

***An Empirical Study on Factors Influencing the
Mutual Fund/Scheme Selection by Retail Investors***

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Abstract

MF is a retail product designed to target small investors, salaried people and others who are intimidated by the mysteries of stock market but, nevertheless, like to reap the benefits of stock market investing. At the retail level, investors are unique and are a highly heterogeneous group. Hence, their fund/scheme selection also widely differs. Investors demand inter-temporal wealth shifting as he or she progresses through the life cycle. This necessitates the Asset Management Companies (AMCs) to understand the fund/scheme selection/switching behaviour of the investors to design suitable products to meet the changing financial needs of the investors. With this background a survey was conducted among 350 Mutual Fund Investors in 10 Urban and Semi Urban centers to study the factors influencing the fund/scheme selection behaviour of Retail Investors. This paper discusses the survey findings. It is hoped that it will have some useful managerial implication for the AMCs in their product designing and marketing.

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Introduction :

In financial markets, “expectations” of the investors play a vital role. They influence the price of the securities, the volume traded and determine quite a lot of things in actual practice. These ‘expectations’ of the investors are influenced by their “perception” and humans generally relate perception to action. The beliefs and actions of many investors are influenced by the dissonance effect and endowment effect. ***The tendency to adjust beliefs to justify past actions is a psychological phenomenon termed by Festinger (1957) as Cognitive Dissonance.*** We find ample proof for the wide prevalence of such a psychological state among Mutual Fund (MF) investors in India. For instance, UTI had a glorious past and had always been perceived as a safe, high yield investment vehicle with the added tax benefit. Many UTI account holders had justified their beliefs by staying invested in UTI schemes even after the 1999 bail out and many have still not lost faith in UTI, even after the July 2001 episode. “Endowment Effect” is explained by Thaler Kahneman and Knetsch (1992) as ***“People are more likely to believe that something they own is better than something they do not own”***. We have evidence for the influence of this effect also among Indian MF investors, for, how else can we explain the reason for the existence of many poor performing funds without investors staying invested with them?

However, in the financial literature, there are no models which explain the influence of these “perceptions” and “beliefs” on “Expectations” and “Decision Making”. Because of our own inability to understand the sources of motivations and the basis of these expectations we tend to ignore it. No doubt, reality is so complex that trying to fit an individual investor’s beliefs into a model is impossible. But, to a certain extent, we can borrow concepts from social psychology where behavioural patterns, rational or irrational, are developed and empirically tested. On the same lines, we can develop certain models to test the financial behaviour, to the extent of the availability of the explanatory variables. Such models can help to understand the Why? and How? aspect of investor behaviour, which can have managerial implications for policy makers.

Background and Need for the Study :

It is widely believed that MF is a retail product designed to target small investors, salaried people and others who are intimidated by the stock market but, nevertheless, like to reap the benefits of stock market investing. At the retail level, investors are unique and are a highly heterogeneous group. Hence, designing a general product and expecting a good response will be futile, though

UTI could do this nearly for three decades (1964-1987) due to its monopoly in the industry. In the second phase of oligopolistic competition (1987-1992), the public sector banks and financial institutions entered the field, but with the then existing boom condition, it was a smooth sailing for the industry. Further, the globalisation and liberalization measures announced by the government led to a paradigm shift in the mind set of investors and the capital market environment became more unfriendly to retail investors. They had no other choice but to turn to MFs to reap the benefits of stock market investing. Hence, the need to be innovative in designing the product was not felt and investors had to choose from among the limited schemes offered. During the third phase (1992 hence) the industry was thrown open to the private sector and the stage got set for competition.

Currently (as on 31/3/2001) there are 326 schemes (Source : Mutual Fund Year Book, 2000) with varied objectives and AMCs compete against one another by launching new products or repositioning old ones. In the future, MF industry has to face competition not only from within the industry but also from other financial products that may provide many of the same economic functions as mutual funds but are not strictly MFs. For example, in US, one savings institution has patented a product that promises to deliver consumers a pay off indexed to college tuition costs, thus attempting to meet a common consumer requirement [Ellen Schultz (1992)]. This product is structured as a certificate of deposit but it could have been set up as a Mutual Fund. Such products will shortly appear in the Indian market also. All this, in aggregate, heightens the consumer confusion in his selection of the product. He is confused as to how to sift the grain from the chaff? Unless the MF schemes are tailored to his changing needs, and unless the AMCs understand the fund selection/switching behaviour of the investors, survival of funds will be difficult in future. With this background an attempt is made in this paper to study the factors influencing the fund/scheme selection behaviour of Retail Investors.

Objectives of the Study:

In order to examine the issues raised above, this paper has the following objectives before it :

- 1) To understand the savings avenue preference among MF investors
- 2) To identify the features the investors look for in Mutual Fund products
- 3) To identify the scheme preference of investors
- 4) To identify the factors that influence the investor's fund/scheme selection
- 5) To identify the information sources influencing the scheme selection decision.
- 6) To identify the preferred communication mode.

Limitations of the Study :

- 1) Sample size is limited to 350 educated investors in Urban and Semi-Urban cities only. The sample size may not adequately represent the national market.
- 2) This study has not been conducted over an extended period of time having both market ups and downs. The market state has a significant influence on the buying patterns and preferences of investors. For example, the July 2001 UTI fall has sent violent shock waves across the MF investor community and is bound to influence the scheme preference/selection of the investors. The study has not captured such situations.

Review of Literature :

The existing “Behavioural Finance” studies are very few and very little information is available about investor perceptions, preferences, attitudes and behaviour. All efforts in this direction are fragmented.

Ippolito (1992) says that fund/scheme selection by investors is based on past performance of the funds and money flows into winning funds more rapidly than they flow out of losing funds.

Goetzman (1997) states that there is evidence that investor psychology affects fund/scheme selection and switching.

