutual funds, 15 in private sector and 10 in public sector for the time period of June 1992-96. The study has examined the performance in terms of funds diversification and consistency of performance. The study concluded that mutual fund industry’s portfolio diversification has performed well. But it supported the consistency of performance. **Sahadevan and Thiripalraju (1997)** analyzed the performance of private sector funds. They compiled and analyzed the monthly average return and standard deviation of 10 selected private sector-funds. The investigation revealed that in terms of the rate of return, 5 funds viz., Alliance 95, ICICI Power, Kothari Prima, Kothari Pioneer Blue Chip and Morgan Stanley Growth Fund outperformed the market, during the period of comparison. The analysis also showed that, by and large, performance of a fund is not closely associated with its size. **Block & French (2000)** emphasised the importance to use multiple index while evaluating the performance of equity mutual funds. **Rao (2003)** studied the performance evaluation of Indian mutual funds in bear market through relative performance index. He found that most of the mutual fund schemes were able to satisfy investor’s expectations by giving excess returns over expected returns. **Zakri Y. Bello (2005)** matched a sample of socially responsible stock mutual funds matched to randomly select conventional funds of similar net assets to investigate differences in characteristics of assets held, degree of portfolio diversification and variable effects of diversification on investment performance.

In light of the above a project was taken to delineate the difference or similarity between the performance of public sector and private mutual funds. The public sector of mutual funds comprises of the mutual funds sponsored by public-sector banks, financial-Institutions along with Unit Trust of India (UTI). All other mutual funds sponsored by the private companies or business houses are taken under this category.

3. Justification of the Study

The growth of mutual funds in India has attracted the attention of Indian researchers, individuals and institutional investors over the last couple of years. Mutual funds are the vehicles for mobilization and canalization of savings from individuals and house holds towards the capital markets. In other words, the concept of mutual funds was conceived to pool the resources of small and retail investors and deploy the same in the capital market through participation in equity and debt instruments. Therefore, mutual funds are significant financial intermediary collecting funds mainly from small investors and investing them in financial market securities. Thus, the mutual funds play an important role in Indian economy.

An effort has been made in this study to establish the gap between the private and public sector mutual funds in India with the help of the Gap Index Analysis. The findings may help the small investors, households, institutional investors to find out the new ideas techniques or methods to make the investment strategies, to analyse and compare the performance of public and private sector mutual funds in India.

4. Objectives of the Study

The following are the main objectives of the study:

1. To study the Gap mobilization of resources in public and private sector mutual funds.
2. To study the gap in redemption / repurchase by the public and private sector mutual funds.
3. To compare the performance of public and private sector mutual funds in India.

5. Research Methodology

Two mutual funds viz. public sector mutual funds and private sector mutual funds have been selected for the purpose of this study. Both the mutual funds in their respective business are playing the crucial role in the Indian economy. The study is based on the secondary sources of information which is collected from the various related fact books alongwith the AMFI, SEBI, published annual reports, manuals and other office records. The study covers the period of twelve years i.e. from 1998-99 to 2009-10. Editing, classification and tabulation of the financial data which has been collected from the above mentioned sources have been done as per the requirement of the study. For the purpose of analyzing the collected data of both the categories of funds, mean, percentage and correlation coefficient have been applied. In order to measure the extent of difference between various parameters of study regarding mutual funds with their special reference to mobilization of fund, repurchase/redemption, cumulative net assets position, net in/out flow of the two sectors of mutual funds industry i.e., private sector mutual funds and public sector mutual funds, the Gap-Index Analysis will be carried out as suggested by Sharad Kumar and Sreeramulu (2007). The Gap-indices will be worked out as a percentage of the difference of the value of the variables between public and private sector mutual funds (PB and PR) as ratio of aggregate value. The purpose of the Gap-index construction is to see whether or not the gap between two sectors is changing over period of study (1998-99 to 2009-10). It is suitable to give graphical presentation of the changing pattern in the gap, to have and idea about the fluctuations in gap. The analysis through Gap-Indices is considered as a non-parametric technique and advanced statistical techniques are not considered appropriate as gap between two sets of mutual funds (public and private), on the variables are expected to be quite large.

- GAP-INDEX (G.I) = $|\{(PB-PV)|/(PB+PV)\}$ X100

6. Limitation of the Study

The following are the main limitations of the study:

1. The study confined only public and private sector mutual funds in India.
2. The study is covers only twelve years i.e. from 1998-99 to 2009-10.
3. The study is based only the secondary sources of information.
4. A symmetry problem of timing for getting equal times results of mutual funds was the main problem.
5. Only the gap index analysis has been used to draw the conclusions.
6. The study covers only the two aspect i. e. mobilization of funds and repurchases and redemptions of mutual funds in India.

