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Rapid Growth of Mutual Fund Industry in India: Non Economic Factors viz a viz Economic Factors R

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ABSTRACT:
A country's economic development depends upon domestic capital formation. Although in modern times Foreign Investment is also a great source of capital formation and investment. Empirically it has been found that many East Asian Tigers and Cubs have/had achieved high rate of growth with the help of Foreign Investment but for a large country like India the key to development is domestic capital formation. Capital formation in a country is a function of saving and its mobilization. The household saving are generated in both financial market i.e. through banks and other financial institutions and in capital markets through shares, equities and debentures. The first kind of instruments are less risky but yield low returns while the second kind of instruments are more risky and have high positive/negative yield.
In economics it was believed that investor is highly rational, has complete information and decides his investment to maximize his returns. But recent studies in Behavioral Economics by Tversky, Becker, Kahneman, Simon, Thaler, Ariely, Laibson and others have found that neither does the consumer /investors has or even can have complete information nor does he always act in what may be called as maximizing behavior especially in investment where the outcomes are highly unpredictable and uncertain. The basic objective of the study is to find the causes that impact the saving and investment pattern of different individuals in India? (1) How individuals decide to invest in a particular institutions/ instruments among various various alternatives available? and (2) What are the main reasons to choose mutual fund as an investment avenue? Part 1 of the paper deals with Research Problem along with a brief review of literature. Methodology of the research paper is discussed in Part 2. Part 3 is devoted to testing of hypothesis and finally part 4 is devoted to findings and recommendations.

Keywords: Risk, Yield, Investment, Nudge, Mutual Fund

I (A) Saving is one of the important variables for economic development that has emerged as the central issue in developing countries. For economic development and economic growth capital formation must which can be achieved by either decreasing consumption or using foreign capital. But external capital inflow involves huge uncertainty, political influences. Apart from this, the amount of such assistances is neither timely nor sufficient. For a country of the size of India it would certainly be better if it can fully mobilize domestic financial savings and turn them into right area of investment for not only present growth but also act as a precursor to future growth.

Virtually everyone makes investments. Even if the individual does not select specific assets such as funds deposits or equity, investments are still made through participation in pension plan, and employee saving program or through purchase of life insurance or a home or by some other mode of investment like investing in Real Estate (Property) or gold and other precious metals.

At the time of independence India had a low savings rate (8% of GDP) because of low Income/ Per capita gdp. Most of the savings were in the form of Gold and physical asset. 3% to 4% of savings was held in financial assets and most of the financial assets of the Indians were deposited in banks due to the less risk appetite of investor and lack of suitable alternatives. Indians were afraid of taking risk and so they did not invest in share market or other financial instrument apart from banking but this changed soon. India like many developing countries followed Keynes and deficit financing was used as an instrument of growth. Through deficit financing expansionary monetary policy was followed to generate Aggregate

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Demand. With increased demand of goods and commodities investors were encouraged to invest in financial assets because of higher returns. But expansionary monetary policy also created high inflation which led to more speculative activities. Government was forced to adopt the policy of growth with stability. An inflation rate of more than 4% was not acceptable hence government has to decide borrowing and lending rate of institutions and programmes governed by it. Moreover Monetary and Fiscal policies were also changed (Introduction of GST,Notebandi, operation twist) which effected the rates of lending and deposits of various formal and informal financial sectors and generally the rates of riskless investments were lowered and almost zero in real terms which did help the equity market and mutual funds market as investors were in search of positive returns but returns in them are supposedly uncertain and involve risk. Traditional Economics theories did not accept that individuals would prefer uncertainity over certainity. Although some economists like Morgenstren, Neuman did discuss choices under uncertainty and concluded that decisions are made by individuals by considering returns with risk. Tobin concluded in this field is of great importance. But Economists as a whole agreed that all decisions of investments like consumption and production depend upon rational choices i.e. individuals try to maximise the returns.

