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## Global Fund: An Exciting Investment Prospect

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### **Abstract**

*Global funds are the latest trend in the Indian mutual fund industry that is fast catching the attention of the investors. With the launch of global mutual funds by reputed fund houses, the Indian investors now get an easy access to the global market, besides getting an international exposure. Investment in global funds has further opened a window for the Indian investors to diversify their portfolios beyond the conventional domestic equity and debt-investment avenues, thereby mitigating the overall portfolio risks. An overseas investment was a distant dream for the mutual fund houses in the past, owing to stringent foreign exchange regulations laid down by the Government of India (GOT). But huge foreign exchange reserves and the recent volatility in the Indian markets has spurred the GOT in promoting the Indian mutual fund houses to move out for international diversification, that helps an investor to invest across a range of countries around the world, hence exposure to country—specific risks is considerably reduced. Many domestic asset management companies (AMCs), including ICICI Prudential and UTI Mutual Fund have tied up with foreign players to raise offshore funds for investments. On the basis of the global funds, investors are ready to capitalize on the benefits of diversification by investing predominantly in the emerging markets across the globe. It also remains a moot point as to what strategies the Indian investors would adopt while venturing into an investment universe to which they have had little or no exposure.*

*The purpose of this paper is to show that investments in a Global Fund can reduce the geographical risk for investors who do not always have to rush into debt whenever domestic equity markets collapse — especially if their asset allocation profile suggests that equity is appropriate. Further, currency movements should not be a deterrent — investing in the right markets could also provide a currency hedge - particularly where business is conducted globally.*

**Key Words:-** Investments, Global, Diversification, Assets, Funds

## **Introduction**

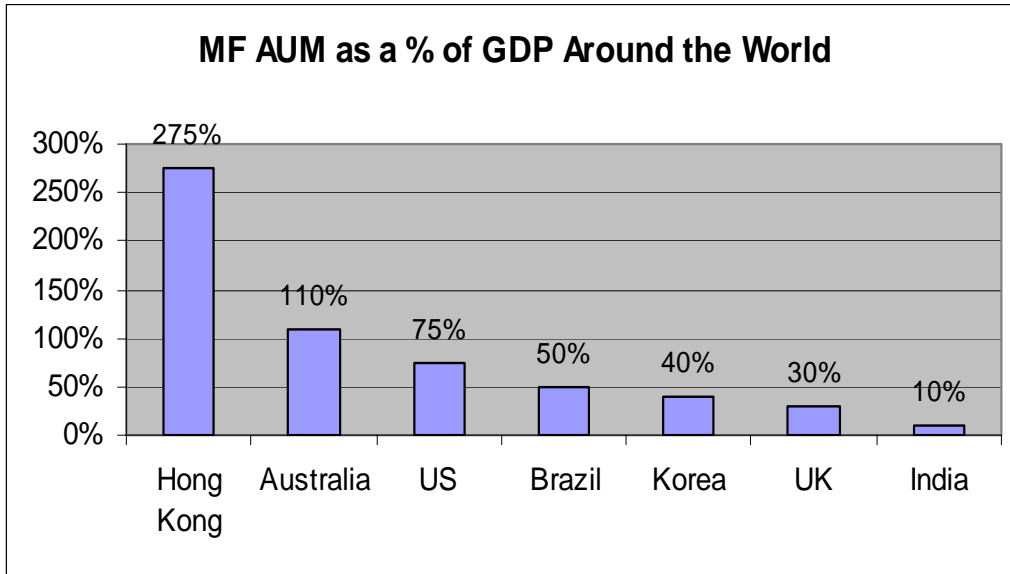
Recently global funds are launched by many mutual funds. Main purposes of launching these funds are to reduce geographical risks. These funds can act as a cushion when the Indian markets are down. In fact, other markets may often do better than India in a Goodyear. Global funds are the latest trend in the Indian mutual fund industry that is fast catching the attention of the investors. With the launch of global mutual funds by reputed fund houses, the Indian investors now get an easy access to the global market, besides getting an international exposure. Investment in global funds has further opened a window for the Indian investors to diversify their portfolios beyond the conventional domestic equity and debt-investment avenues, thereby mitigating the overall portfolio risks. An overseas investment was a distant dream for the mutual fund houses in the past, owing to stringent foreign exchange regulations laid down by the Government of India (GOI). But huge foreign exchange reserves and the recent volatility in the Indian markets has spurred the GOI in promoting the Indian mutual fund houses to move out for international diversification, that helps an investor to invest across a range of countries around the world, hence exposure to country-specific risks is considerably reduced. Many domestic asset management companies (AMCs), including ICICI Prudential and UTI Mutual Fund have tied up with foreign players to raise offshore funds for investments. On the basis of the global funds, investors are ready to capitalize on the benefits of diversification by investing predominantly in the emerging markets across the globe. It also remains a moot point as to what strategies the Indian investors would adopt while venturing into an investment universe to which they have had little or no exposure. Global funds are mutual funds that invest predominantly in foreign stocks or foreign mutual funds which invest in foreign stocks. The world's largest companies are domiciled all over the place, so global funds help the investors to invest in shares of big corporate houses.