De Bondt and **Thaler** (1985) while investigating the possible psychological basis for investor behaviour, argue that mean reversion in stock prices is an evidence of investor over reaction where investors overemphasise recent firm performance in forming future expectations.

In India, one of the earliest attempts was made by NCAER in 1964 when a survey of households was undertaken to understand the attitude towards and motivation for saving of individuals. Another NCAER study in 1996 analysed the structure of the capital market and presented the views and attitudes of individual shareholders. **SEBI – NCAER Survey** (2000) was carried out to estimate the number of households and the population of individual investors, their economic and demographic profile, portfolio size, investment preference for equity as well as other savings instruments. This is a unique and comprehensive study of Indian Investors, for, data was collected from 3,00,000 geographically dispersed rural and urban households. Some of the relevant findings of the study are : Households preference for instruments match their risk perception; Bank Deposit has an appeal across all income class; 43% of the non-investor households equivalent to around 60 million households (estimated) apparently lack awareness about stock markets; and, compared with low income groups, the higher income groups have higher share of investments in Mutual Funds (MFs)

signifying that MFs have still not become truly the investment vehicle for small investors. Nevertheless, the study predicts that in the next two years (i.e., 2000 hence) the investment of households in MFs is likely to increase. We have to wait and watch the investors' reaction to the July 2nd 2001, great fall of the Big Brother, UTI. (Note : Behaviour is a reaction to a situation. So as situation changes, behaviour gets modified. Hence, findings and predictions of behaviour studies should be viewed accordingly).

Gupta (1994) made a household investor survey with the objective to provide data on the investor preferences on MFs and other financial assets. The findings of the study were more appropriate, at that time, to the policy makers and mutual funds to design the financial products for the future.

Kulshreshta (1994) offers certain guidelines to the investors in selecting the mutual fund schemes.

Shanmugham (2000) conducted a survey of 201 individual investors to study the information sourcing by investors, their perceptions of various investment strategy dimensions and the factors motivating share investment decisions, and reports that among the various factors, psychological and sociological factors dominated the economic factors in share investment decisions.

Madhusudhan V Jambodekar (1996) conducted a study to assess the awareness of MFs among investors, to identify the information sources influencing the buying decision and the factors influencing the choice of a particular fund. The study reveals among other things that Income Schemes and Open Ended Schemes are more preferred than Growth Schemes and Close Ended Schemes during the then prevalent market conditions. Investors look for safety of Principal, Liquidity and Capital appreciation in the order of importance; Newspapers and Magazines are the first source of information through which investors get to know about MFs/Schemes and investor service is a major differentiating factor in the selection of Mutual Fund Schemes.

Sujit Sikidar and Amrit Pal Singh (1996) carried out a survey with an objective to understand the behavioural aspects of the investors of the North Eastern region towards equity and mutual funds investment portfolio. The survey revealed that the salaried and self employed formed the major investors in mutual fund primarily due to tax concessions. UTI and SBI schemes were popular in that part of the country then and other funds had not proved to be a big hit during the time when survey was done.

Syama Sunder (1998) conducted a survey to get an insight into the mutual fund operations of private institutions with special reference to Kothari Pioneer. The survey revealed that awareness about Mutual Fund concept was poor during that time in small cities like Visakapatnam. Agents play a vital role in spreading the Mutual Fund culture; open-end schemes were much preferred then; age and

income are the two important determinants in the selection of the fund/scheme; brand image and return are the prime considerations while investing in any Mutual Fund.

Anjan Chakarabarti and Harsh Rungta (2000) stressed the importance of brand effect in determining the competitive position of the AMCs. Their study reveals that brand image factor, though cannot be easily captured by computable performance measures, influences the investor's perception and hence his fund/scheme selection.

Shankar (1996) points out that the Indian investors do view Mutual Funds as commodity products and AMCs, to capture the market should follow the consumer product distribution model.

Since 1986, a number of articles and brief essays have been published in financial dailies, periodicals, professional and research journals, explaining the basic concept of Mutual Funds and highlight their importance in the Indian capital market environment. They touch upon varied aspects like Regulation of Mutual Funds, Investor expectations, Investor protection, Trend in growth of Mutual Funds and some are critical views on the performance and functioning of Mutual Funds. A few among them are **Vidyashankar** (1990), **Sarkar** (1991), **Agarwal** (1992), **Sadhak** (1991), **Sharma C. Lall** (1991), **Samir K. Barua et al.**, (1991), **Sandeep Bamzai** (2001), **Atmaramani** (1995), **Atmaramani** (1996), **Subramanyam** (1999), **Krishnan** (1999), **Ajay Srinivassan** (1999). Segmentation of investors on the basis of their characteristics was highlighted by **Raja Rajan** (1997). Investor's characteristics on the basis of their investment size **Raja Rajan** (1997), and the relationship between stage in life cycle of the investors and their investment pattern was studied **Raja Rajan** (1998).

From the above review it can be inferred that Mutual Fund as an investment vehicle is capturing the attention of various segments of the society, like academicians, industrialists, financial intermediaries, investors and regulators for varied reasons and deserves an indepth study.

In this paper, an attempt is made by the author, mainly to study the factors which influence the investors in their selection of the fund/scheme.

Data Collection :

This paper makes use of some of the data collected in a survey by the author for her doctoral thesis, which is under progress. The survey was conducted during April, May and June 2000, among 350 geographically dispersed present investors spread over 10 Urban and Semi-Urban cities. Area profile of Investors is given in Annex – Table 1. Distribution of the present investors by demographic factors is given in Annex – Table 2. The unit of observation and analysis of this survey is the individual present retail investor. Our definition of present retail investor is

“An individual who has currently (i.e., as on April, May or June 2000) invested in any MF scheme and it does not include high net-worth individuals (i.e., those who earn above 6,00,000/- per annum) and Institutions. The required data was collected through a pre-tested questionnaire which was administered on a judgement sample of 350 educated present retail investors. Judgement sample selection is due to the time and financial constraints.