I (B) **Behavioural Economics and Investment Decisions**

At the end of 20th century and in early 21st century a new field of Behavioural Economics was propounded. The field of behavioral economics blends insights of psychology and economics. It provides valuable insights that as to what are the factors that affect individuals' behavior when they make decision over uncertain outcomes. Behavioral economics provides a framework to understand when and how people make decisions? Are their decisions based on rational choices? Do they make errors? Behavioral economics emerged against the backdrop of the traditional economic approach known as rational choice model. The rational person is assumed to correctly weigh costs and benefits and calculate the best choices for himself. In contrast, behavioral economics shows that people have limited cognitive abilities and often make choices that allow a mixed relationship to their own preference .They are intensely influenced by context, and often have little idea of what they will like next year or even tomorrow. As Daniel Kahneman put this, "it seems that traditional economics and behavioral economics are describing two different species." The behavioral economics shows that individuals are exceptionally inconsistent and imperfect in making choices. They choose a goal and then frequently act to pursue it but may not be able to implement right policies due to various factors such as lack of information or misinformation, lack of calculability of each and every outcome, personal biases, as well as their background. So, investment decision of investors are affected by reference point, rigidities and other biases. The question is what is more important in making choices of investment in uncertain areas of mutual fund , equities etc. The researcher has taken up this research question in this paper. A brief review of literature is presented below that the researcher studied to grasp the subject.

Review of Literature

Herbert Simon, Bounded Rationality, 1950. This view supports that human preferences are embodied with scientific principles of observation and experiments rather than the assumptions and deduction characteristics of theoretical economics. There are limitations to human information processing, due to constraints in knowledge (or information) and computational capacities (Simon, 1982; Kahneman, 2003).

Gary S. Becker , The Economic Approach to Human Behavior,1976, developed the theory known as Rational Choice. The theory believes that human actors have firm preferences and engage in maximizing behavior. Their decisions would be taken by comparing costs and benefits carefully and informed by existing preferences. And People would always make optimal decisions.

One of the most widely applied theories from behavioral economics is prospect theory **(Kahneman & Tversky, 1979**), a model that shows how people decide between alternatives that involve risk and uncertainty. Theory argues that decisions are not always optimal but willingness to take risks is influenced by the way in which choices are framed, i.e. it is context-dependent. . The theory demonstrates that people evaluate options based on reference points and that they are loss-averse—they dislike losses more than equivalent gains.

The economist **Richard Thaler** invented the term Mental accounting. The predominant idea behind this theory is that people think of value in relative rather than absolute terms. People consider money in a different way, depending on factors such as the money's origin and intended use, rather than thinking of it in terms of formal accounting.

Dan Ariely, Predictably Irrational**.** Ariely's discussion involves prices and value perception

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through anchoring. He explains anchoring as a process whereby a numeric value offers a non-conscious reference point that guides subsequent value perceptions (Ariely, Loewenstein, & Prelec, 2003). Ariely also presents the concept of the **zero price effect**, namely when a product is advertised as 'Free', consumers recognize it as intrinsically more valuable.

Ansari Lubna and Moid Sana (2013), 'FACTORS AFFECTING INVESTMENT BEHAVIOUR AMONG YOUNG PROFESSIONALS', **International Journal of Technical Research and Applications, ISSN: 2320-8163.** Given study deals with young professionals' investment pattern and the factors that determine their investment behaviour. To examine the objective various variables like age, gender, savings objective, different investment avenues are taken. Data are collected through personal interview with 100 sample size. By applying Chi square researchers conclude that Investment is dependent on age and income but independent from gender.

Research Problem

The present study is being undertaken to find out the causes of changes in investors behaviour i.e. why investors are moving away from traditional investment institutions to newer one especially the mutual funds since the dawn of 21st century. The research question involved is that whether these changes are due to human behaviour or are based on rational choices? This question would be analysed in present research paper on the basis of following hypotheses. An empirical survey of 300 individuals of a variety of people with different level of Income, age, Savings and background have been selected from an universe of 1000 individuals.The universe has been selected from investors of Axis bank, HDFC bank Civilines and Rathis Investment Civil lines. The researcher would test following three hypotheses to analyse the change of investors behaviour.

Hypotheses

1) $\mathbf{H_o}$: Growth of Mutual Fund investment is not significantly different than growth of financial savings in India.

$\mathbf{H_1}$ **:** Growth of Mutual Fund investment is significantly different than growth of financial savings in India.

2) $\mathbf{H_o}$: Investment decisions of individuals are not significantly influenced by the availability of information providing platforms.

$\mathbf{H_1}$**:** Investment decisions of individuals are significantly influenced by the availability of information providing platforms.

3) $\mathbf{H_o}$: There is no significant association between the Age of investor and investment in Mutual fund schemes.

$\mathbf{H_1}$ **:** There is significant association between the Age of investor and investment in Mutual fund schemes.

Methodology

The present paper analyses the changing pattern of Investors' behavior .The study is based on primary survey. For collecting the data questionnaire method is used. This primary survey is based on stratified sampling with sample size of 300 investors. The demographic profile of the investor is used. Stratified sample method was adopted by the researcher so that different age group, gender, occupation, family size and income groups can be captured.

