ISSN 0976-495X (Print)
2321-5763 (Online)
DOI:

Vol. 09| Issue-01|
January- March 2018

Available online at
www.anvpublication.org

Asian Journal of Management
Home page *www.ajmjournal.com*

Factors Affecting the Fund Selection Capability of Mutual Fund Advisors

Sharika Hassan[1], Dr. Asif Iqbal Fazili[2], Asif Hamid[3]
[1]PhD Scholar, IUST, Awantipora,
[2]Assistant ProfessorIUST, Awantipora
[3]PhD Scholar, IUST, Awantipora
*Corresponding Author E-mail: **sharikahassan07@gmail.com, asif.fazili@islamicuniversity.edu.in, asif739.jobs@gmail.com**

ABSTRACT:
The Mutual Fund Industry of India traces its origin from the establishment of the Unit Trust of India in 1964. The mutual fund industry of India has seen a tremendous growth since its incorporation. A number of research studies have been carried out so far to understand the nature of the Indian mutual fund industry. However, every study attempts to bring forth something that is of great interest to the stakeholders of the industry. Much has been discussed by the researchers regarding the evolution and growth of Indian Mutual fund Industry, the performance evaluation of different mutual fund schemes, the investors' behaviour towards mutual funds etc. However, no major study has been done so far regarding the fund selection capability of the mutual fund advisors in India. Undoubtedly, the contribution of the mutual fund advisors in taking the Indian Mutual Fund Industry to new heights is self-explanatory. Such a huge growth of Assets under Management (Rs 10827.57crore, as of March 31, 2015) can be attributed mainly to the expertise of the fund advisors/managers. Thus, the main objective of the study is to find the factors that matter to the financial advisors while making recommendations about the mutual fund schemes to the Indian mutual fund investors. The important factors that are considered by the fund advisors include the Past Performance of a Mutual Fund, the Risk associated with the Fund, Brand equity of the fund and the Current market conditions. The average performing funds which involve moderate level of risk and are mostly debt oriented are recommended by the financial advisors mostly. Regarding the current market conditions factor, the presence of optimistic conditions is believed to be conducive for the better returns on fund investments. If the brand equity for a particular fund is high, the advisors perceive such funds as the mouth-watering ones.

KEYWORDS: Fund Selection Capability, Financial Advisors, India, Fund Recommendations, Mutual funds, Past-performance

INTRODUCTION:
The progress of any nation depends largely on the strength and activeness of its financial markets. The liberalization of the economies and the internationalization have totally changed our financial markets from structural and technical view-points[1].

Our financial institutions have come up with a wide range of financial products especially the investment related products. In the United States, investment funds are the most preferred financial instrument used by citizens to invest the money for meeting their after retirement expenses[2].The Mutual Fund Industry of India is of recent origin. Nearly five decades ago, with the establishment of the Unit Trust of India, the Indian Mutual Fund Industry came into existence. The industry has grown tremendously with about 42 mutual fund houses with the total assets under management as

189.66 billion US dollars, as of March 31, 2016[3].

According to the UK Financial Services Authority (FSA, 2005), financial capability includes the personal traits of an individual that are acted upon by several other factors in their micro and macro environment. The individuals live in a society so the interaction of the environmental factors (i.e. micro and macro like inflation, infrastructure, etc.) with those of the personal traits (i.e. demographic and mental factors) of the person is natural. These factors act as the determinants in the development of one's financial capability. Since the study focuses on the capability of our advisors, so discussing the behavioural risk is important. Though the notion that behavioural risks exist and their influence on the performance of the funds can be significant, still managers exhibit low level of self-awareness about the controlling of behavioural risks and the same is about our financial institutions which also show the low level of readiness towards behavioral risks[4].

Fund managers have the tendency to achieve the best possible place in the year-end performance-based rankings so that the greatest amount of inflow of funds is possible which in turn would help them in earning greater incentives. The research studies show that greed of earning more incentive creates tournament behavior among mutual fund managers, that is, those who lie at the lowest positions in the ranking at the end of the first part of the year (interim losers) try to move up to the higher and better positions in the list of rankings and for this they increase their exposure to risk to a greater extent than those fund managers in the best positions (interim winners), in an attempt to catch up with them[5]. Higher-compensated managers tend to outperform lesser-compensated managers[6].

