Review Of Research
ISSN 2249-894X

Impact Factor : 3.1402(UIF)
Volume - 5 | Issue - 1 | Oct - 2015

ROLE OF MUTUAL FUNDS IN FINANCIAL MARKET AND RISKS INVOLVED IN MUTUAL FUNDS

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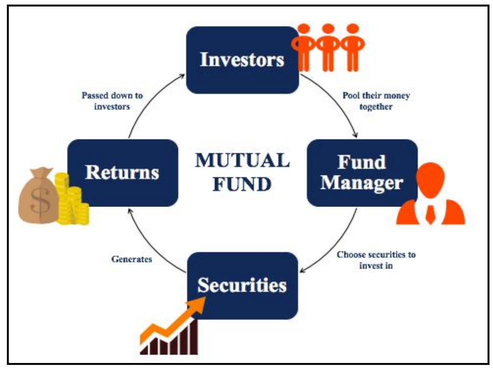
ABSTRACT

Indian Mutual Funds have significance in investment pattern and investment style in fiscal system and plays a poignant role in building finance system. Mutual funds have paved a new way for investors and it has become easy choice because of its liquidity and flexibility. It has become a marvel in the commercial banks and financial market. The dynamic contribution of Mutual Funds in stimulating monetary growth can be seen not only in terms of their sharing in the saving market but also in their dominant presence in the money and capital market.



KEYWORDS: *Mutual Fund Risks, Mutual Fund Market, Investor Perception.*

MUTUAL FUNDS AND FINANCIAL MARKET

A developed financial market is perilous to general economic development, and Mutual Funds play an active role in promoting a progressive capital market. The asset croft form of mutual funds in India indicates the dominant role of Mutual Funds in the capital market and money market. Moreover, they have also rendered critical support to securities mortgage loans and municipal bond market in India.

In India, Mutual Funds provide very active sustenance to the secondary market in terms of purchase of securities. Investors' preference form in India has undergone a sea of change during current times, along with the changes in the share of pecuniary assets in the total annual savings. Indian investors have moved towards more liquid and growth-oriented trade able tools likes shares/debentures and units of Mutual Funds. The shift is asset croft pattern of investors has been suggestively predisposed by the 'equity' and 'unit' culture while the holders of company shares and debentures are focused in the urban areas, small/medium investors in the semi-urban and rural areas are inclining towards Mutual Funds. Mutual Funds in India have definitely shaped awareness among investors about equity-oriented investments and its benefits.

IMPORTANCE OF MUTUAL FUND

Small investors face a lot of difficulties in the share market, limited resources, lack of expert advice, lack of information etc. Mutual funds have come as a much-desired help to these investors. It is a special type of institutional device or an asset vehicle through which the investors pool their savings which are to be invested under the guidance of a team of experts in wide variety of ranges of corporate securities in such a way so as to minimize risk, while ensuring safety and steady return on investment. It forms an important part of the capital market, providing the benefits of a diversified portfolio and expert fund management to large number particularly small investors. Nowadays, mutual fund is gaining its admiration due to the following reasons:

1. As mutual funds are accomplished by experts, they are considered to have a better knowledge of market performances. Besides, they bring a certain capability to their job. They also maximize gains by proper selection and timing of speculation.
2. Another important thing is that the payments and capital gains are reinvested routinely in mutual funds and, hence, are not fritted away. The automatic reinvestment feature of a mutual fund is a form of involuntary saving and can make a big difference in the long run.
3. The mutual fund maneuver provides a realistic protection to investors. Besides, presently all schemes of mutual funds provide income tax relief under Section 80 L of the Income Tax Act and in addition, some outlines provide tax relief under Section 88 of the Income Tax Act lead to the development of importance of mutual fund in the minds of the investors.
4. As mutual funds create responsiveness among urban and rural middle-class people on the benefits of venture in capital market, through profitable and safe avenues, mutual fund could be able to make up a large amount of the excess funds available with these people.