## **Indian Mutual Fund Industry: - An Overview**

The history of mutual funds in India can be traced back to 1963 with the formation of the Unit Trust of India (UTI), at the initiative of the Government of India (GOI) and the country's central bank. But with the entry of public and private sector players since 1987, the number of mutual fund houses increased by leaps and bounds. As on May 31<sup>st</sup> 2009, the number of mutual fund houses stood at 35 with Assets Under Management (AUM) of Rs. 664,450 crores under its belt, compared to just one in 1963.

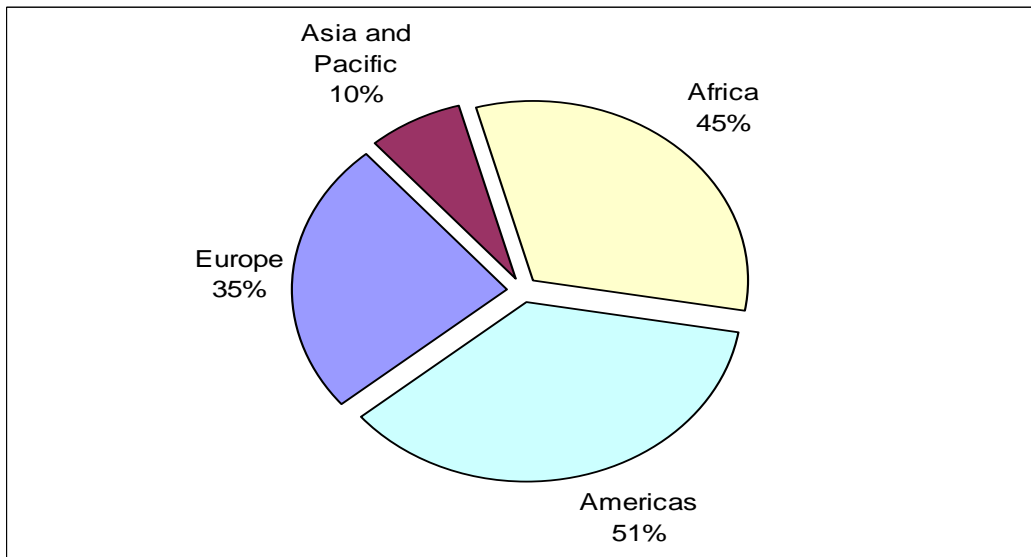
The total AUM, as a % of GDP, stood at 10% which is quite low compared to the global penetration level. The total size of the mutual fund industry in US stood at \$44 trillion and alone accounts for 74% of the country's GDP growth (Graph 1.1). Compared with other developed markets, there is evidence of lack of penetration in the Indian market all point to a significant untapped opportunity ahead.