LITERATURE REVIEW:

Sehgal (2017) studied that the fund selection capability of fund managers is largely dependent on two important factors. First, the stock picking skill and second, the market timing. The stock selection skills, which involve the micro-forecasting of movements in prices of individual stocks and identifying over or undervalued stocks relative to other equities in the market[7]

Olga Pak, Monowar Mahmood (2015) studied that there is a connection between the personality traits of investors' and their risk tolerance behaviour. This connection decides the way investors take decisions regarding their investments about stock, securities and bonds. Therefore, it becomes indispensable for the investment advisors to consider the personal characteristics and individual risk tolerance while making fund recommendations to the investors.[8]

Stephen Diacon (2004), studied that the growing complexities of the financial markets has complicated the investment decision process for common investors who lack knowledge and understanding of the financial matters. So for better decisions, often, such investors take the help of experts / financial advisors. But the thing is that the perception of financial advisors regarding the risk associated with a particular financial product may not necessarily be the same as that of the common investors. This distinction in perception is, therefore, crucial in deciding what products should be offered and how the products should be offered and what level of information and advice needs to be provided for different products to the common investors.[9]

Shaista Wasiuzzaman Siavash Edalat (2016): made an attempt to reveal how an individual's online social network activity can be used to understand that individual's financial risk tolerance. The study concluded that the persons with higher financial risk tolerance show high frequency of logging on to social network sites. However, when logging on to social network site shows high frequency for obtaining the social connections only then it is found to be associated with lower financial risk tolerance of the individual.[10]

Prateek Sharma and Samit Paul (2015) made an attempt to measure the skills of Indian mutual fund managers. The major conclusion was that the superior investment skill is lacking in the sample of Indian equity mutual funds because mutual funds could not beat the constrained random portfolios which was used and tested, as a framework to measure the skills of the mutual fund managers.[11]

Vinita Bharat Manek (2016), revealed how management style can have an influence on the returns of mutual fund schemes and the investors can use it as tool to decide how to make investments in schemes based on management styles.[12]

Shukla and Inwegen (1995), conducted a study which compared the foreign mangers with those of the local managers in UK and US. They concluded that local managers have greater access to investors as compared to the foreign managers.[13]

Avramov and Wermers (2006), found that the mutual funds outperformed market benchmarks and claim that the managers' skills are the dominant source of investment profitability.[14]

Klaas P. Baks (2001), studied that the performance of a mutual fund is dependent on two things-first, the manager who takes the investment decisions and second, the fund organization itself which plays an important role through administrative procedures, execution efficiency, quality of the analysts, relationships with companies, etc. The study makes the difference by studying the impact of the manager and the fund organization separately on the performance of the fund when most of the studies have studied the impact of these two things on performance in conjunction with each other. The performance is studied in terms of the Returns earned and the Assets under Management. Like in a production process, the study takes the managers, fund organization and the manager-fund combinations as the inputs and the performance of the fund as the output. After analyzing the impact of the concerned factors on the performance of the fund, it is found that managers are responsible for only 30% of the fund's performance and the rest of & the rest of 70% is actually contributed by the fund organization. The study concludes that the major determinant of the performance is thus the fund organization itself and not the manager.[15]

Lorenzo Casavecchia (2016) examined that though herding behavior is a common thing about the managers and investors. Those managers that refrain from herding behaviour usually possess above-average managerial skills, trade less on noise, and significantly outperform herding managers. It is also demonstrated that the stronger managerial incentive schemes are effective tools against the detrimental herding strategies and serve the purpose of an effective monitoring device to gauge the reactions of fund managers towards the poor flow-performance sensitivity. This way the stronger managerial incentive schemes help in the better governance of the invested funds[16].

From the review of the previous studies it becomes clear that the researchers are actively carving out the details about the behaviour of the managers and the investors towards the fund selection. But still the literature that is available so far is scarce and hence, further studies need to be conducted in this area so that more enlightenment is possible for all types of stakeholders of the industry. This study is an attempt in the same pursuit of revealing further insights about the Capability of the mutual fund managers and advisors regarding the selection of mutual funds.