7. Profile of the Sample

- **Public-Sector-Mutual funds:** According to Department of Public Enterprises (DPE) "The mutual fund registered with and regulated by SEBI, where the government, its financial institution and public sector banks holds/hold individually or collectively more than 50% of equity in the Asset Management Company of that mutual funds. Mutual funds occupy a large share of the primary market of Certificates of Deposit (CDs) and CPs. As on June 10, 2011, the total holdings of mutual funds in CDs and CPs remained at Rs.2, 95,164 crore (66 per cent of the aggregate outstanding) and Rs.82, 951 crore (65 per cent of the aggregate outstanding) respectively. Mutual funds have also provided substantial liquidity to the secondary market segments of CPs and

CDs. Their increased activity in the secondary market corresponds to their growing portfolio of money market investments. During the last six months, mutual funds share in the daily turnover the secondary market of CDs and CPs stood at around 41 per cent and 46 per cent respectively.

- **Private Sector Mutual Funds**: The succeeding decade showed a new horizon in Indian mutual fund industry. By the end of 1993, the total AUM of the industry was Rs. 470.04 bn. The private sector funds started penetrating the fund families. In the same year the first mutual fund regulations came into existence with re-registering all mutual funds, Bank of India mutual fund. Kothari Pioneer was the first private sector mutual fund company in India which has now merged with Franklin Templeton. Just after ten years with private sector players' penetration, the total assets rose up to Rs. 1218.05 bn. Major mutual fund companies in India ABN AMRO mutual fund was set up on April 15, 2004 with ABN AMRO Trustee (India) Pvt.Ltd, as the Trustee Company. The AMC, ABN AMRO Asset Management (India) Ltd. was incorporated on November 4, 2003. Deutsche Bank is the custodian of ABN AMRO mutual fund. Birla Sun Life mutual fund is the joint venture of Aditya Birla Group and Sun Life Financial. Sun Life Financial is a global organization evolved in 1871 and is being represented in Canada, the US, the Philippines, Japan, Indonesia and Bermuda apart from India. Birla Sun Life mutual fund follows a conservative long-term approach to investment. Recently it crossed AUM of ₹ 10,000 crores. Bank of Baroda mutual fund (BOB Mutual Fund) was setup on October 30, 1992 under the sponsorship of Bank of Baroda. BOB Asset Management Company Limited is the AMC of BOB Mutual Fund and was incorporated on November 5, 1992. Deutsche Bank AG is the custodian.

8. Analysis and Interpretration

The Gap Index Analysis has been used to measure the extent of difference between mobilization of funds and repurchase / redemption of the public and private sector mutual funds in India. These variables are being analysed in Table 1, 2 and Graph 1, 2 as under:

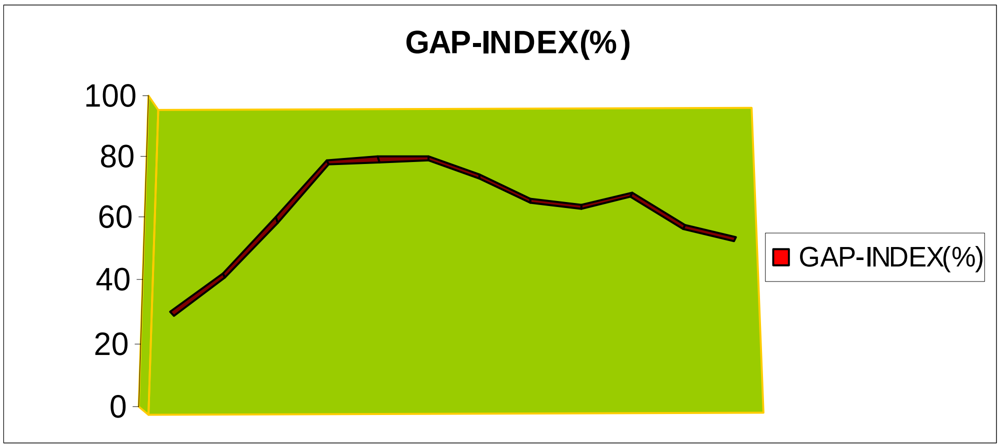
9. Gap-Index Analysis of Mobilization of Funds in Publlic and Private Sector

In order to measure the extent of different between mobilization of funds by public-sector and private sector mutual funds spread over 12-years period of study, the Gap-Index-Analysis was adopted as per methodology discussed earlier. The table 1 gives the gap index values in respect of mobilization of funds for private sector and public-sector mutual funds from 1998-2010.

Table 1: Gap Index For Mobilization of Funds in Public-Sector and Private Sector Mutual Funds.

