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Debt Funds – A Prominent Player In Indian Mutual Fund Industry

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Abstract:
We analyze the role of debt in corporate governance with respect to a large emerging economy, India, where debt has been an important source of investment. Several mutual funds have diverted a large portion of their portfolios into debt schemes. Debt funds are low risk profile funds that seek to generate fixed current income to investors. This study aims at investigating the immense existence of debt segment of mutual funds by way of capturing the greater market stand. In this context, the main emphasis of this study is on examining the performance of debt segment in comparison to the other segments of mutual funds. The trend and present status of debt funds in the Indian Mutual Funds Industry will also be examined. To attempt these purposes the study has relied on secondary data. Secondary data have been collected from various journals viz. Indian Journal of Accounting, Indian Journal of Finance, Finance India, text books, publications, such as, Handbook of Statistics published annually by Reserve Bank of India, SEBI Bulletin, web sites, such as, amfiindia.com, nseindia.com, mutualfundsindia.com, and other institutional monthly brochures etc..

Key words*: mutual fund, debt funds, investors, market, portfolio.*

1.Introduction

Corporate governance is the in-thing nowadays, both in India and globally. Following financial liberalisation a new paradigm for corporate governance is moving with times. However, corporate governance is concerned with establishing a system where by directors of a company/concern are entrusted with responsibilities and duties in relation to running of company's affairs besides maximizing Shareholders welfare. The literature on corporate finance and governance widely recognizes debt as an important mechanism for solving agency problems in corporations characterized by separation of ownership and control. Specifically, debt could be an effective disciplining device in the hands of shareholders which can be used strategically to curb managerial actions that run counter to the objective of shareholder-value maximization. The effectiveness of debt as a disciplining device or as a mechanism for expropriation is considered to depend on the institutional context within which corporations are embedded such as the presence of a well-developed capital market and banking systems, effective bankruptcy laws, active takeover markets, and transparent auditing, accounting and disclosure norms.

The need for systematic and robust evidence on the precise governing role of debt in emerging economies like India is underscored by the fact that country level experiences show that the quality of debt governance has important system-wide ramifications, and that prior knowledge of the underlying dynamics and timely institutional reforms are important to guard against systemic crisis. A case in point is the East Asian crisis, with regard to which Prowse observes that notwithstanding the disciplining effect that debt is posited to have on company management, the extensive use of debt financing did little to loosen the grip of the insiders as the controlling power of debt was weakened by weak monitoring by financial institutions, weak market and statutory regulations, legal protection of outside shareholders, high ownership concentration and poorly competitive financial systems, all of which together not only imposed high and severe costs on the economy, but may have contained the seeds of crises. In this light the objective of this study is to examine the performance of debt funds in investment perspectives so that the role of debt fund can be analysed.

Debt funds are funds that invest in "debt instruments", which include government securities, corporate bonds and money market instruments. These are called debt instruments because the issuers have borrowed money from the lender (investors) by issuing these securities. These "debts", mainly known as "bonds", are income generating properties i.e. investors receive regular interest payments on them. These payments could be monthly, semi-annually or annually. However, many of the most attractive debt instruments are unavailable directly to the retail investors. But, they can invest in those debt instruments indirectly through debt funds. For retail investors Debt Mutual Funds are the best way to invest in debt i.e. income generating instruments.

In order that mutual fund managers act in a judicious manner so as to bring about ultimate beneficial consequences to the investing community, it is essential that the performance of such funds is evaluated. Such an appraisal would help the funds compare themselves with other funds, besides being a potential source of information to the present and prospective investors, especially the small investors.

2.Review Of Literature

With the growing importance of the subject under study, some literature covering different aspects of investors' preferences have been produced by economists, researchers and practitioners are mentioned below:

Faccio et al. (2001) studied with respect to a cross-section of East Asian and European countries find evidence of expropriation through debt in corporations with concentrated ownership and control. The study particularly finds the level of such expropriation to be lower with respect to the European firms, the difference being attributed to the existence of better governance institutions in Europe.

Jambodukar (1996) conducted a study to access the awareness of mutual funds among the investors, to identify the sources of information that influences the buying decision that have an impact on buying behaviour and ultimately become a determinant factor in the choice of a particular fund. The study reveals among other thing that income schemes and close ended scheme are more preferred than growth schemes and close ended schemes during that prevalent market conditions.