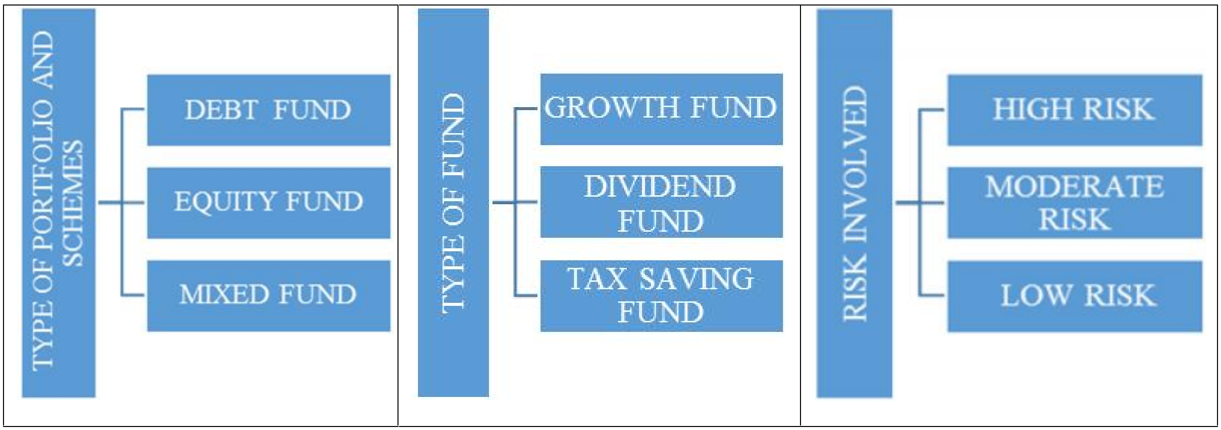
OBJECTIVE OF THE STUDY:

The main objective of the study is to find the factors that matter to the financial advisors while making recommendations about the mutual fund schemes to the Indian mutual fund investors.

RESEARCH METHODOLOGY:

Fund advisors / managers take into consideration the attributes of the mutual fund schemes before making the actual fund selection. The attributes of the fund schemes have to be attractive for both the advisors as well as the investors. Developing such fund schemes that suit the fund advisors by the Mutual Fund Companies is easier when the companies consider the type of importance its advisors/managers attach to different types of attributes and combinations thereof for given mutual fund schemes while making fund recommendations. There is a technique that serves this purpose the best, namely Conjoint Analysis. This technique helps in identifying the combinations of attributes that will be most preferred by the managers, advisors or even the investors. Conjoint analysis is a survey-based statistical technique a limited number of attributes is most influential on respondents' choice or decision making.

The attributes that are mostly given importance by the financial advisors while offering the mutual fund schemes to the investors include Type of Fund, Type of portfolio and schemes, Risk involved in Mutual Funds, Past Performance of the Fund, the Current Market Conditions and the Brand Equity as revealed by the literature review in the past. There can be several other factors as well but we take only the above mentioned factors into consideration in this study See Fig.1.



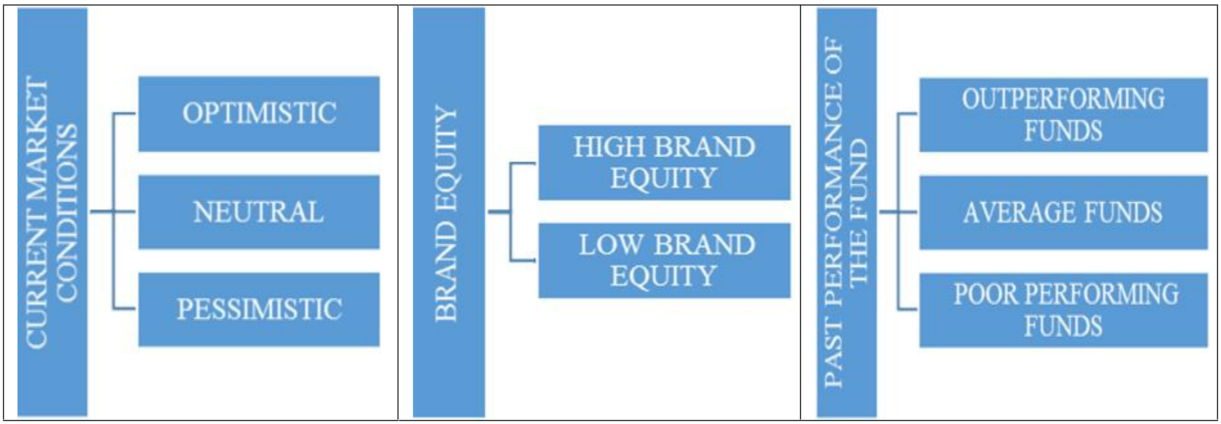


Fig.1

Thus, the possible combinations of these attributes that the financial advisors can consider for recommending a particular fund/scheme to the investors here totaled **3×3×3×3×2×3×= 486** combinations.