**Graph 1.1**  
**Mutual Fund industries as % of GDP around the world**



**Source:** - Investment company Institute

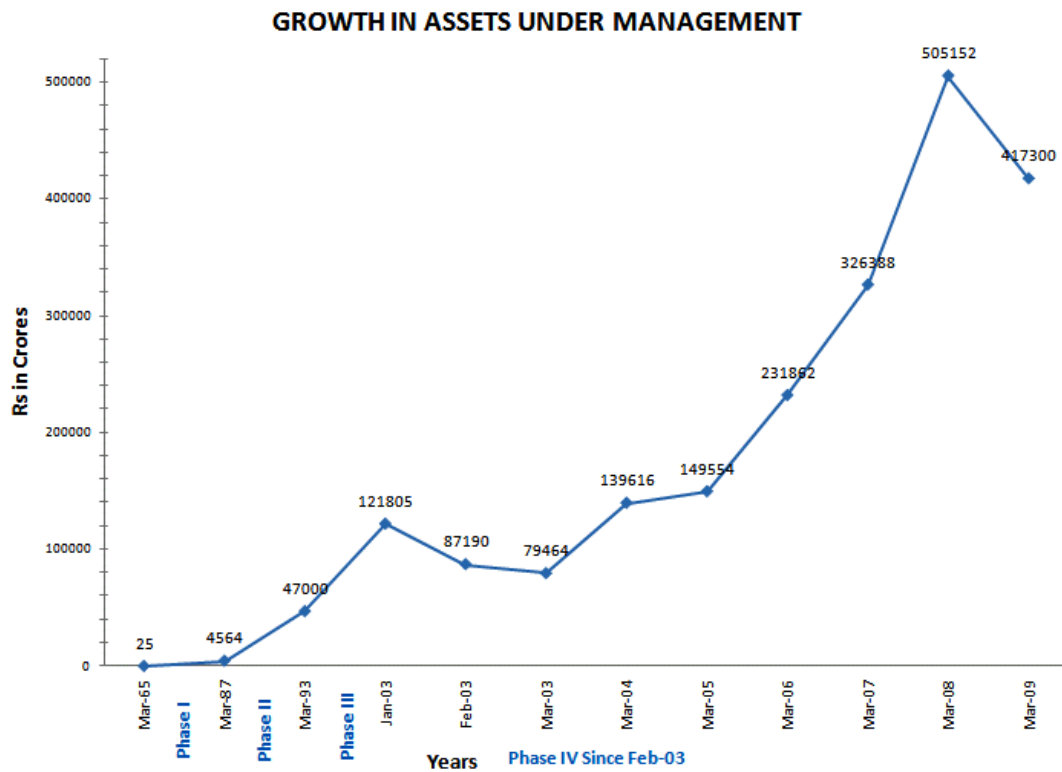
**Chart 1.1**  
**World Mutual fund Industry at a Glance**



**Source:** - Investment company Institute

The global industry size is over US \$ 44 trillion. The global industry grew by 22.47% in 2008. US accounts for over 50% of the global fund size. Major players in Europe are France and Luxembourg-based funds with USD1.8 trillion and 2.2 trillion respectively. Mutual Funds are freely traded on Stock Exchanges. Number of listed MFs exceed shares. The Indian industry size is about US 85 billion. The Indian MF industry has grown by 43% in the last year and by 77% in the last two to three years. The Indian mutual fund AUM accounted for 11% of the combined Market Capitalization of Bombay Stock Exchange (BSE) and National Stock Exchange (NSE) indices, at the end of 2006-07. Thanks to the launch of innovative products as well as growing awareness in the mutual funds segment, the Mutual Fund industry in India has registered a growth of 43% in 2006-07 with just a dip in may 2009 due to recession and slow down in world market and a 378% overall growth since 1963 (Graph1.2).