Jensen (1986) studied the disciplining effect of debt, as the "control hypothesis" of debt creation, arises from the fact that debt can constrain managerial expropriation in a situation where corporations have more internally generated funds than investment opportunities in terms of the availability of projects with positive net present value.

Leite and Cortez (2009: 565) estimated and compared the performance of Portuguese-based mutual funds that invest in the domestic market and in the European market using unconditional and conditional models of performance evaluation. The study shows the mutual fund managers are not able to outperform the market.

Ralph (1999) in his book Investing for Income - A Bond Mutual fund Approach to High-Return, Low-Risk, Profits outlines fresh, easy to understand insights into maximizing income while lowering risk. In this literature, investing for income reveals the convincing reasons that by investing in bond funds the return would be more desirable.

Sivakumar et.al. (2010) evaluated the performance of mutual funds players in India based on their resource mobilization during the past decade. The study found that the players are broadly classified in to public and private participants. The study revealed that there is significant contribution by all the participants for the growth of the mutual fund industry in India.

Tiwari (2008: 99-147) deals with outlining how to invest in stock market and mutual funds. It provides a comprehensive parameters relating to selection of a mutual fund. The study also outlines various guidelines of purchase and sale of mutual funds, tracking mutual funds performance, procedure of investing in mutual funds.

The study of existing literature found the theoretical framework for investing in the mutual fund industry. But given the different theoretical parameters, investors often get puzzled to choose the right alternative among many. This study is a modest attempt to highlight the scenario of mutual fund industry over the last 12 years so to analyse the growth trend of different segments.

3.Objectives

- To see overall resources mobilised by mutual funds during the period 2001 to 2012.
- To analyse the trends in investment on stock exchange during the period 2001 to 2012 so as to the role of debt mutual funds.
- To study scheme-wise resource mobilization in different mutual fund schemes in general and in debt funds in particular for the current period.

4.Need For The Study

The study has covered the period of 2001-2012 i.e a decade. Since investors have growing interest in investing their savings in debt securities than the equity, the study is attempted to examine the performance of debt funds as well as their role of dominance as acting an eminent player in Indian Mutual Funds Industry. So an effort is made to give a comprehensive trends of mutual funds in now-a-days.

5.Data Source

The present study is based on secondary data. For the purpose of the study secondary data have been collected from various journals viz. Indian Journal of Accounting, Indian Journal of Finance, Finance India, text books, publications such as Handbook of Statistics published annually by Reserve Bank of India, SEBI Bulletin web sites such as amfiindia.com, nseindia.com, mutualfundsindia.com, and other institutional monthly broachers etc.

6.Discussion

Mutual funds play an important role in mobilising the household savings for deployment in capital markets and to examine this role let us look at the resources mobilised by mutual funds during the decade 2000-01 to 2009-10 in following table :

(Rs. Crore)

Period	Gross Mobilisation	Redemption	Net Inflow	Assets at the end of Period
2000-01	92,957	83,829	9,128	90,587
2001-02	1,64,523	1,57,348	7,175	1,00,594
2002-03	3,14,706	3,10,510	4,196	1,09,299
2003-04	5,90,190	5,43,381	46,808	1,39,616
2004-05	839,708	8,37,508	2,200	1,49,600
2005-06	10,98,149	10,45,370	52,779	2,31,862
2006-07	19,38,493	18,44,508	93,985	3,26,292
2007-08	44,64,376	43,10,575	1,53,802	5,05,152
2008-09	54,26,353	54,54,650	-28,296	4,17,300
2009-10	1,00,19,022	99,35,952	83,080	6,13,978
2010-11	88,59,515	89,08,921	-49,406	5,92,250
2011-12	68,19,679	68,41,702	-22,024	5,87,217

Table 1 : Mobilisation Of Resources By Mutual Funds
Source :compiled from SEBI Annual Report 2009-10
SEBI Bulletin August 2012

In the above table it is observed that the gross mobilisation of resources by all mutual funds during 2009-10 was at Rs.1,00,19,022 crore compared to Rs.54,26,353 crore during the previous year indicating an increase of 84.7 percent over the previous year.