This becomes practically cumbersome to consider all the possible combinations for the advisors/managers. Thus, we employ a technique called the orthogonal array which is a special type of fractional factorial design. It helps in reducing the original factorial design that resulted in large number of combinations to a small number of combinations called as the stimuli combinations. This way only the outstanding combinations of the attributes that need to be given the priority come to the knowledge of the managers/advisors. Here in this study, finally, 16 combinations were recognized after the application of the technique.

These combinations were used in developing the questionnaire. The respondents were asked to rate each of the attribute combination on the scale of 5, where 5 denoted strongly recommended and 1 represents strongly not recommended.

Sample Size:
After developing the questionnaire, 100 questionnaires were distributed among the mutual fund advisors. However, due to non-response rate of 10% only 90 questionnaires were returned. The demographic characteristics of the sample are given in Table1.

Table1 depicts that the dominant gender among the financial advisors is that of males, 84 in number, constituting about 93.33% of the total 90 respondents. Regarding the marital status of the advisors, out of 90 respondents, 69 are married constituting 76.67% of the total. Most of the advisors belong to the age group of 50-60yrs, constituting about 51% of the total number of respondents (90). Most of the advisors in the given sample possess post-graduation as their educational qualification. 51% of the advisors fall in the category of 10-15yrs of experience as financial advisors.

Table1
Demographic Pattern

Gender		**Educational qualification**	
Male	93.33	Under graduates	03.00
Female	06.67	Graduates	31.00
Total	100.00	Post graduates	39.00
Marital Status			
Unmarried	23.33	Professionals	27.00
Married	76.67	Total	100.00
		Experience as FA	
Total	100.00	Less than 5yrs.	09.00

Age Group			
Less than 40 yrs.	10 00	5-10yrs.	21.00
40-50yrs.	17.00	10-15yrs	51.00
50-60yrs.	51.00	Above 15yrs.	19.00
Above 60yrs.	22.00	Total	100.00
Total	100.00		

Note: FA denotes Financial Advisor; Sample size n = 90; Figures are percentages

Research Findings:
The statistical measure employed to know about the goodness of fit is Coefficient of Determination (R2). R2 is a statistical measure which depicts how well the regression line approximates the real data points. The value of R2 is given by taking the square of the value of Pearson's coefficient of correlation R. It was found that the value of R2 comes out to be 0.896, significant at 5% level. The results are shown graphically.

Figure2, clearly depicts the relative importance that the advisors attach to each of the selected six factors in our study. The Past Performance of the mutual fund dominates all other factors that are given due consideration while recommending the funds.

After past performance of a fund, the Risk involved in a fund stands as the second important factor considered by the financial advisors. The Brand Equity follows next.