Limitations

The Survey is limited to Prayagraj district and also of three Investment banks/ Institutions. Moreover the survey was conducted during the pandemic hence its results could not be generalised.

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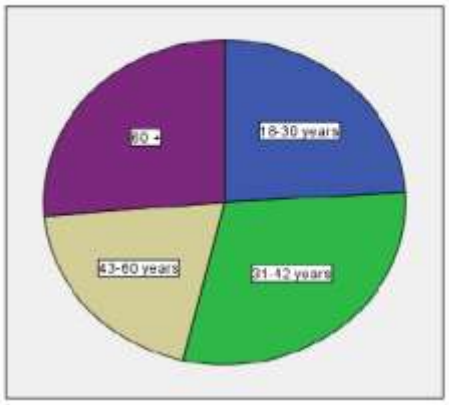
Analysis

Demographic Profile of Individuals

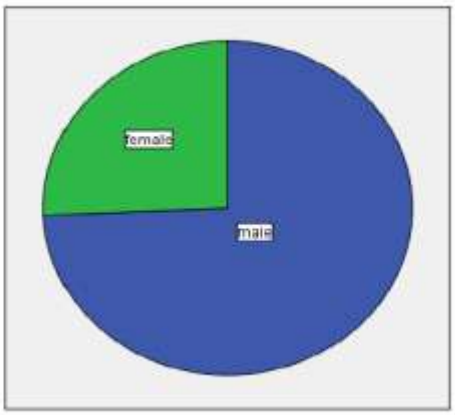
1) Age of the Respondents

Age	Frequency
18-30 years	72
31-42 years	89
43-60 years	60
60 +	79
Total	300



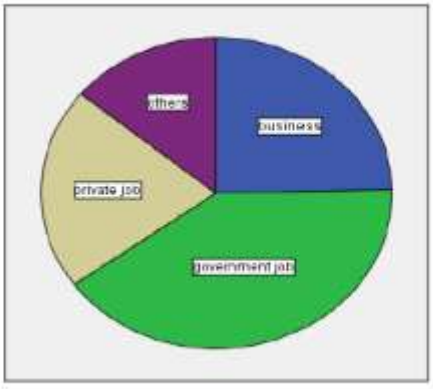
2) Gender of the respondents

		Frequency
Valid	male	223
	female	77
	Total	300



3) **Occupation of the respondent**

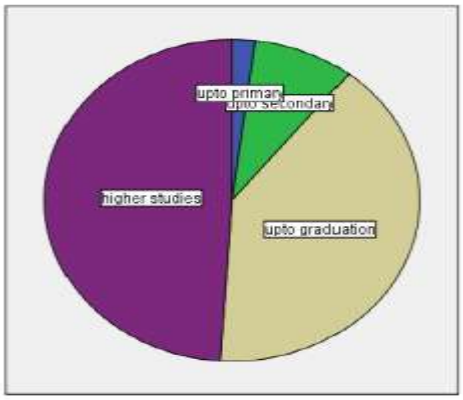
		Frequency
Valid	business	74
	government job	121
	private job	63
	others	42
	Total	300



International Journal of Advances in Engineering and Management (IJAEM)
Volume 3, Issue 7 July 2021, pp: 2220-2231 www.ijaem.net ISSN: 2395-5252

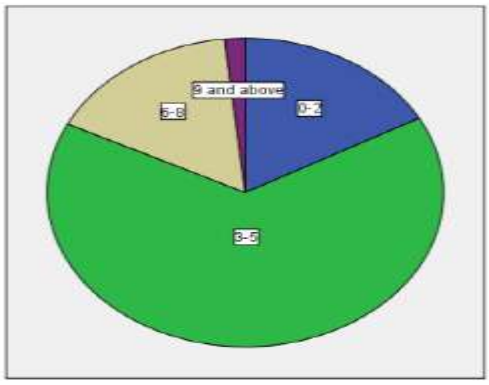
4) **Education level of the Respondent**

		Frequency
Valid	upto primary	6
	upto secondary	26
	upto graduation	121
	higher studies	147
	Total	300



