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PROBLEMS AND PERSPECTIVES IN DEVELOPMENT OF MUTUAL FUNDS IN THE REPUBLIC OF KAZAKHSTAN

Today, Kazakhstan has an acute problem of investment support diversification in the process of economic development. An important resource for investment is savings, not all of which are transformed into investment. This occurs, for example, if the excess revenue is invested in cash of national or foreign currency. In this case it does not enter to the capital market, it is withdrawn from circulation, which can lead to investment scarcity, reduce the aggregate demand and reveal to "the paradox of thrift", where the reduction in propensity consume and decreases gross domestic product.

Consequently, financial support of successful economic development requires well-functioning mechanism for transforming savings into investments. Stock market allows direct movement of capital between its owners and those who need it, without intermediaries in the form of credit institutions. However, the work requires from the investor a certain level of competence and time spent on preparation and decision making.

The complexity of investment decisions in the stock market, on one hand, its potential attractiveness to investors, on the other hand, creates conditions for delegating investment decisions to professionals within the trust management. If the investor owns the large-scale resources, it can sign an individual contract with the manager of the investment fund. To attract the mass market investors it creates collective investment funds - mutual funds.

Mutual fund industry in Kazakhstan has a relatively recent history. With the adoption of July 7, 2004 the law about "About Investment Funds' investors were able to invest their capital, not only in bank deposits, where the interest rates are falling, as well as real estate, government securities, the interest on which is not above inflation, corporate bonds, where access has only professional players but also in mutual funds, rates of return are more attractive. That is the law laid the foundation for the creation of new financial institutions in Kazakhstan.

Since 2004, the Government of the Republic of Kazakhstan has consistently pursued a policy directed into intensification of investment activity in the country. This policy comes from the fact that economic recovery requires the inflow of private investors. Increasing investment activity of the population depends largely on the results formed from the current institutional environment for investment, involving the introduction of effective forms of organization of the investment process, including the establishment of mutual funds. Mutual funds are so-called "collective investment schemes" by which means, consciously and purposefully invested by investors in certain funds, accumulate in a single pool managed by the professional manager with a view to a profitable future investments. Investment Funds as an organization of collective investments in securities are particularly important in countries where there are a lot of small investors. This fully applies to Kazakhstan. Studying the experience of countries where various forms of collective investment have demonstrated their advantages, one can make some conclusions. First of all, in the development of collective investments in Kazakhstan wins the whole population because with their help increase flows of investment into the economy that will create conditions for economic growth. Grow up tax revenues, which mean - to improve the financing of social programs and budgetary organizations. Increases the demand for government securities, while reducing the borrowing cost. Additionally, expand citizens' ability to maintain and increase their savings, which in itself is capable of protecting their interests and enhance the credibility of the market economy. The economic development of the country would benefit and increase competition between collective investment and commercial banks for the money of population - financial resources will be available to businesses.

Mutual fund market is by far one of the most profitable ways of collective investment for the following reasons:

- availability of special tax regime (in particular, the ongoing operations of the Fund is not taxable, the investor paid tax only on the sale of the unit);
- reliable infrastructure of the fund, supported by cross-checking of the set of its participants;
- diversification of investment risks;
- professional management;
- the liquidity of investments.

At the discretion of the investor can choose fund with most preferred operating structure (open-end, closed-end and interval) in the direction of investment (shares mutual fund, bonds mutual fund, mixed investment mutual fund, etc.).

Mutual fund is a trust that pools money from a group of investors (sharing common financial goals) and invest the money thus collected into asset classes that match the stated investment objectives of the scheme. Since the stated investment objectives of a mutual fund scheme generally form the basis for an investor's decision to contribute money to the pool, a mutual fund can not deviate from its stated objectives at any point of time.

Every Mutual Fund is managed by a fund manager, who is using his investment management skills and necessary research works and ensures a much better return than what an investor can manage on his own. The capital appreciation and other incomes earned from these investments are passed on to the investors (also known as unit holders) in proportion of the number of units they own.

Mutual funds are portfolios that have lower risks than other unhedged portfolios solely because mutual funds put a lot of analysis onto their stock picks and come up with options that negate or reduce each others negative attributes. For people who are new to the stock markets or do not know the working process and the analysis that goes behind stock picks in a portfolio, mutual funds offer all this expertise through their services.