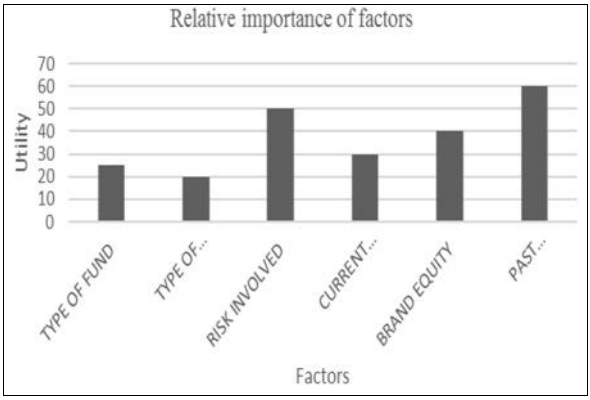


Fig2

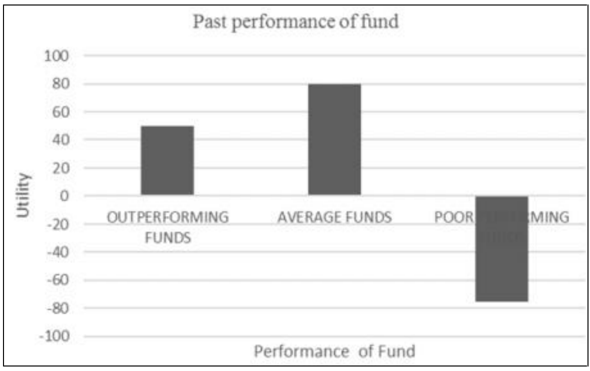


Fig3

Upon analyzing the past performance, it is evident that fund advisors recommend average performing funds mostly as the utility for them is comparatively higher. The outperforming funds stand next to Average Funds. The poor performing funds are usually not recommended by the advisors as the utility for them suggests so.

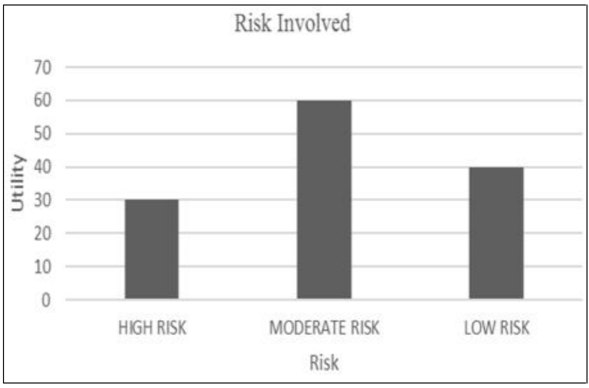


Fig4

The advisors seem to adhere to the golden rule that the higher the returns, the more is the risk involved. The funds having moderate risk have been mostly preferred by the advisors, this makes it clear that the advisors believe in value addition without putting the hard-earned money of the investors at stake.

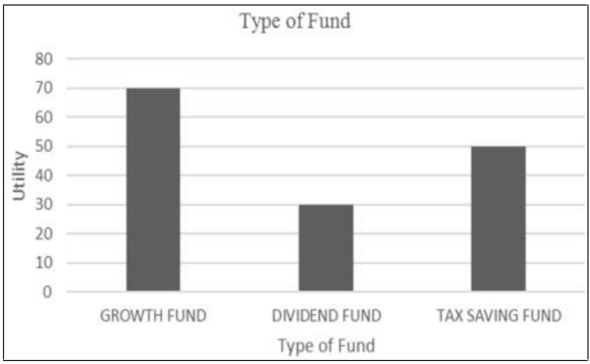


Fig5

The growth funds dominate the other type of funds available to the advisors. After the growth funds, the tax savings funds are recommended, thereby leaving the dividend funds behind in terms of utility shown by the advisors. In India, the mutual industry is more debt oriented. This is again supported by the utility shown by the advisors for the

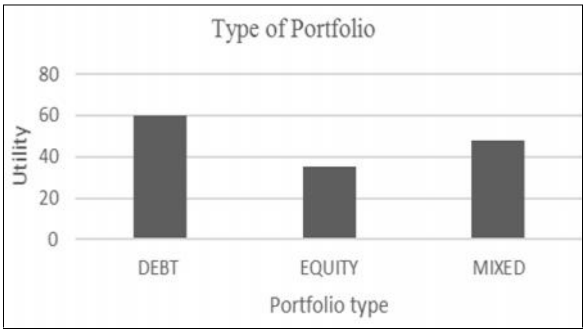


Fig6

Debt type funds.Advisors seem to be more concerned about the Brand equity enjoyed by a particular fund. Funds with high Brand equity are favorite to the financial advisors in the Indian context.

Fig7

CONCLUSION:

This paper makes an effort to understand the factors that are important to the financial advisors while making recommendations of mutual fund schemes to the investors in India. The study has been successfully able to explore some of the factors that are considered important by the financial advisors. As the Indian Mutual fund Industry has a long way to go for reaching to the matured stage of its life cycle, therefore, understanding its each aspect is highly indispensable for the same. This study actually paves the way for AMC to tailor their products as per the requirements of their customers as reflected by the fund selection decisions made by the financial advisors. The important factors that are considered by the financial advisors in the Indian context include the Type of Portfolio, the Type of Fund, the Past Performance of a mutual fund, the Risk associated with it, Brand equity of a fund and the Current market conditions.