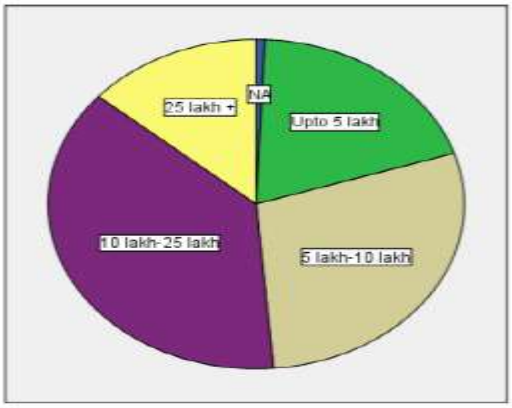
5) **Famiy size of the respondent (including respondent)**

		Frequency
Valid	0-2	51
	3-5	196
	6-8	48
	9 and above	5
	Total	300



6) Annual Income of respondents

		Frequency
Valid	NA	2
	Upto 5 lakh	58
	5 lakh-10 lakh	86
	10 lakh-25 lakh	113
	25 lakh +	41
	Total	300



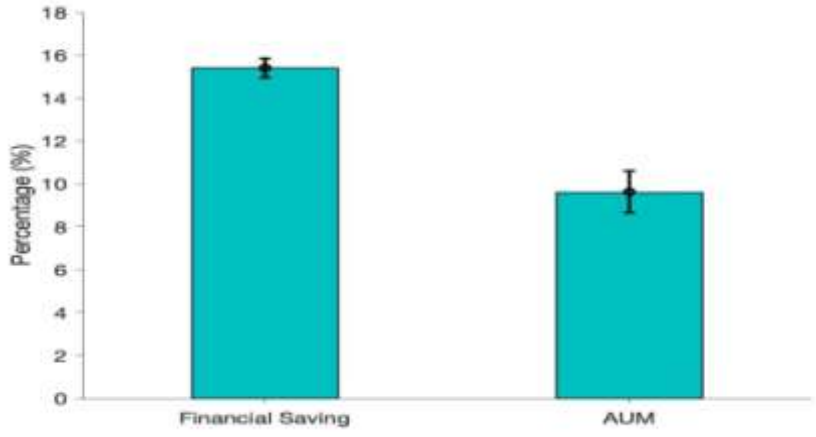
International Journal of Advances in Engineering and Management (IJAEM)
Volume 3, Issue 7 July 2021, pp: 2220-2231 www.ijaem.net ISSN: 2395-5252

Testing of Hypothesis
Hypothesis 1

Year	Financial Savings(% of GDP)	AUM(% of GDP)
2011	14.05	6.7
2012	14.45	7.1
2013	14.74	7.3
2014	15.39	8.7
2015	15.25	9.8
2016	15.1	11.5
2017	16.97	12.7
2018	17.41	13.2

Group	N	Missing	Mean	SD	SEM
Financial Savings(% of GDP	8	0	15.42	1.18	0.4468
AUM (% of GDP)	8	0	9.625	2.59	0.9793

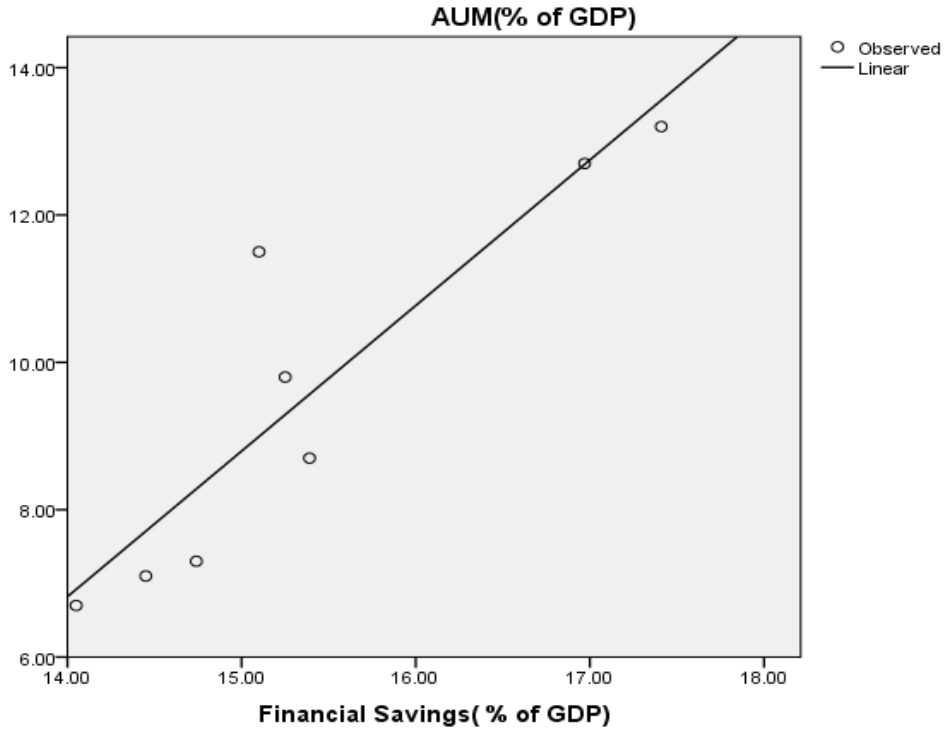
t = 10.18 with 7 degrees of freedom (P = 0.00018)
Since, p value <0.05 , Null hypothesis is rejected.
The difference in the mean values of the two groups is greater than would be expected by chance; there is a statistically significant difference between the input groups .