**Graph 1.2 Mutual fund Sales & Assets under management**

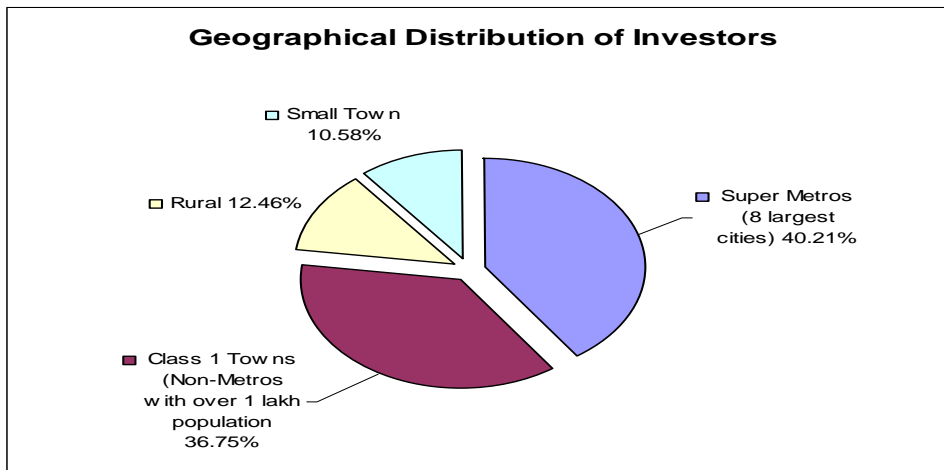


Source:- AMFI INDIA

As on May 31<sup>st</sup> 2009 the total no. of schemes offered by all the funds stood at 920, of which 595 are open ended, while the remaining 263 are closed ended and 62 are interval scheme in nature. Investments in equity schemes shot up by 70 percent, reflecting the buoyancy in the Indian stock markets. Retail Penetration increased multifold and investor base was expected to be over 20 million from 400 cities, with the increase in the number of global players in India. Schemes like Systematic Investment Plans (SIP), which currently accounts for 1.2 million became hugely popular. An upwardly mobile population in India is also responsible for the growth foundation of the mutual fund houses. The country's working population is expected

to climb up in the near future which was expected to enhance the growth of the mutual fund industry in India. 77% of investments in mutual funds come from super metros and class I towns. It is even predicted that the mutual funds would not be restricted in the hands of an affluent few, as was the case earlier; and would spread more across all sections of the society (Chart 1.2 & 1.3).

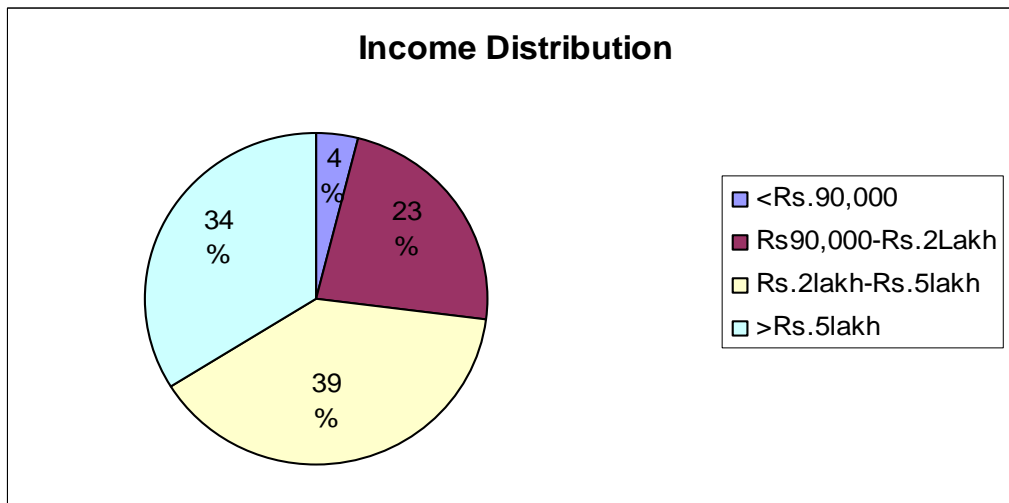
**Chart 1.2 Geographical distribution of Mutual fund investor in India**