Framework of Analysis :

To understand the savings avenue preference, scheme preference and objectives for investment in MFs, and to identify the information sources influencing scheme selection, and the preferred mode of communication, the respondents were asked to rank their preferences on a ranking scale. The ranks were ascertained by obtaining the weighted mean value of the responses. To identify the factors that influence the investors fund/scheme selection, 23 variables were identified through a brainstorming session and evidence from past research prior to the construction of the questionnaire at the time of the pilot study. The people involved in brainstorming session were selected from two places, Anantapur (semi-urban centre) and Bangalore (urban centre) and the profile is given in Annex – Table 3.

Based on theory, past research, and judgment of the researcher, the factors that could influence the investors in their selection of Mutual funds/schemes was first grouped into 3 major factors – Fund/Scheme qualities, fund sponsor qualities and the expected investor services. Then the 23 identified variables were classified under the appropriate group as follows :

A) Product Qualities

- A1 Fund's/Scheme's performance record
- A2 Fund's/Scheme's reputation or brand name
- A3 Scheme's expense ratio
- A4 Scheme's portfolio of investments
- A5 Reputation of scheme(s), portfolio manager(s)
- A6 Withdrawal facilities
- A7 Favourable rating by a rating agency
- A8 Innovativeness of the Scheme
- A9 Products with tax benefits
- A10 Entry and Exit load

B) Fund Sponsor Qualities

- B1 Reputation of a sponsoring firm
- B2 Sponsor offers a wide range of schemes with different investment objectives
- B3 Sponsor has a recognised brand name

- B4 Sponsor has a well developed Agency Net Work/Infrastructure
- B5 Sponsor has an efficient research wing
- B6 Sponsor's expertise in managing money

C) Investor Services

- C1 Disclosure of investment objectives, method and periodicity of valuation in advertisement
- C2 Disclosure of the method and periodicity of the scheme's sales and repurchase in the offer documents
- C3 Disclosure of NAV on every trading day
- C4 Disclosure of deviation of the investments from the original pattern
- C5 Disclosure of scheme's investments on every trading day
- C6 Mutual Fund Investors' grievance redressal machinery
- C7 Fringe benefit like free insurance, free credit card, loans on collateral, tax benefits etc.

In the survey, the respondents were asked to rate the importance of the 23 specified variables on a 5 point scale ranging from Highly Important (5) to Not at all Important (1). The data for each of the 3 sub-groups were factor analysed using Principal Component Analysis, with the objective of identifying the factor in the sub-group which turns out to be significant in the fund/scheme selection.

Summary and Findings

The survey reveals that the most preferred investment vehicle is Bank Deposits, with MFs ranking 4th in the order among 8 choices (Annex – Table 4). Growth schemes are ranked first, followed by Income Schemes and Balanced Schemes (Annex – Table 5). Based on the duration of operation of schemes, the 1st preference is for open-ended schemes (84.57%) and only 15.43% of the respondents favour close-ended schemes. The investors look for safety first in MF products, followed by good returns, Tax Benefits, liquidity and capital appreciation (Annex – Table 6). The survey further reveals that the scheme selection decision is made by respondents on their own, and the other sources influencing their selection decision are News papers and Magazines, Brokers and Agents, Television, Friends suggestions and Direct Mail in that order (Table 7). Further 44% of the respondents reported that they use internet facility to know more about MFs while 56% reported that they do not have access to Internet. Further, 37.43% of the respondents prefer to get the routine/special information like daily NAV, dividend, bonus, change in asset mix etc., through automated response system while 53.71% prefer personal communication and 8.86% have no preference. The findings regarding the influential fund selection factors are :

Influence of Product Qualities on Selection of Fund/Scheme

The 10 fund related variables were analysed for their importance. The analysis reveals that the investor considers all the 10 variables as important in his

selection of the fund/scheme. The weighted mean value and scale importance is given in Table 1.

Table - 1

Importance of product related factors in fund/scheme selection

| <i>Sl. No.</i> | <i>Variable</i> | <i>WMV</i> | <i>Std. Dev.</i> | <i>Scale Importance</i> |
|-----------------------|--|-------------------|-------------------------|--------------------------------|
| 1 | Fund's/Scheme's performance records | 4.37 | 0.78 | Important |
| 2 | Fund/Scheme's reputation or brand name | 4.21 | 0.73 | Important |
| 3 | Scheme's Expense ratio | 3.62 | 0.95 | Important |
| 4 | Scheme's portfolio of Investment | 4.15 | 0.93 | Important |
| 5 | Reputation of scheme(s) portfolio manager(s) | 3.99 | 0.90 | Important |
| 6 | Withdrawal/Exit facility | 4.10 | 0.86 | Important |
| 7 | Favourable rating by a rating agency | 3.85 | 1.02 | Important |
| 8 | Innovativeness of the scheme | 3.60 | 0.97 | Important |
| 9 | Products with tax benefits | 3.91 | 1.02 | Important |
| 10 | Entry and exit load | 3.66 | 1.02 | Important |

Hence, to identify the investor's underlying fund/scheme selection criteria, so as to group them into specific market segment to enable the designing of the appropriate marketing strategy, Factor Analysis was done using Principal Component Analysis.

Bartlett's test of sphericity and Kaiser-Meyer Olkin (KMO) measure of sampling adequacy were used to examine the appropriateness of factor analysis. The approximate chi-square statistic is 311.425 with 45 degrees of freedom which is significant at 0.05 level. The KMO statistic (0.684) is also large (>0.5). Hence factor analysis is considered as an appropriate technique for further analysis of data.

Results of Principal Component Analysis for Product related qualities are tabulated in Table 2.