Relationship between the financial savings and AUM is analysed by the Regression Analysis.

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate	Constant	Beta	Sig
1	.901[a]	.813	.781	1.21143	-20.846	0.901	0.002

International Journal of Advances in Engineering and Management (IJAEM)
Volume 3, Issue 7 July 2021, pp: 2220-2231 www.ijaem.net ISSN: 2395-5252



Since the Beta value is positive which shows the positive relationship between the variables. High R square (81.3%) indicates that Financial savings (Independent variable) explains variances in AUM (Dependent Variable) efficiently.

In this hypothesis it is being observed that gross domestic savings as a percentage of gross domestic product is demonstrating a declining trend over the whole period 2011 to 2018. Savings have declined from a high of 35.26% as a percentage of GDP in 2012 to 31.1% in the above period. This means that during this period consumption of household was rising. It may be due to variety of reasons (a) greater choice of products and services (b) greater credit facilities (c) stable growth of income leading to less uncertainty in future (d) greater emphasis on consumption of non-priority goods etc (e) high inflation rate. But an important thing to remember is that financial savings are increasing while savings in the form of metals and real assets have declined as a percentage of total saving. In case of metals it leading to negative returns. In case of real estate there were many factors specially Government policies on land, real estate but the most important role for lack of demand of real estate has been frauds conducted by real estate companies and rising land disputes which lead to investors moving away from savings in Real estate. Investors have now more faith in financial savings. But in terms of distribution of financial savings in different alternatives i.e. bank, post offices, insurance market, capital market, NBFC and mutual funds. Investors have shown greater faith in mutual funds. During the above period the AUM of mutual fund has more than doubled as a percentage of the GDP while financial savings have more up by around 25% in the same period. This was mainly because of low returns in Government and bank deposits rates (3% to 7%) for short and medium term while equities and mutual funds were giving double digit return. This phenomenon is also backed by statistical evidence and this also explains null hypotheses being rejected.

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Testing of Hypothesis 2 : Second Hypothesis is tested by using the Chi square analysis

			Respondent decision is affected by any advertisement of MF					Total
			0	no	yes, in newspaper	yes in telivison	yes, in social sites	
How new investment is purchased by respondent	NA	Count	7	4	2	3	1	17
		Expected Count	.6	6.3	4.0	5.0	1.1	17.0
	call up agent/ financial advisor	Count	1	32	20	26	5	84
		Expected Count	3.1	31.1	19.6	24.9	5.3	84.0
	company's website	Count	1	26	11	15	4	57

		Index	2.1	21.1	13.3	16.9	3.6	57.0
		Count	1	28	15	22	4	70
	by comparing commercial sites	Index	2.6	25.9	16.3	20.8	4.4	70.0
		Count	1	21	22	23	5	72
	information collected through news paper, advertisement	Index	2.6	26.6	16.8	21.4	4.6	72.0
		Count						

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Total	11	111	70	89	19	300
	11.0	111.0	70.0	89.0	19.0	300.0

Chi-Square Tests

	Value	Df	Asymp. Sig. (2-sided)
Pearson Chi-Square	77.090[a]	16	.000
Likelihood Ratio	34.601	16	.005
N of Valid Cases	300		

Since, the p value <0.05 , Null hypothesis is rejected.