**Source:** - Investment India Incomes & Savings Survey, IIMS 2008.

**Chart 1.3**

**Income distribution of the Mutual fund investor in India**



**Source:** - Investment India Incomes & Savings Survey, IIMS 2008.

## **Indian Mutual Funds: Why Going Global?**

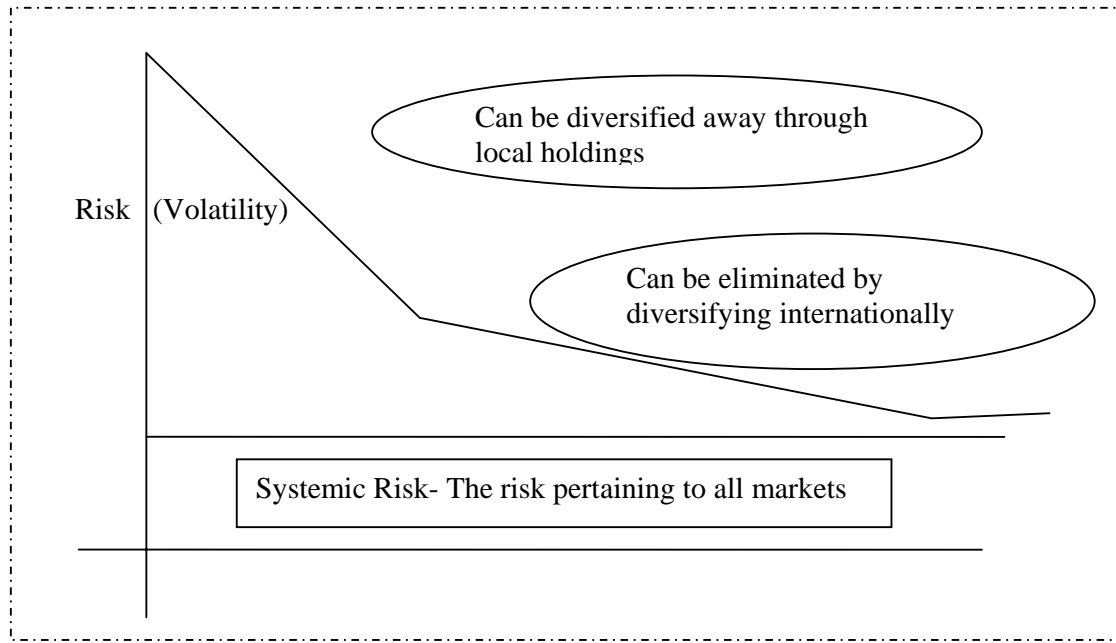
The acquisition of London-based Corus Group by TATA Steel can be manifested as a prime example of why India wants to go global. TATA Steel's acquisition of Corus raised the share prices of Corus in the London Stock Exchange whereas Tata's share prices witnessed a severe decline in the stock exchanges in India. If the Indian investors had the opportunity to trade in the London stock exchange, they would not have experienced such a massive blow in profits. So, the necessity for the Indian investors to go global can be realised from this very instance. India represented just a small part of world market cap. India, which is a part of the Asia-Pacific region, held a meager 10% of the global mutual fund distribution, compared to America's 51%. Europe held the second spot with 35%. Markets move in cycles, around the world India is no exception. Just because Indian markets are down, it does not mean the situation is replicated across the globe. Other markets may often do better than India even in a good year. A globally diversified portfolio can help an investor better withstand domestic volatility more countries adds-on more opportunities for the growth of the mutual funds industry. Our equity markets are just a small part of world market capitalisation there is a larger world out there. Other equity markets have delivered significantly higher returns than Indian debt without significantly higher excess volatility. Indian debt is not the only alternative to Indian equity any more, when the equity market is down. Investors do not always have to rush into debt when markets fall. Investors may experience higher returns by stepping out of the comfort zone that debt provides. Markets move differently across the globe diversification smoothes returns. Lower correlations with the rest of the world further aids in diversification. Global diversification could also provide a currency hedge. Rupees is appreciating against the dollar but it has actually weakened against other major currencies. Currency movements should not be a deterrent diversifying in the right markets could also provide a currency hedge.

Business is increasingly conducted globally our competitor may be on the other side of the world instead of the other side of the street. Global industry dynamics drive the prospects for many businesses. Individual stock markets tend to have biases towards certain sectors relative to the world market. Different sectors lead market performance at different times - consistently picking the leading sectors is very difficult. Stock selection within sectors offers greater potential to add value, compared to sector selection. Companies in many industries are influenced by common global dynamics. Sectors across countries are increasingly moving in cycles around the world. A country could be over-represented in certain sectors (increasing un-systemic risk), whereas under-represented in others (reducing the opportunity set available). Hence, stock-picking combined with vigilant trend identification can uncover the best ideas, at the right time from across the globe.