YEARS	PB	PV	GAP-INDEX (%)
1998--99	14864.23	07846.50	31
1999--00	17515.57	43725.66	43
2000--01	17948.28	75009.11	61
2001--02	16724.91	147798.26	80
2002--03	30610.70	284095.49	81
2003--04	55540.59	534649.28	81
2004--05	103245.07	736463.30	75
2005--06	183446.05	914703.26	67
2006--07	338619.53	1599873.44	65
2007--08	683623.69	3780752.63	69
2008--09	1133602.96	4292750.31	58
2009--10	2320539.26	7698483.37	54

Source: Complied from the Annual-Reports



Graph 1

Table 1 exhibits the gap index values in respect of mobilization of funds for public and private sector are 31 % in the year 1998-99, 43 % in 1999-2000, 61 % in 2000-01, 80 % in 2001-02, 81 % in 2002-03 and 2003-04, 75 % in 2004-05, 67 % in 2005-06, 65 % in the year 2006-07, 69 % during the year 2007-08, 58 % in 2008-09 and 54 % in the year 2009-10. Thus, it ranged from 31 % in the year 1998-99 to 54 % in the year 2009-10. This shows that the gap has been widening very fast up to 2003-04 and has shown a decline thereafter. The analysis also suggests that the private sector mutual funds are gaining more in terms of magnitude of mobilization of funds compared to that of public sector mutual funds. The pattern of the trend of movement of the gap between the two has also been shown in Graph 1. The figure has suggested that the gap reaching up to 81% in 2003-04 from 31% in 1998-99 and finally settled at 54% in 2009-10. If the trend continues to be the same it is likely that the both the private and public sector mutual funds may come more closure to each other in terms of mobilization of funds.

10. Gap-Index Analysis of Redemption/ Repurchase in Public and Private Sector Mutual Funds

In the above analysis, we have measured the gap between two-sectors and accordingly it is essential to analyze the gap between redemption/repurchase also as this sub-segment is directly associated with the mobilization of funds. The Gap-Index Analysis carried out for Redemption / Repurchase in respect of public sector and private sector utual funds spread over a period of 12 years and presented in Table 2.

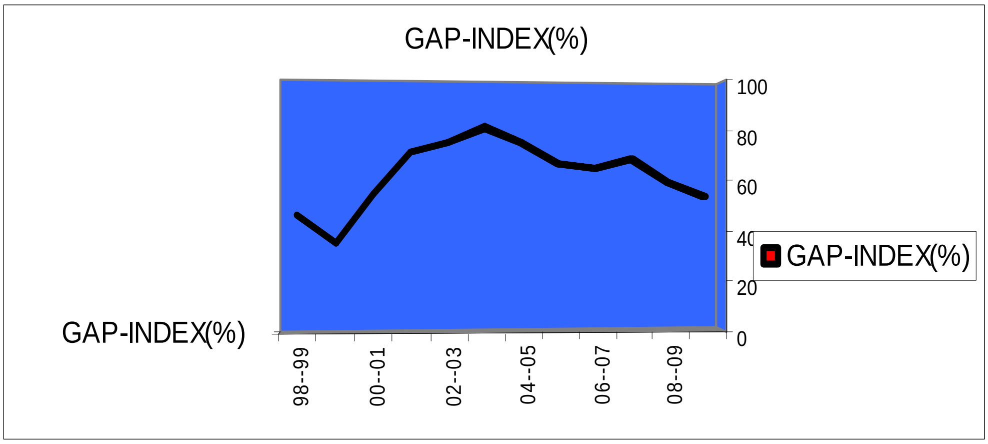
Table 2 depicts the gap index values in respect of redemption / repurchase of public and private sector mutual funds are 46 in the year 1998-99, 35 in 1999-2000, 55 in 2000-01, 81 in 2001-02, 75 in 2002-03, 81 % in 2003-04, 75 % in 2004-05, 67 % in 2005-06, 65 % in the year 2006-07, 69 % during the year 2007-08, 59 % in 2008-09 and 54 % in the year 2009-10. Thus, it fluctuated from 46 in the year 1998-99 to 54 % in the year 2009-10. It appears on the analysis that the year 1998-99 being an out liar or abnormal (a reported earlier also), the index has shown some difference but however from 1999-2000 onwards a steady growth is observed up to 2003-04 with a peak of 81% Gap-Index, which appears to be significantly high. As in the case of the mobilization of funds the gap in redemption also started receding there after and touched a point of 54% of gap-index during 2009-10. however if the trend goes like this it may be projected that the redemption in private and public sector mutual funds may show quite closeness after 2009-10.The pattern or the trend on gap-index has also been shown in graph 2 and Graph 3 shows the gap indices.

Table 2: Gap-Indexes For Redemption / Repurchase of Public and Private Sector Mutual Funds.