Redemption also rose by 82.2 percent to Rs.99,35,942 crore in 2009-10 from Rs.54,54,650 crore in 2008-09. All mutual funds, put together, recorded a net inflow of Rs.83,080 crore in 2009-10 as compared to an outflow of Rs.28,296 crore in 2008-09. The assets under management by all mutual funds increased by 47.2 percent to Rs.6,13,978 crore at the end of March 2010 from Rs.4,17,300 crore at the end of March 2009 followed by gradual decrease in 2011 and 2012 by Rs.5,92,250 and Rs.5,87,217 respectively. In connection of the above table let us make in-depth study of trends in transactions on stock exchanges to examine the performances debt funds in relation to equity funds in table-2

(Rs. Crore)

Year	Equity			Debt			Total		
	Gross Purchase	**Gross Sales**	**Net Purchase/ Sales**	**Gross Purchase**	**Gross Sales**	**Net Purchase/ Sales**	**Gross Purchase**	**Gross Sales**	**Net Purchase/ Sales**
2000-01	17,376	20,143	-2,767	13,512	8,489	5,023	30,888	28,631	2,257
2001-02	12,098	15,894	-3,796	33,557	22,594	10,963	45,655	38,488	7,167
2002-03	14,521	16,588	-2,067	46,664	34,059	12,604	61,185	50,647	10,538
2003-04	36,664	35,356	1,308	63,170	40,469	22,701	99,834	75,825	24,009
2004-05	45,045	44,597	448	62,186	45,199	16,987	1,07,232	89,796	17,435
2005-06	1,00,436	86,133	14,303	1,09,720	72,969	36,801	2,10,202	1,59,102	51,104
2006-07	1,35,948	1,26,886	9,062	1,53,733	1,01,190	52,543	2,89,681	2,28,075	61,606
2007-08	2,17,578	2,01,274	16,306	2,98,605	2,24,816	73,790	5,16,183	4,26,090	90,095
2008-09	1,44,069	1,37,085	6,984	3,27,744	2,45,942	81,803	4,67,815	3,83,026	88,787
2009-10	1,95,662	2,06,173	-10,512	6,24,314	4,43,728	1,80,588	8,19,976	6,49,901	1,70,076
2010-11	1,54,217	1,74,018	-19,802	7,62,644	5,13,493	2,49,153	9,16,861	6,87,511	2,29,352
2011-12	1,32,137	1,33,494	-1358	11,16,760	7,81,940	3,34,820	12,48,897	9,15,434	3,33,463

Table 2: Trends In Transactions On Stock Exchange By Mutual Funds
Source: Compiled From Handbook Of Statistics 2009-10 And
Sebi Bulletin August 2012

The mutual funds were one of the major investors in the debt segment of the Indian securities market. During 2009-10, the combined net investments by the mutual funds in debt and equity was Rs.1,70,076 crore compared to Rs.88,787 crore in 2008-09, registering an increase of 91.5 percent. While during the year 2010-11 and 2011-12 the combined net investment by the mutual funds in debt and equity was Rs. 2,29,352 crore and Rs.3,33,463 crore. In the year 2011-12 Mutual Funds were net sellers in equity segment with Rs.1,358 crore, whereas, their net investments in the debt segment rose by Rs.3,34,820 crore during the same period. This performance can be more clearly understood with the help of graphical representation as under:

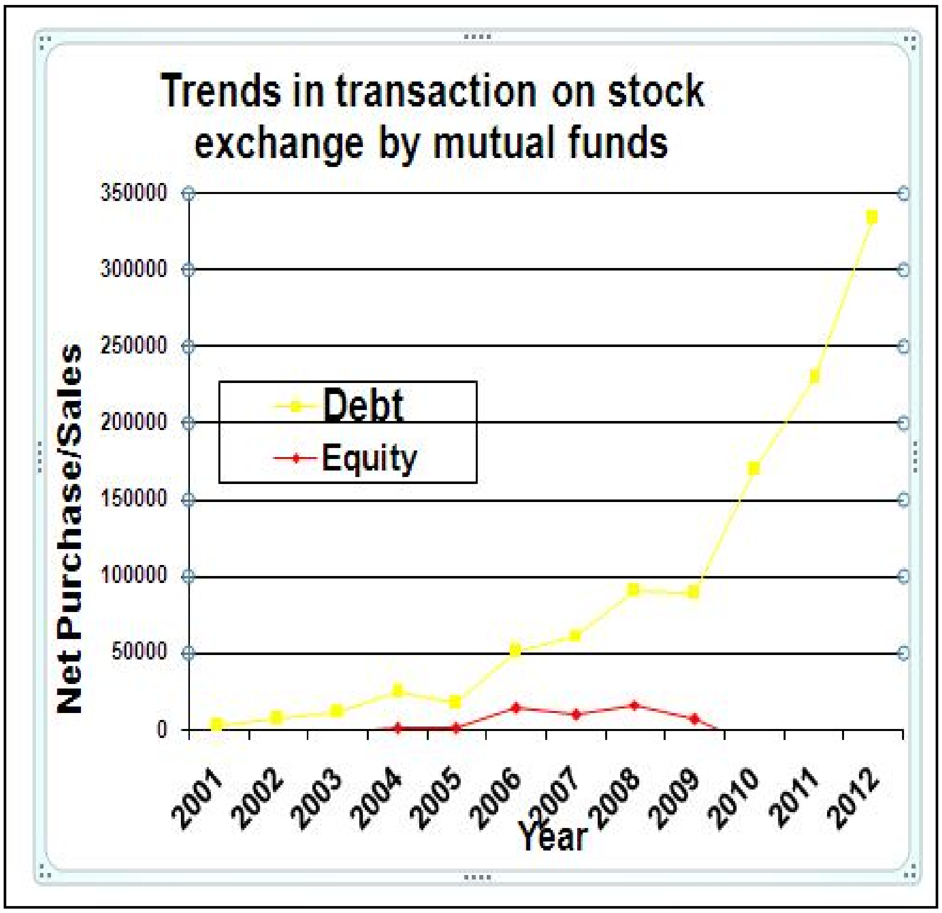

Figure 1

(Rs. Crore)

Schemes	Number of schemes	Gross Funds mobilised (Rs.crore)	Repurchase / Redemption (Rs.crore)	Net Inflow/ Outflow of Funds (Rs.crore)	Cumulative Assets Under Management (Rs.crore)
A. Income/Debt Oriented Schemes					
(i) Liquid/Money Market	51	65,99,724	66,03,244	-3520	73,666
(ii) Gilt	37	4,450	4,566	-116	3,409
(iii) Debt (other than assured return)	591	21,72,860	22,09,567	-36,707	2,91,975
Sub Total (i+ii+iii)	679	87,77,034	88,17,377	-40,343	3,69,049
B. Growth/Equity Oriented Schemes					
(i) ELSS	48	3,450	3,184	266	25,569
(ii) Others	328	63,142	76,547	-13,405	1,69,753
Sub Total (i+ii)	376	66,592	79,730	-13,13	1,95,322
C. Balanced Schemes					
(i) Balanced Schemes	32	7,490	6,145	1345	18,445
D. Exchange Traded Fund					
(i) Gold ETF	10	2,842	593	2,249	4,400
(ii) Other ETFs	18	4,867	3,479	1,388	2,516
Sub Total (i+ii)	28	7,709	4,072	3,637	6,917
E. Fund of Funds Investing Overseas					
(i) Fund of Funds investing overseas	16	689	1,596	-907	2,516
TOTAL (A+B+C+D+E)	1,131	88,59,515	89,08,920	-49,406	5,92,249

Table 3: Scheme-Wise Resource Mobilisation And Assets Under Management By Mutual Funds As On March 31st , 2011.

Source : Sebi Annual Report 2010-11

As on 31st March 2011 there were 1,131 schemes operating in mutual fund industry. Scheme-wise pattern reveals the domination of income/debt oriented schemes in total resource mobilisation during 2010-11. Under Income/debtoriented schemes, gilt funds and money market funds recorded net outflow of Rs 40,343 crore in 2010-11 as against net inflow of growth/equity oriented schemes of Rs.13,138 crore during 2010-11. Under the balanced schemes and Exchange Traded Fund schemes, there was a net inflow of Rs 1,345 crore and Rs.3,637 crore, respectively. Fund of funds which invest overseas also reported a net outflow of Rs. 907 crore in 2010-11.

7.Conclusion

It is revealed from the study that due to various doldrums and risks associated in equity market people are gaining interest to invest in debt mutual funds as it figuring out a regular income to the investors with a minimum risks. As well as from the above mentioned data it is evident that portfolios are immensely diversified and gaining huge outcome in capital market. Thus, from this study we can observe that the rational investors are more interested in debt funds rather than to invest in equity mutual fund schemes available in India.

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