Different markets respond to different factors. They could be political, economic or social, and are particular to each country or region. And despite the increasingly integrated world in which we live, these differences ensure that markets are not always synchronized with each other. But diversification helps to eliminate the market risks to some extent possible. But holding more stocks does not mean that it will help to control risk. The stocks should ideally be uncorrelated with each other and belonging to sectors, or industries, that generally do not rely on the same variables for success. Non-systemic risk or company-specific risks can be diversified by adding assets that has a low correlation with each other to the portfolio. But that doesn't mean that the portfolio is risk-free. But the real motive lies in mitigating the

market-related risks. The aim of diversification is to get the portfolio to a point where it can generate the maximum return for the least amount of risk (Graph 1.4).

### Graph 1.3 Diversification of Systematic & Non-Systematic risks



Source: Bloomberg

Graph 1.3 illustrates the ways of diversifying non-systematic risks either by international diversification or by means of diversifying away through local holdings. The more and more non-systematic risks gets diversified, risks associated with the stock markets also gets reduced substantially. Systematic or market-related risks are hard to get diversified as it is more dependent on the socioeconomic environment of the country. Some markets have a bias towards those industries in which they have a long and profitable tradition; others may find that they have minimal exposure to a particular industrial section. In that way, some countries will be more or less exposed to particular economic risks. In India case, our stock market is. Over all weighted towards information technology, financial services, and the energy sector — although in the case of financials, when compared to the rest of the world, our market has a relative underweight. Markets dominated by one particular industry will be very exposed to the risk that faces the industry and will see their ups and downs driven by that industry's fortunes. Therefore, it makes sense to explore industries that may have greater global participation, but are relatively under-represented in the home country.

#### Indian Scenario

In the recent past, many mutual funds launched global funds after the RBI relaxed the limits for overseas investment. Apart from geographical diversification, the global funds will also give an opportunity to the Indian Investor to invest in the

international market. These funds not only invest in different countries, but they also invest in different sectors of those countries. These funds are mainly invested in emerging Asian markets, Eastern Europe and Latin America. Some of these markets have generated spectacular returns during the past few years. Historically, all these markets have very little correlation, though in the recent years their stock markets are sometimes moving in tandem.

All these markets are fast growing and that is why these markets have become an alternative investment destination for many countries. Some of these emerging markets have very strong infrastructure and they are planning to have even a stronger infrastructure. Therefore, there is a scope for investment in infrastructure industries in these countries.

Similarly, some countries are strong in consumer electronics, some in travel and tourism etc. Countries like Brazil and Russia provide investment opportunities in mining, precious metal, oil, natural resources and other commodity stocks for which not many options are available in India.

In fact, one can look at the global funds as a new investment opportunity where the investors can diversify their portfolio. Some Global Real Estate funds are launched which will invest in real estate investment trusts and global real estate stocks for which there are few listed options in India. These funds are expected to give higher returns than fixed income in India, but with less volatility than Indian equity. Similarly, funds which are invested in gold mining companies are expected to give higher returns than the gold ETFs because the price of gold mining companies rises more than proportionally when gold prices rise due to the leverage effect.

Are our fund managers ready to invest in overseas markets? Do they have the expertise and resources? Funds which have international backing do not face any problem as they get support from their international fund management team for research and expertise knowledge. They can also make the investment through an existing overseas fund. Mutual funds which do not have an overseas partner can opt for fund of funds (i.e. invest in overseas mutual funds) till they become experts in the overseas market.

## **Conclusion**

Though the performances of these funds are not satisfactory when compared with the Indian market, it will be too early to comment on their performance as these funds are launched very recently. Apart from that the Indian equity market is running through an exceptional period and giving spectacular returns. Therefore at this stage one should not compare the performance of global funds with their Indian counterparts and one should measure the performance of these funds on a long term basis. The utility and performance of these funds can be measured during the bear phase of the Indian equity market caused due to India specific factors.

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**Online Resources:-**

1. [www.affarsvarlden.se](http://www.affarsvarlden.se)

2. [www.six.se](http://www.six.se)

3. [www.msci.com](http://www.msci.com)

4. [www.sebi.gov.in](http://www.sebi.gov.in)

5. [www.amfiindia.com](http://www.amfiindia.com)

6. [www.pwc.com](http://www.pwc.com)