Table - 2
Results of Principal Component Analysis

Bartlett's Test of sphericity

Approximate chi-square =311.425; df=45; significance = 0.000

Kaiser-Meyer-Olkin Measure of Sampling Adequacy = 0.684

| Communalities | | | Initial Eigen Values | | | |
|----------------------|----------------|-------------------|-----------------------------|--------------------|----------------------|---------------------|
| Variable | Initial | Extraction | Factor | Eigen value | % of variance | Cumulative % |
| A1 | 1.000 | 0.438 | 1 | 2.327 | 23.268 | 23.268 |
| A2 | 1.000 | 0.798 | 2 | 1.265 | 12.653 | 35.921 |
| A3 | 1.000 | 0.248 | 3 | 1.086 | 10.861 | 46.782 |
| A4 | 1.000 | 0.675 | 4 | 0.971 | 9.710 | 56.492 |
| A5 | 1.000 | 0.409 | 5 | 0.931 | 9.307 | 65.799 |
| A6 | 1.000 | 0.371 | 6 | 0.870 | 8.701 | 74.500 |
| A7 | 1.000 | 0.352 | 7 | 0.710 | 7.098 | 81.598 |
| A8 | 1.000 | 0.359 | 8 | 0.693 | 6.930 | 88.528 |
| A9 | 1.000 | 0.593 | 9 | 0.610 | 6.098 | 94.626 |
| A10 | 1.000 | 0.435 | 10 | 0.537 | 5.374 | 100.00 |

| Factor | Extraction Sums of Squared Loadings | | | Rotation Sums of Squared Loadings | | |
|---------------|--|----------------------|---------------------|--|----------------------|---------------------|
| | Eigen Value | % of Variance | Cumulative % | Eigen Value | % of Variance | Cumulative % |
| 1 | 2.327 | 23.268 | 23.268 | 2.006 | 20.059 | 20.059 |
| 2 | 1.265 | 12.653 | 35.921 | 1.481 | 14.809 | 34.868 |
| 3 | 1.086 | 10.861 | 46.782 | 1.191 | 11.914 | 46.782 |

| Variable | Factor Matrix | | | Rotated Factor Matrix | | |
|-----------------|----------------------|-----------------|-----------------|------------------------------|-----------------|-----------------|
| | Factor 1 | Factor 2 | Factor 3 | Factor 1 | Factor 2 | Factor 3 |
| A1 | 0.316 | 0.429 | -0.392 | 6.193E-02 | 0.641 | -0.153 |
| A2 | 0.234 | 0.194 | 0.840 | 2.400E-02 | -5.785E-02 | 0.891 |
| A3 | 0.416 | 0.272 | -2.558E-02 | 0.202 | 0.423 | 0.166 |
| A4 | 0.354 | 0.700 | -0.245 | -6.480E-02 | 0.816 | 6.913E-02 |
| A5 | 0.542 | 0.250 | 0.229 | 0.299 | 0.369 | 0.428 |
| A6 | 0.468 | -0.389 | -1.907E-02 | 0.604 | -7.630E-02 | -1.173E-03 |
| A7 | 0.551 | -0.199 | 9.141E-02 | 0.562 | 7.093E-02 | 0.177 |
| A8 | 0.589 | -0.102 | 4.759E-02 | 0.544 | 0.182 | 0.174 |
| A9 | 0.540 | -0.446 | -0.320 | 0.719 | 2.876E-02 | -0.275 |
| A10 | 0.646 | -0.131 | 7.126E-03 | 0.611 | 0.202 | 0.144 |

Retaining only the variables with eigen values greater than one (Kaiser's criterion), we can infer that 23.268% of variance is explained by factor 1; 12.653% of variance is explained by factor 2 and 10.861% of variance is explained by factor 3 and together, all three factors contributed to 46.782% of variance.

Factor loadings are very high in case of factor 1 (5 out of 10 variables have factor loading >0.5). It reveals that 50% of the variables are clubbed into one factor. But on the basis of theory, we can infer that there must be more than one factor. Therefore, Varimax Rotation was done to obtain factors that can be named and interpreted. Under Varimax Rotation also 5 out of 10 variables have factor loadings >0.5 in case of factor 1.

On the basis of Varimax Rotation with Kaiser Normalisation, 3 factors have emerged. Each factor is constituted of all those variables that have factor loadings greater than or equal to 0.5. Thus A6, A7, A8, A9 and A10 constituted the first factor. The researcher conceptualised this factor as "Intrinsic Product Qualities"; A1 and A4 constituted the second factor and this was conceptualized as "Portfolio Management"; A2 constituted the 3^d factor and was conceptualized as "Image" factor.

Thus, after rotation, factor 1 (Intrinsic Product Qualities) accounts for 20.059% of the variance; factor 2 (Portfolio Management) accounts for 14.809% of variance and factor 3 (Image) accounts for 11.914% of variance and all 3 factors together explain for 46.782% of variance. The identified factors with the associated variable and factor loadings are given in Table 3.

Table - 3
Identification of product related factors in fund/scheme selection

| Factor Name | | Variables | Factor Loadings |
|------------------------------------|-----|------------------------------|------------------------|
| Intrinsic qualities of the product | A6 | Withdrawal/Exit facility | 0.604 |
| | A7 | Favourable Rating | 0.562 |
| | A8 | Innovativeness of the Scheme | 0.544 |
| | A9 | Tax Benefits | 0.719 |
| | A10 | Entry and Exit load | 0.611 |
| Portfolio Management | A1 | Performance Record | 0.641 |
| | A4 | Portfolio of Investment | 0.816 |
| Image | A2 | Reputation and Brand Name | 0.891 |

Influence of Fund Sponsor Qualities on Selection of Fund/Scheme

The six sponsor related variables were analysed for their importance. The analysis reveals that the investor considers all the six variables as important in his selection of the fund/scheme. The weighted mean value and scale importance is given in Table 4.