The average performing funds which involve moderate level of risk and are mostly debt oriented are recommended by the financial advisors. The advisors believe the presence of optimistic conditions are conducive for the better returns on fund investments. If the brand equity for a particular fund is high, the advisors perceive such funds as the mouth-watering ones. To conclude, if the mutual fund industry has to show tremendous growth in a short span of time, then the role of financial advisors has to be strengthened further. Further the studies need to be carried out that will cover each and every aspect of the financial advisors thereby fostering the individual investors' confidence in the mutual fund investment by enhanced satisfaction.

REFERENCES:

1. Pellinen and Uusitalo (2010), "Measuring the financial capability of investors: A case of the customers of mutual funds in Finland", International Journal of Bank Marketing, Vol. 29 No. 2, 2011. pp. 107-133.
2. L. Cohen and B. Schmidt (2009), "Attracting flows by attracting big clients", Journal of Finance, 64, pp. 2125-2151
3. Sanjay Sehgal and Sonal Babbar (2017)," Evaluating alternative performance benchmarks for Indian mutual fund industry", Journal of Advances in Management Research, Vol. 14 Iss 2, pp. 1-40.
4. Zamri Ahmad, Haslindar Ibrahim and Jasman Tuyon (2017), "Behavior of fund managers in Malaysian investment management industry", Qualitative Research in Financial Markets, Vol. 9 Issue: 3, pp.205-239
5. K.C. Brown, W.V. Harlow, L.T. Starks (1996), "Of tournaments and temptations: an analysis of managerial incentives in the mutual fund industry", Journal of Finance, 15 pp. 85-110
6. James Philpot and A. Peterson, (2006),"Manager Characteristics and real estate mutual fund returns, risk and fees", Managerial Finance, Vol. 32 Iss 12 pp. 988 – 996
7. Sanjay Sehgal and Sonal Babbar , (2017)," Evaluating alternative performance benchmarks for Indian mutual fund industry", Journal of Advances in Management Research, Vol. 14 Iss 2, pp. 1-40.
8. Olga Pak, Monowar Mahmood, (2015) "Impact of personality on risk tolerance and investment decisions: A study on potential investors of Kazakhstan", International Journal of Commerce and Management, Vol. 25 Issue: 4, pp.370-384, doi: 10.1108/IJCoMA-01-2013-0002.
9. Stephen Diacon, (2004) "Investment risk perceptions: Do consumers and advisers agree?" International Journal of Bank Marketing, Vol. 22 Issue: 3, pp.180-199, doi: 10.1108/02652320410530304.
10. Shaista Wasiuzzaman and Siavash Edalat, (2016),"Personality, risk tolerance and social network use: an exploratory study", Managerial Finance, Vol. 42 Iss 6, pp. 536 – 552.
11. Prateek Sharma and Samit Paul, (2015) "Testing the skill of mutual fund managers: evidence from India", Managerial Finance, Vol. 41 Issue: 8, pp.806-824, doi: 10.1108/MF-04-2014-0112.
12. Vinita Bharat Manek. (2016), "Mutual Fund Performance: A Study on the Effect of Portfolio Turnover on Mutual Fund Performance in the Indian Financial Market", Scholarly Research Journal for Interdisciplinary Studies, Volume-3/23, March-April, 2016
13. Shukla, R.K. and Van Inwegen, G.B. (1995), "Do Local perform better than Foreigners? An Analysis of UK and US Mutual Fund Managers", Journal of Economics and Business, Vol. 47, pp. 241-54.
14. Avramov, D. and Wermers, R. (2006), "Investing in mutual funds when returns are predictable", Journal of Financial Economics, Vol. 81 No. 2, pp. 339-377.
15. On the performance of Mutual fund managers –American University. Retrieved from: www1.american.edu/academic.depts/ksb/finance_realestate/mrobe/.../Baks.pdf
16. Lorenzo Casavecchia, (2016) "Fund managers' herding and mutual fund governance", International Journal of Managerial Finance, Vol. 12 Issue: 3, pp.242-276.