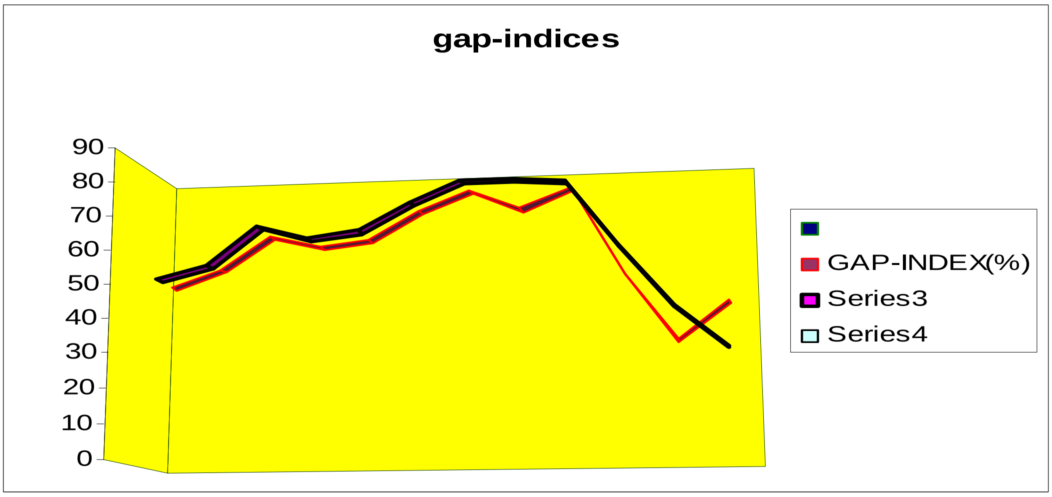
YEAR	R/RPB	R/RPV	GAP-INDEX (%)
1998--99	17266.6	6393.8	46
1999--00	13712.17	28559.18	35
2000--01	18669.78	65159.59	55
2001--02	22599.6	134748.37	81
2002--03	38483.75	272026.05	75
2003--04	51276.66	492104.78	81
2004--05	105644.26	728863.8	75
2005--06	173643.6	871726.53	67
2006--07	323672.4	1520835.78	65

2007--08	663126.07	3647448.68	69
2008--09	1127881.65	4326767.88	59
2009--10	2292387.2	7643555.18	54

Source: Complied from the Annual-Reports.



Graph 2



Graph 3

11. Correlation Analysis

- In order to measure the relation between gap-index of mobilization of funds and redemption/repurchase, the Karl Pearson's coefficient of correlation(r) also calculated. The coefficient of correlation (r) is found to be of the order of .92 and is found to be significant at 1% level of significance. The analyses suggest that there is strong evidence of relationship between the pattern of the gap–movement over different periods of the study between mobilization of funds and Redemption/Repurchase of public sector and private sector mutual funds. Graph 3 shows the superimposition of the two Gap-Indices curves and the relationship is self-explanatory.

- However it may be mentioned here that the individual growth in mobilization of funds for public and private sector are 63% and 75 % respectively. In the case of redemption / repurchase these are 63 % and 80 % respectively, which further strengthen the idea that the redemption / repurchase are showing almost the same status of growth as in the case of mobilization of funds. This phenomenon has been observed with a high-degree of correlation between gap-indices as discussed above.

12.Conclusions and Suggestions

On the basis of foregoing analysis, the following conclusions and suggestions can be made:

1. To measure the extent of difference between mobilization of funds by public and private sector, the period spreads over 12 years. The Gap-Index Analysis was adopted. It is observed that the gap has been widening very fast up to 2003-04 and has shown a decline thereafter.
2. The private sector mutual funds are gaining more in terms of magnitude of mobilization of funds compared to that of public sector.
3. The gap is reaching up to 81 % in 2003-04 from 31 % in 1998-99 and finally settled at 54 % in 2009-10.
4. If the trend continues to be the same it is likely that both the private and public sector mutual funds may come more closure to each other in terms of mobilization of mutual funds.
5. The Gap-Index-Analysis suggest that the year 1998-99 being an outlier or abnormal (as reported earlier also). The index shows some difference but from 1999-00 onwards a steady growth is observed up to 2003-04 with a peak of 81 % Gap-Index.
6. The gap in redemption also started receding after 2003-04 and touched a point of 54 % during 2009-10.
7. It may be projected that the redemption in private and public sector mutual funds may show quite closeness after 2009-10.
8. To measure the relation between Gap-Index of mobilization of fund and redemption / repurchase a high degree of co-efficient of correlation of the order of .92 is found to be significant at 1 % level of significance.
9. The analysis suggests that there is a strong evidence of relationship between the pattern of the gap movement between mobilization of funds and redemption / repurchase of public and private sector mutual funds.

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