Table - 4
Importance of sponsor related factors in fund/scheme selection

| <i>Sl. No.</i> | <i>Variable</i> | <i>WMV</i> | <i>Std. Dev.</i> | <i>Scale Importance</i> |
|-----------------------|---|-------------------|-------------------------|--------------------------------|
| B1 | Reputation of the sponsoring firm | 4.29 | 0.79 | Important |
| B2 | Sponsor's ability to offer a wide range of schemes with different investment objectives | 3.75 | 0.88 | Important |
| B3 | Sponsor has a recognised brand name | 3.99 | 0.86 | Important |
| B4 | Sponsor has a well developed agency network/ infrastructure | 4.06 | 0.89 | Important |
| B5 | Sponsor has an efficient research wing | 3.96 | 1.04 | Important |
| B6 | Sponsor's expertise in managing money | 4.37 | 0.83 | Important |

Hence, to identify the investor's sponsor related qualities which influence his fund/scheme selection, so as to enable the sponsors to develop the identified qualities, Factor Analysis was done using Principal Component Analysis.

Results of principal component analysis for sponsor related qualities are tabulated in Table 5.

Table - 5
Results of Principal Component Analysis

Bartlett's Test of sphericity

Approximate chi-square = 328.627; df=15; significance = 0.000

Kaiser-Meyer-Olkin Measure of Sampling Adequacy = 0.702

Communalities

Initial Eigen Values

| Variable | Initial | Extraction | Factor | Eigen value | % of variance | Cumulative % |
|-----------------|----------------|-------------------|---------------|--------------------|----------------------|---------------------|
| B1 | 1.000 | 0.362 | 1 | 2.376 | 39.605 | 39.605 |
| B2 | 1.000 | 0.530 | 2 | 1.009 | 16.824 | 56.428 |
| B3 | 1.000 | 0.636 | 3 | 0.796 | 13.262 | 69.690 |
| B4 | 1.000 | 0.675 | 4 | 0.737 | 12.280 | 81.970 |
| B5 | 1.000 | 0.758 | 5 | 0.673 | 11.212 | 93.182 |
| B6 | 1.000 | 0.426 | 6 | 0.409 | 6.818 | 100.000 |

| Factor | Extraction Sums of Squared Loadings | | | Rotation Sums of Squared Loadings | | |
|---------------|--|----------------------|---------------------|--|----------------------|---------------------|
| | Eigen Value | % of Variance | Cumulative % | Eigen Value | % of Variance | Cumulative % |
| 1 | 2.376 | 39.605 | 39.605 | 1.776 | 29.593 | 29.593 |
| 2 | 1.009 | 16.824 | 56.428 | 1.610 | 26.835 | 56.428 |

| Variable | Factor Matrix | | Rotated Factor Matrix | |
|-----------------|----------------------|-----------------|------------------------------|-----------------|
| | Factor 1 | Factor 2 | Factor 1 | Factor 2 |
| B1 | 0.550 | 0.242 | 0.251 | 0.546 |
| B2 | 0.546 | 0.481 | 8.975E-02 | 0.722 |
| B3 | 0.606 | 0.519 | 0.110 | 0.790 |
| B4 | 0.708 | -0.417 | 0.806 | 0.157 |
| B5 | 0.698 | -0.520 | 0.867 | 7.388E-02 |
| B6 | 0.648 | -8.068E-02 | 0.538 | 0.369 |

Retaining only variables with Eigen Values greater than 1, we can infer that 39.605% of variance is explained by factor 1 and 16.824% of variance is explained by factor 2, both together contributing 56.428%.

A scrutiny of Factor Matrix reveals that factor loadings are very high in case of factor 1 (all six variables have factor loading >0.5). It reveals that all variables are clubbed into one factor. But, on the basis of theory we can infer that there must be more than one factor. Therefore, Varimax Rotation was done to obtain factors that can be named and interpreted.

On the basis of Varimax Rotation with Kaiser Normalisation, 2 factors emerged. Each factor is constituted of all those variables that have factor loadings greater than or equal to 0.5. Thus, B4, B5 and B6 constituted the first factor. The researcher conceptualised this factor as “Infrastructure” and B1, B2 and B3 constituted the second factor and this was conceptualized as “Reputation”.

Thus, after rotation, factor 1 (Infrastructure) accounts for 29.593% of variance and factor 2 (Reputation) accounts for 26.835% of variance and together they explain for 56.428% variance. The identified factors with the associated variable and factor loadings are given in Table 6.

Table - 6
Identification of sponsor related factors in fund/scheme selection

| Factor Name | Variables | Factor Loadings |
|--------------------|--|------------------------|
| Infrastructure | B4 Agency Network | 0.806 |
| | B5 Research wing | 0.867 |
| | B6 Expertise in money management | 0.538 |
| Reputation | B1 Reputation of the sponsoring firm | 0.546 |
| | B2 Ability to offer a range of schemes | 0.722 |
| | B3 Brand name | 0.790 |

Influence of Investor Services on Selection of Fund/Scheme

The seven Investor Services related variables were analysed for their importance. The analysis reveals that the investors consider 6 out of 7 variables as important and consider C5 (Disclosure of schemes’ investment on every trading day) as somewhat important in the selection of fund/scheme. The weighted mean values of the variables and scale importance are given in Table 7.