As mentioned above, fees can be a serious impediment to mutual funds. In fact, some of the costliest funds may charge 4-5% per year in fees. Any fund that charges high fees will undoubtedly claim that it does so in an effort to provide superior management. While this may occasionally be true, it is rarely the case. Studies have shown that in the long run, most mutual funds underperform the overall market by exactly the same amount they charge in fees. With this in mind, we suggest finding funds with low expense ratios and no front- or back-end loads. A fund that charges 2% per year will cost you $200 for every $10,000 that you have invested. Unless the fund can outperform the market by 2%, you will have unwisely paid the manager extra money when you could have put that same money into your own portfolio. Index funds generally provide the overall lowest costs because they do not actively manage their holdings (this lowers managerial and transaction costs). These are often referred to as “passively-managed” funds because they simply track a predetermined index such as the S&P 500, Dow Jones Industrials, or the Nasdaq Composite.[1]

Mutual funds also require well-developed security markets with a high level of market integrity and liquidity. Market integrity implies that insiders are barred from taking advantage of privileged information, while large shareholders and market intermediaries are prevented from engaging in market manipulation. Market integrity also requires that officers of listed corporations observe high standards of corporate governance and honesty and do not engage in extensive fraud and theft. Market liquidity ensures that transaction costs are low and investors do not suffer from large adverse price movements when they initiate transactions in individual securities.

Like many investments, mutual funds offer advantages and disadvantages, which are important to consider and understand before decision to buy is made. Here we explore some of the drawbacks of mutual funds.

1) Fluctuating Returns. Mutual funds are like many other investments without a guaranteed return: there is always a possibility that the value of your mutual fund will depreciate. Unlike fixed-income products, such as bonds and Treasury bills, mutual funds experience price fluctuations along with the stocks that make up the fund. When deciding on a particular fund to buy, you need to research the risks involved - just because a professional manager is looking after the fund, that does not mean that the performance will be stellar.

2) Overdiversification. Although diversification is one of the keys to successful investing, many mutual fund investors tend to overdiversify. The idea of diversification is to reduce the risks associated with holding a single security; overdiversification (also known as divorsification) occurs when investors acquire many funds that are highly related and, as a result, don not get the risk reducing benefits of diversification.

At the other extreme, just because we own mutual funds does not mean that we are automatically diversified. For example, a fund that invests only in a particular industry or region is still relatively risky.[2]

3) Cash, Cash and More Cash. As known, mutual funds pool money from thousands of investors, so everyday investors are putting money into the fund as well as withdrawing investments. To maintain liquidity and the capacity to accommodate withdrawals, funds typically have to keep a large portion of their portfolios as cash.

Having ample cash is great for liquidity but money sitting around as cash is not working for you and thus, is not very advantageous.

4) Costs. Mutual funds provide investors with professional management but it comes at a cost. Funds will typically have a range of different fees that reduce the overall payout. In mutual funds, the fees are classified into two categories: shareholder fees and annual operating fees.

5) Misleading Advertisements. The misleading advertisements of different funds can guide investors down the wrong path. Some funds may be incorrectly labeled as growth funds, while others are classified as small cap or income funds.

6) Evaluating Funds. Another disadvantage of mutual funds is the difficulty they pose for investors interested in researching and evaluating the different funds. Unlike stocks, mutual funds do not offer investors the opportunity to compare the P/E ratio, sales growth, earnings per share, etc. A mutual fund's net asset value gives investors the total value of the fund's portfolio less liabilities.

Global financial crisis has demonstrated the shortcomings of existing models of financial relations as globally, and at the national level. Weaknesses were identified in the structure of state regulation and in the activities of financial institutions themselves. The problems of financial institutions emerged in the imperfections and inconsistencies of risk management systems with modern trends and level of exposure (both in extent and quality of risk), low levels of corporate governance, lack of transparency and, consequently, ineffective business models that appeared to be sensitive to negative trends.

One of the distinguishing features of post-crisis period is the need to address the identified problems of the financial sector, correcting errors and ensuring a stable diversified growth. Further work is needed to create a modern, stable and competitive financial system of sovereign Kazakhstan.[3]

Another four or five years ago, mutual funds were at the peak of their popularity. With their help, buying shares of mutual funds, private investors, which is not always experienced in the intricacies of the financial market, could invest in new tools for themselves - stocks and bonds, yield goes off scale for 30-40%.

But after the world economic crisis has began, it has changed everything. The risks have increased, the yield fell. Currently, Kazakhstan is experiencing a large outflow of shareholders, which can not positively characterize the state of the market of collective investments. In the years since the adoption of the law “About Investment funds” mutual fund industry grew rapidly, helped by strong market growth, increasing needs of our fellow citizens in the new investment tools and the emerging positive attitude related to the stock market.