The decision of the investment as per the traditional theory is based on maximising expected utility but in the above survey when respondents were asked as to how did they made their decision of investment 72 individuals answered that they were attracted through the advertisement of mutual funds (availability heuristics) . Another 74 individuals informed that they made investment by discussing with financial advisor and accepted his advice in totality i.e. they did not analyse /study the advantage of investment because they thought that it is impossible for them to study all investment avenues (bounded rationality) and were very impressed by the knowledge of the financial expert and made default choice ,whatever was recommended by the financial expert (Herd behaviour). Another 62 informed that they were attracted by the claims of Mutual funds companies because they searched the websites to make a decision. Their answer seems to be closest to traditional theory but when they were asked whether did you check the claims of various mutual fund companies or whether did you look at beta, standard deviation, treynor ratio, sharpe ratio or whether did you also see the annual report of the companies in which you made investment even whether did you read the statutory warning of companies as mandated by SEBI. All investors answered in negative. In fact these investors were nudged (Richard Thaler) to invest due to framing heuristics. The results of the company, the returns of the mutual funds are framed in a manner that investors get the information of peak and average returns. Many of the respondents did not answer this question (73). Hence it is quite clear that the hypothesis is rejected and it can be safely concluded that investment decisions in 21st-century are not based entirely on economic rationality but also on behaviour attitude, past experiences as well as on advertisements.

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Testing of Hypothesis 3: Third Hypothesis is tested by using the Chi square analysis.

			If you suppose to invest in MF then which one you will choose					Total
			NA	equity fund	debt funds	liquid funds	hybrid funds	
Age of the Respondent	18-30 years	Count	13	34	9	6	10	72
		Expected Count	7.2	27.8	16.3	9.8	10.8	72.0
	31-42 years	Count	13	39	16	9	12	89
		Expected Count	8.9	34.4	20.2	12.2	13.4	89.0
	43-60 years	Count	4	21	16	8	11	60
		Expected Count	6.0	23.2	13.6	8.2	9.0	60.0
	60 +	Count	0	22	27	18	12	79
		Expected Count	7.9	30.5	17.9	10.8	11.9	79.0
Total		Count	30	116	68	41	45	300
		Expected Count	30.0	116.0	68.0	41.0	45.0	300.0

Chi-Square Tests

	Value	Df	Asymp. Sig. (2-sided)
Pearson Chi-Square	36.664[a]	12	.000
Likelihood Ratio	43.209	12	.000
N of Valid Cases	300		

a. 0 cells (0.0%) have expected count less than 5. The minimum expected count is 6.00.

Since ,the p value <0.05, Null hypothesis is rejected.

As per traditional theory every investor must have selected the scheme with maximum expected utility. But in this survey the respondents opted different schemes which had different returns for one year period and three year period. The selection o scheme was based on different choices. When this answer was regressed with the profile of investors the results were: (1) Younger people (82%) preferred equity investments which is the riskiest suggesting that age affects risk-taking appetite of investors. It is further proved when most Middle Aged persons (65%) opted for hybrid funds and senior citizens (70%) opted for debt instruments or hybrid funds. (2) Occupational structure also impacted the choice of mutual fund scheme. government employees preferred different schemes (risk less) while informal workers and traders opted for equity schemes. (3) Income distribution also affected the investment schemes. High net worth individuals opted for risky schemes while middle income group opted for less risky (hybrid funds, debt schemes). Thus, it proves that investment decisions/ choices are based upon various factors.

CONCLUSION

Based upon the empirical results of the survey it can be concluded that investment decisions of the individuals are effected by various considerations. Human psychology is an important determinant of decision making. Individuals from different religion, social values, cultural ethos, religious faith behave differently in similar situations. The concept of Islamic Banking is an example which was developed because of preaching of Quran. Education, family background, level of Income and even the age impacts the decision especially which related to Investment. At younger age people may invest in risky assets but retired government pensioners may not take such

risky. One can clearly conclude that investment in Mutual Funds industry has been very high from some group of people like high net worth Indians, Metro dwellers, Tech savvy individuals. The growth is more or less in books and returns increase the book value jumps and the companies' net worth is enhanced. In the period of recession the book value falls just as inflation and deflation do not impact the real worth of economy. Similarly, rise in prices of stocks do not enhance real net worth of company. Present growth although also is affected by greater number of investment by individuals who were forced to shift because of declining returns on alternatives but books more attractive because of high prices of share and equities. Yet its true that non economic factors have also caused a rapid growth in Mutual funds industry but non economic factors have also caused a rapid growth in Mutual Fund Industry but non economic factors especially psychological factors through various measures have forced many individuals to invest in Mutual Fund especially the confidence to invest and feel good factor nudged by various advertisements of Mutual Fund Industry. The moral of the story is individuals can be prompted to make a decision provided right type of information is fed in the in the mind of investors.

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