Table - 7
Importance of Investor Service related factors in fund/scheme selection

| Sl. No. | Variable | WMV | Std. Dev. | Scale Importance |
|----------------|--|------------|------------------|-------------------------|
| C1 | Disclosure of investment objectives, methods and periodicity of valuation in advertisements | 4.16 | 0.81 | Important |
| C2 | Disclosure of the method and periodicity of the schemes sales and repurchases in the offer documents | 4.04 | 0.89 | Important |
| C3 | Disclosure of NAV on every trading day | 4.03 | 0.92 | Important |
| C4 | Disclosure of deviation of the investments from the original pattern | 3.96 | 0.94 | Important |
| C5 | Disclosure of scheme’s investments on every trading day | 3.35 | 1.11 | Somewhat Important |
| C6 | Mutual Fund Investors grievance redressal machinery | 4.12 | 0.87 | Important |
| C7 | Fringe Benefits like free insurance, free credit card, loans on collateral tax benefits etc. | 3.54 | 1.22 | Important |

Hence, to identify the investor services related factor, which influences the investor's fund selection, and to enable the AMCs to develop/maintain/improve the identified services, Factor Analysis was done using the Principal Component Analysis. Results of principal component analysis for investor services related factors are tabulated in Table 8.

Table – 8

Results of Principal Component Analysis (Investor Services)

Bartlett's Test of sphericity

Approximate chi-square =411.849; df=21; significance = 0.000

Kaiser-Meyer-Olkin Measure of Sampling Adequacy = 0.680

| Communalities | | | Initial Eigen Values | | | |
|----------------------|----------------|-------------------|-----------------------------|--------------------|----------------------|---------------------|
| Variable | Initial | Extraction | Factor | Eigen value | % of variance | Cumulative % |
| C1 | 1.000 | 0.754 | 1 | 2.466 | 35.226 | 35.226 |
| C2 | 1.000 | 0.755 | 2 | 1.108 | 15.826 | 51.052 |
| C3 | 1.000 | 0.674 | 3 | 1.022 | 14.604 | 65.656 |
| C4 | 1.000 | 0.613 | 4 | 0.893 | 12.752 | 78.408 |
| C5 | 1.000 | 0.713 | 5 | 0.635 | 9.071 | 87.479 |
| C6 | 1.000 | 0.391 | 6 | 0.443 | 6.332 | 93.811 |
| C7 | 1.000 | 0.697 | 7 | 0.433 | 6.189 | 100.00 |

| Factor | Extraction Sums of Squared Loadings | | | Rotation Sums of Squared Loadings | | |
|---------------|--|----------------------|---------------------|--|----------------------|---------------------|
| | Eigen Value | % of Variance | Cumulative % | Eigen Value | % of Variance | Cumulative % |
| 1 | 2.466 | 35.266 | 35.226 | 1.644 | 23.479 | 23.479 |
| 2 | 1.108 | 15.826 | 51.052 | 1.622 | 23.177 | 46.656 |
| 3 | 1.022 | 14.604 | 65.656 | 1.330 | 19.000 | 65.656 |

| Variable | Factor Matrix | | | Rotated Factor Matrix | | |
|-----------------|----------------------|-----------------|-----------------|------------------------------|-----------------|-----------------|
| | Factor 1 | Factor 2 | Factor 3 | Factor 1 | Factor 2 | Factor 3 |
| C1 | 0.631 | -0.568 | 0.180 | 0.123 | 0.858 | 4.353E-02 |
| C2 | 0.689 | -0.486 | 0.209 | 0.165 | 0.842 | 0.139 |
| C3 | 0.568 | 0.191 | -0.561 | 0.819 | 5.571E-02 | -2.173E-03 |
| C4 | 0.690 | -4.572E-02 | -0.366 | 0.694 | 0.360 | 3.337E-02 |
| C5 | 0.695 | 0.470 | -9.949E-02 | 0.657 | 5.784E-02 | 0.527 |
| C6 | 0.337 | 0.422 | 0.315 | 0.119 | -1.390E-02 | 0.614 |
| C7 | 0.444 | 0.334 | 0.623 | -5.310E-02 | 0.203 | 0.808 |

Retaining only variables with eigen values greater than 1, we can infer from Table 8 that, 35.226% of variance is explained by factor 1, while 15.826% of variance is explained by factor 2 and 14.604% of variance is explained by factor 3 and all three together explains 65.656% of variance.

A scrutiny of factor matrix reveals that factor loadings are very high in case of factor 1 (5 out of 7 variables have factor loadings >0.5). It shows that all variables are clubbed into one factor. But on the basis of theory, we can infer that there must be more than one factor. Therefore, Varimax rotation was done to obtain factors that can be named and interpreted.

On the basis of Varimax Rotation with Kaiser Normalisation, 3 factors have emerged. Each factor is constituted of all those variables that have factor loading greater than or equal to 0.5. Thus, C3, C4 and C5 constituted the first factor. The researcher conceptualised this factor as “Subsequent Disclosure”; C1 and C2 constituted the 2nd factor and this was conceptualized as “Preliminary Disclosure”; and C6 and C7 constituted the 3rd factor and was conceptualised as “Fringe Benefits”. C5 has a high correlation with factor1 (0.657) as well as Factor3 (0.527). Since it shows a higher relationship with factor1, it is clubbed with factor 1.

Thus, after rotation, factor 1 accounts for 23.479% of variance, factor 2 accounts for 23.117% of variance and factor 3 accounts for 19% of variance and together they account for 65.656% of variance. The identified factors with the associated variable and factor loadings are given in Table 9.