Most low level of confidence of respondents in relation to the activities of the stock market, and mutual funds (less than 10%). Greatest interest to financial institutions and instruments shows the population aged 18-24 years, the population with incomes of more than 90,000 tenge per month for all family members. Information about mutual funds and Stock Exchange's most interesting for people with incomplete higher education and higher education.

According to this data, suggests several conclusions:

- There is a direct correlation between the average monthly household income and an indicator of financial literacy: the higher the income, the higher the total combined score of respondent.
- Direct relationship between the level of awareness about financial instruments and the level of confidence in financial institutions.
- The most promising target audience of financial products is a population with an income of more than 70,000 tenge per month.

Another problem is a tendency of private investors to short-term investments. Meanwhile, when investing in mutual funds, this approach would be unjustifiable. At its core mutual funds are a mechanism for long-term investment and are oriented by a fundamental component of securities value. Investments in mutual funds are typically investments, carried out not for a year or two, but for a longer period. Only long-term investments can ignore the speculative game, short-term decline and even stagnation of the market.

Funds are limited in their investment opportunities in the tools market in Kazakhstan, which significantly narrows the range of funds. In addition, the divergent outcomes of mutual funds over the past year have reduced interest in such way of income. Unfortunately, when we invest our investments is mainly oriented to the possibility of obtaining high yield, which should not be forgotten, is directly linked to high risks.

And, of course, there are a number of problems in funds, which does not allow mutual funds to develop fully. Among the key factors is a lack of reliable investment tools and high market volatility, which does not allow to fully implement the investment strategy of funds. The local stock market is sufficiently active and liquid, it narrows a range of available securities for investment. Among other things, include imperfect accounting techniques for financial instruments in the fund's assets, a low budget campaigns to promote mutual funds and high cost of the fund's presence in the regions. The above and other emerging problems, Asset management companies are trying to solve in their own way.

The composition and operation of stock market participants largely determine its current state and then, in what direction it will develop further. Consideration of institutional investors in terms of efficient market hypothesis, the definition of their role in the development of security markets is one of the most pressing questions for the establishment of the domestic financial system. Based on the basic provisions of the hypothesis of market efficiency can be expected that more actively traded market participants in the market, the higher the efficiency of the market.

Looking at the history of the formation of institutional investors, we can distinguish several directions, through which their presence may improve the development of financial markets in general and the stock market in particular.

One of them is in strengthening competition in financial markets. The development of new sources of funding, whether from the presence of foreign banks, opening access to foreign markets or on the growth of institutional and other non-bank financial intermediaries, makes the market-dominating commercial banks to become more competitive and start to value for their clients. This increase in competition provides more services of better quality. Increasing the number of market participants and increased competition in the financial market will be expressed and to enhance the investment in the stock market.

Institutional investors with sufficient means who analyze and carry out active trading market, will use the slightest opportunity for getting profit, thus, increase the efficiency of the market. In addition, the development of institutional investors can reduce the costs of security tradings.

The activity of institutional investors makes a positive impact on market liquidity. Primarily this is directly connected with increasing in the volume of trading on the market due to the presence of institutional investors.

Further development of the mutual funds industry in our country are related primarily to address the challenges currently facing the industry, which had been considered earlier. In addition, the prospects of mutual funds will directly depend on the results of economic development of Kazakhstan in the coming years from fiscal, economic, financial, social and foreign policy of the state and regulatory authorities the stock market.

As international experience shows, the tendency to preserve and enhance the profitability of their savings becomes especially relevant in times of economic and financial instability. Storage savings at home, in addition to unsafe and not produce any income, under the impact of inflation reduces their value. So investors, for the most part, try to make active use of reliable and affordable ways to invest their savings. At the same time, in our market available to the general public are very few tools. Traditionally, Kazakhs keep their money in bank deposits. Real Estate for the individual investor in the recent past has become attractive but now as a way of investing has not become of interest. Voluntary pension contributions, too, did not become an important component of savings for oldness. Securities, including mutual funds, today still can not be attributed to the highly used tools.

By the time the market of mutual funds will be a phase of consolidation, only the strongest survived Assets management companies can provide investors with the most interesting investment strategy in mutual funds. In addition, mutual fund, as a tool for a long-term investment for any investor can serve as the means of saving for oldness and education of children. Increasing consumer power of the population and the growth of the stock market, coupled to provoke interest to the stock market and accordingly to different types of investments, including mutual funds.

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