ROLE OF FUND MANAGERS

The mutual fund is administered by a professional investment manager who buys and sells securities for the most active growth of the fund. As a mutual fund investor, one has become a "shareholder" of the mutual fund company. When there are profits, Fund manager will earn dividends. When there are losses, shares will decrease in value. The investment experts who invest the pooled money on behalf of investors of the scheme are known as Fund Managers. These fund managers take the investment pronouncements pertaining to the selection of securities and the proportion of investments to be made into them. However, these pronouncements are administered by certain strategies which are decided by the investment objectives, investment pattern of the scheme and are subject to controlling restrictions. It is this investment objective and investment pattern which also guides the investor in choosing the right fund for his investment purpose.

RISKS INVOLVED IN MUTUAL FUNDS

Mutual funds also include perils and risks which the investors have to confront while investing in the industry.

1. The companies in which the fund has invested might perform poorly, suffer misconduct.
2. Some economic, political or other development might cause the overall market to fall, dragging down with it the holdings of one’s particular fund.

Managing Risks

Mutual funds offer unbelievable flexibility in managing investment risk.

Diversification and Automatic Investing (SIP) are two key techniques one can use to reduce investment risk considerably and reach your long-term financial goals.

Diversification

When one invests in one mutual fund, it is instantly spread risk over a number of different companies. One can also diversify over several different kinds of securities by investing in different mutual funds, further reducing potential risk. Diversification is a basic risk management tool that one will want to use throughout lifetime as rebalance portfolio to meet changing needs and goals. Investors, who are willing to maintain a mix of equity shares, bonds and money market securities, have a greater chance of earning significantly higher returns over time than those who invest in only the most conservative investments. Additionally, a diversified approach to investing combining the growth potential of equities with the higher income of bonds and the stability of money markets helps moderate your risk and enhance your potential return.

Types of Risks

These common types of risk and assess them against probable rewards when one selects an investment in Mutual fund.

Market Risk

At times the prices of all the securities in a particular market rise or fall due to wide external influences. When this happens, the stock prices of both an outstanding, highly profitable company and a new corporation may be affected. This change in price is due to "market risk".

Inflation Risk

Inflation risk also occurs when prices rise faster than returns.

Credit Risk

In short, how steady is the company or entity to which one lends money for investment.

Exchange Risk

A number of companies generate revenues in foreign currencies and may have investments or expenses also denominated in foreign currencies. Changes in exchange rates may, therefore, have a positive or negative impact on companies which, in turn, would have an effect on the investment of the fund.

Investment Risk

The sectorial fund schemes, investments will be predominantly in equities of select companies in the particular sectors. Accordingly, the NAV of the schemes are linked to the equity performance of such companies and may be more volatile than a more diversified portfolio of equities.

Change in the Government Policy

Sudden and tentative changes in Government policy, especially in regard to the tax benefits, may have its impact on the business predictions of the companies leading to an impact on the investments made by the fund. Mutual Fund schemes can be categorized into different categories and subcategories based on their maturity periods and their investment objectives.

CONCLUSION

Considerably there are optimal risks jolt the process and minds of small investors in Mutual funds. Likewise, an open-ended fund is a deposit that is available for subscription and can be redeemed on a continuous basis. It is available for subscription throughout the year and investors can buy and sell units at NAV related prices. These funds do not have a fixed maturity date. The key feature of an open-ended fund is liquidity. In addition, a close-ended fund is a fund that has a distinct maturity period, e.g. 3-6 years. These funds are open for subscription for a specified period at the time of preliminary launch. These funds are listed on a recognized stock exchange. Moreover, Interval funds combine the types of open-ended and close-ended funds. These funds may trade on stock exchanges and are open for sale or renovation at programmed intervals on the prevailing NAV. A careful study of investment pattern and financial expert on right product will always yield in good returns from the money invested in mutual fund.

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