Table - 9

Identification of Service related factors in Fund/Scheme Selection

| <i>Factor Name</i> | | <i>Variables</i> | <i>Factor Loadings</i> |
|---------------------------|----|--|-------------------------------|
| Subsequent Disclosure | C3 | Daily disclosure of NAV | 0.819 |
| | C4 | Disclosure of Deviation of investment | 0.694 |
| | C5 | Daily disclosure of Investment | 0.657 |
| Preliminary Disclosure | C1 | Objective disclosure in advertisements | 0.858 |
| | C2 | Disclosure in offer documents | 0.842 |
| Fringe Benefits | C6 | Grievances Redressal Machinery | 0.614 |
| | C7 | Fringe Benefits | 0.808 |

Suggestions

- 1) The survey reveals that the investors are basically influenced by the intrinsic qualities of the product followed by efficient fund management

and general image of the fund/scheme in their selection of fund schemes. Hence, it is suggested that AMCs should design products consciously to meet the investors' needs and should be alert to capture the changing market moods and be innovative. Continuous product development and introduction of innovative products, is a must to attract and retain this market segment. Some suggestions are :

- a) Since insurance business has now become open, MFs can design products combining insurance and investment benefits to cater to the investor needs of safety and returns respectively. This will surely attract/retain low and moderate risk profile investors who often resist their desire to play directly in the capital market. (Note : Majority of the Indian middle income group population belong to this category). We have currently schemes like GIC MF and LIC MF which provide life and accident coverage. More such schemes can attract and expand this segment of investors.
- b) Retirement schemes similar to 401K plan, a popular MF product in US, will attract the middle income group which seeks regular income after retirement. AMFI has suggested a similar scheme and submitted its proposal to the Government in March 2001. Under the envisaged scheme, individuals can contribute on monthly or yearly basis to select MFs which in turn will invest them. On retirement of the individual his accumulated NAV will be converted into units of their monthly income scheme. The schemes will offer 3 options under which the accrued amount will be invested
 - i. Fully in government securities
 - ii. 50% in government securities, 30% in bonds of AAA rated companies, and 20% in equities.
 - iii. 40% in government bonds, 20% in AAA rated securities, 30% in equities and 10% in money market instruments.

A large chunk of retail investors will turn to this product on government's approval, for, their financial needs of safety, return, and liquidity are reasonably met by this product.

- c) Theme based schemes can attract specific groups. These funds generally differ among themselves in defining problems and pursuing investment goals. For example, Aquinas Fund of U.S. is a Social Responsibility Fund to promote catholic values. PAX World Fund is a diversified no load fund that invests in such industries as pollution control, health care, food, clothing, housing, education, energy and leisure activities. It does not invest in industries involving weapon production, nuclear power, tobacco, alcohol, abortion, pornography or casino gambling. Funds/schemes on similar lines addressing ethical, ecological, environmental or educational themes can be launched in

India too. Ethical funds can be a good option to someone who avoids the stock market entirely on philosophical objections and it is sure to capture/retain the retail investors with social/civic values (Note : India has quite a lot of such people).

- 2) It is further revealed that the investors are influenced by the infrastructural facilities of the sponsor and the reputation enjoyed by the sponsor, in their selection of the schemes. Hence, AMCs should take steps to develop their infrastructural facilities. Bank sponsored MFs and Public Sector MFs enjoy their already built-in branch networks. AMCs should note that investment in the development of, agency network, research and, introduction of technology in money management, will capture a segment of investors. Further, establishing a brand name and building up reputation and carefully maintaining the reputation by prudent public money management on the Gandhian principle of Trusteeship will also attract one segment of investors. Huge fund mobilization by Public Sector sponsored funds in the early 90s was purely due to their image and reputation factor. In Morgan Stanley case, it was the sponsor's reputation which attracted a serpentine line of investors. But unfortunately, these funds failed to recognise that their brand name and reputation was influential in the selection of funds/schemes by investors. They ignored to further build and maintain their goodwill, which ultimately resulted in loss of investors to them and loss of investment to investors. Days ahead will reveal the loss of investor accounts due to the July 2001 UTI scam.
- 3) Further, investors are influenced by the extent and quality of disclosure of information subsequent to their investment regarding disclosure of NAV, portfolio of investment and disclosure of deviation of investment from the stated objectives and the attached fringe benefits to the scheme in their selection of the scheme. Hence, AMCs should take steps to be as transparent as possible and follow the disclosure norms spelt out by SEBI and AMFI in this connection. UTI's unique place in the industry that allowed it to be non-transparent has led to the July 2001 UTI scam. The investors were kept in dark when its income schemes portfolio of debt to equity as 70:30 got slowly tilted to 20:80. We have to wait and see the impact of such non-disclosures on future fund mobilization by UTI.
- 4) The falling interest rates and a reasonably good performance of many growth schemes during the turn of the century might have been the reason for the high preference of Growth Schemes during the period under study. Now the scale is in favour of Income Schemes. So, it is suggested that AMCs should react in time to the changing market moods by launching new products or repositioning old ones. Deviation from the stated investment objectives without authority should be dealt seriously by the regulatory bodies. Safety of capital subject to market risk, should be assured to the MF investor.

- 5) Since the survey reveals priority to “Self decision in scheme selection. Information dissemination through all possible routes which will reach the investors should be tapped in a cost-effective manner by AMCs. Diagnostically looking, the fact that the investors prefer to make their own scheme selection decision, inspite of their lack of knowledge about the sophisticated market environment, reflects their reluctance to believe the available quality of service provided by the agents, financial consultants and investment advisers. These agencies and persons engaged in giving investment advice should gear up now to win the confidence of the investors. In the long run, it will help both the investors and the investment advisers, thus strengthening the link between the individual investors and the Mutual Funds.
- 6) In spite of having access to Internet, investors prefer “Personal Communication” mode to “Automated Service Mode”. This necessitates establishment of more manually operated service centers throughout the length and breadth of the country. (Note: The study was conducted in Urban and Semi-urban centers only. Hence, the choice of rural population can be guessed to be in favour of personal mode). When the nation is set for automation, the finding of the study is a little irksome!!

Conclusion

Running a successful MF requires complete understanding of the peculiarities of the Indian Stock Market and also the psyche of the small investor. This study has made an attempt to understand the financial behaviour of MF investors in connection with the scheme preference and selection. The post survey developments are likely to have an influence on the findings. Behavioural trends usually take time to stabilize and they get disturbed even by a slight change in any of the influencing variables. Hence, surveys similar to the present one need to be conducted at intervals to develop useful models. Nevertheless, it is hoped that the survey findings will have some useful managerial implication for the AMCs in their product designing and marketing.

Annex – Table 1
Area profile of Respondents

| Place | Number | Percentage |
|--------------|---------------|-------------------|
| Delhi | 50 | 14.3 |
| Madras | 56 | 16.0 |
| Bombay | 43 | 12.3 |
| Calcutta | 23 | 6.6 |
| Bangalore | 29 | 8.3 |
| Hyderabad | 40 | 11.4 |
| Coimbatore | 35 | 10.0 |
| Jamshedpur | 29 | 8.3 |
| Trichy | 20 | 5.7 |
| Anantapur | 25 | 7.1 |
| Total | 350 | 100 |

Annex – Table 2
Distribution of Retail Mutual Fund Present Investors by Demographic Factors

| Present Investor Particulars | Number of Respondents (Total =350) | Percentage (%) |
|-------------------------------------|---|-----------------------|
| Sex | | |
| Male | 276 | 78.85 |
| Female | 74 | 21.15 |
| Age | | |
| Below 30 | 61 | 17.43 |
| 31-40 | 88 | 25.43 |
| 41-50 | 105 | 30.28 |
| Above 50 | 96 | 26.86 |
| Academic qualification | | |
| School Final | 18 | 5.14 |
| Graduate | 142 | 40.57 |
| Post graduate | 64 | 18.29 |
| Professional | 126 | 36.00 |
| Marital Status | | |
| Married* | 301 | 86.00 |
| Unmarried | 49 | 14.00 |
| Occupation | | |
| Professional | 66 | 18.86 |
| Salaried | 202 | 57.71 |
| Business | 40 | 11.43 |
| Retired | 42 | 12.00 |
| Annual Income (in Rs.) | | |
| Less than 1,00,000 | 97 | 27.71 |
| 1,00,001-2,00,000 | 177 | 50.57 |
| 2,00,001-3,00,000 | 52 | 14.86 |
| Above 3,00,000 | 24 | 6.86 |
| Annual Savings (in Rs.) | | |
| Less than 50,000 | 226 | 64.57 |
| 50,001-100,000 | 109 | 31.14 |
| Above 1,00,000 | 15 | 4.23 |

*Includes 1 widow, 3widowers and 2 divorced.

Annex – Table 3
Profile of pilot study participants by demographic factors

| Profile particulars | Number of Respondents (Total =50) | Percentage (%) |
|--------------------------------|--|-----------------------|
| Sex | | |
| Male | 25 | 50 |
| Female | 25 | 50 |
| Age | | |
| Below 30 | 7 | 14 |
| 31-40 | 18 | 36 |
| 41-50 | 15 | 30 |
| Above 50 | 10 | 20 |
| Academic qualification | | |
| School Final | 6 | 12 |
| Graduate | 21 | 42 |
| Post graduate | 12 | 24 |
| Professional | 11 | 22 |
| Marital Status | | |
| Married | 29 | 58 |
| Unmarried | 21 | 42 |
| Occupation | | |
| Professional | 9 | 18 |
| Salaried | 25 | 50 |
| Business | 13 | 26 |
| Retired | 3 | 6 |
| Annual Income (in Rs.) | | |
| Less than 1,00,000 | 7 | 14 |
| 1,00,001-2,00,000 | 27 | 54 |
| 2,00,001-3,00,000 | 7 | 14 |
| Above 3,00,000 | 9 | 18 |
| Annual Savings (in Rs.) | | |
| Less than 50,000 | 26 | 52 |
| 50,001-100,000 | 19 | 38 |
| Above 1,00,000 | 5 | 10 |

Annex – Table 4
Savings avenue Preference among Respondents

| Savings Avenue | WMV | Rank |
|-----------------------|-------------|-------------|
| Currency | 2.78 | VII |
| Bank Deposit | 6.19 | I |
| Life Insurance | 5.55 | III |
| Pension and PF | 5.58 | II |
| Shares and Debentures | 4.14 | VI |
| Units of UTI & MFs | 5.13 | IV |
| Postal Savings | 4.40 | V |
| Chits | 2.24 | VIII |

Annex – Table 5
Scheme Preference among Mutual Fund Investors

| Scheme | WMV | Rank |
|---------------|-------------|-------------|
| Growth | 2.16 | I |
| Income | 2.07 | II |
| Balanced | 1.76 | III |

Annex – Table 6
Mutual Fund Investment Objective among Present Investors

| Objectives | Weighted Mean Value | Rank |
|----------------------|----------------------------|-------------|
| Safety | 3.43 | I |
| Liquidity | 2.74 | IV |
| Tax Benefit | 3.15 | III |
| Good Return | 3.31 | II |
| Capital Appreciation | 2.37 | V |

Annex – Table 7
Preferable Route to Mutual Fund Investing

| Route | WMV | Rank |
|----------------------|-------------|-------------|
| Friend's suggestion | 3.03 | V |
| Newspapers/Magazines | 4.41 | II |
| Self Decision | 4.80 | I |
| Television | 3.13 | IV |
| Brokers/Agents | 3.53 | III |
| Mail | 2.10 | VI |

Note :

- a. 154 (44%) get to know more about MFs through Internet
- b. 196 (56%) do not have access to Internet

Annex – Table 8
Importance of Factors in Mutual Fund/Scheme Selection

| Sl. No. | Factors | Weighted Mean Value | Scale Importance |
|----------------|------------------------|----------------------------|-------------------------|
| 1. | Scheme Qualities | 4.55 | Highly Important |
| 2. | Fund Sponsor Qualities | 4.20 | Important |
| 3. | Investor Services | 4.38 | Important |

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