

## **CHAPTER I**

### **INTRODUCTION**

#### **Introduction to Unit Trusts**

There has been rapid development and launching of numerous unit trust funds in Malaysia during the last few years. One might then ask : "What is a Unit Trust ?"

A unit trust is an open ended mutual fund which pools the financial resources of numerous investors and invest the monies thus received in the stock market such as the Kuala Lumpur Stock Exchange (KLSE) or other permitted investment instruments.

Investors buy units from the managers (management companies) of the fund at what is known as the offer price and can choose to sell them back later to the managers at the bid price. These prices are published daily in our local newspapers. The offer and bid prices are calculated daily based on the current underlying value of the portfolio held by the investment managers. The method of calculating the bid and offer prices is stated in the trust deed of the fund. The offer price is always slightly above the bid price due to the various expenses and charges levied by the management company.

The unique feature of the unit trust is that it establishes a tripartite relationship between three parties namely the investors (unit holders), the investment manager (management company) and the trustee. This unique relationship is governed by the trust deed which spells out the rights, duties and responsibilities of each party. The investors may be individuals, companies or institutions which invest funds in the trust with the hope of generating attractive returns in the form of dividends, interest income and capital gains. Once money is invested in the trust, investors are given certificates

stating the number of units owned which represent their ownership in the assets held in trust by the trustee. The investment manager is usually a public company which is responsible for the daily investment operation. It is responsible for administering the trust, managing the portfolio of investment and maintaining a market for the units. The trustee is an institution which acts as the custodian of the assets of the unit trusts. Most of the trustees are affiliated to major banks or insurance companies. It grants approval for the purchase of securities and hold the securities purchased. In general, the trustees are not responsible for the choice of investments. This task is given to the investment manager. The trustee monitors the investment manager, maintains a register of unit holders and ensures that all terms of the trust deed are strictly adhered to. With the appointment of the independent trustee, the interest of the unit holders are safe guarded against mismanagement by the investment manager.

The managers generally specify the investment objectives of the unit trust in the trust deeds, annual fund reports and prospectuses. The purpose of disclosing the objective of the fund is to enable investors to choose among different types of funds that they are most comfortable with viz risk and return. This subject will be discussed in greater detail in Chapter III.

A unit trust fund offers investors a number of attractive features, some of which are described below.

Investment in unit trust is possible with a small capital outlay and is thus affordable and flexible.

As investors do not have sufficient financial resources to invest in a well diversified portfolio of stocks in the share market in order to diversify the risk to the market risk (undiversifiable or systematic risk) level, unit trust provide a good investment alternative for investors to earn attractive returns and at the same time enjoy the security of capital.

Unit trusts are managed by professional fund managers who devote their full time to maximise the wealth of the unit holders. These managers are experienced, knowledgeable and they possess the necessary expertise to invest and monitor the performance of the trusts' portfolios. With time and expertise to their advantage, investment managers are in a far more better position to take advantage of opportunities than individual investors.

The investment manager is obligated to repurchase units at the published bid prices. Hence unit trusts are readily marketable and quite liquid.

Investors in unit trusts are spared from the administrative chores associated with holding securities such as rights and bonus issues, collection of dividends, share scripts, etc. In addition, investors do not have to spend countless hours researching and evaluating securities to ascertain whether they are optimising their financial resources. These tasks are delegated to the investment managers of the unit trusts.

Investment managers are able to generate higher returns because of their knowledge of various stock markets which an average investor do not possess. Hence they are able to employ the financial resources more efficiently. The benefits of the above will ultimately accrue to the unitholders.

In Malaysia, the regulation of unit trust schemes has now been vested in the Securities Commission (SC) by Parliament via the Securities Commission Act 1993. The SC has issued a set of comprehensive guidelines on unit trust funds dated 10th March 1994 for all those intending to set up unit trust companies and for those managing unit trust funds. These guideline supersedes all previous informal guidelines pertaining to unit trust schemes. The cooperation between the Registrar of Companies (ROC) and the SC is evident in the guideline as all the applications involving unit trusts are channeled to the SC, even those that require the approval of the ROC as required under the Companies Act 1965. The SC acts as the main secretariat for all approvals relating to unit trusts and in this manner makes it convenient for industry practitioners.

### **Purpose of the Study**

The main purpose of this study are :

1. To evaluate the historical performance of a sample of unit trust funds in Malaysia and to rank their performance.
2. To evaluate the degree of risk diversification of the sample of unit trust funds

3. To evaluate the consistency of the investment performance of the unit trusts with time.
4. To evaluate the stability of the unit trusts' systematic risks with time.
5. To determine if unit trust funds in Malaysia adhere to their stated objectives.
6. To determine if the investment managers have the ability to predict security prices.
7. To determine if the fund characteristics such as age, size of fund, expense ratio and portfolio turnover influences the investment performance and the systematic risks of the unit trust funds.

### **Sources of Data**

The secondary data to be used in this study are derived from the sources listed below :

1. Price records of the various unit trust funds obtained from the management companies and newspapers
2. Annual reports of the various funds
3. Investors Digest published by the KLSE

### **Scope of the Study**

As of June 1994, there is a total of twenty five management companies managing a total of fifty seven funds (inclusive of both public and bumiputra funds).

Appendix A provides the list of the management companies and the funds that they manage.

The total net asset value of the unit trust funds as at 30th June 1994 stood at RM 31 Billion. Out of which RM27.9 Billion is accounted for by Amanah Saham Nasional and Amanah Saham Bumiputra. The rest of the unit trust funds account for the balance.

The Malaysian unit trust industry is still at its infancy and is quite small and account for only 6.5% of the market capitalisation of the KLSE as at 30th June 1994.

This study covers a ten year period from January 1984 to December 1993. This ten year period is chosen so that it is sufficiently long to cover the various bull and bear market in the Malaysian capital market and would therefore provide better insight into the performance of the unit trust funds. For this study, a sample of twenty one unit trust funds taken from three management companies are taken. This is shown in Table 1.1 below. The main reason for the choice of these three management companies is that these companies are the pioneers in the unit trust industry and that data can be obtained readily. The other funds are relatively new and most of them are less than ten years old.

### **Limitations of the Study**

The sample of twenty one unit trust funds used have been drawn from three management companies. Thirteen of those funds are bumiputra funds while the remaining eight funds are public funds. As the sample is rather confined in this respect, it would be inappropriate to draw any general conclusions on the performance of the unit trust industry as a whole since the performance of the funds could be considerably influenced by the management companies' policies especially those of the bumiputra funds.

Furthermore data is lacking on those concerning the fund characteristics for the time period prior to 1990. Hence the study on the impact of fund characteristics on the investment performance and the systematic risks of the funds was performed only

for the period 1990 to 1993. In addition to this, data was only available for the public funds. Hence the effects of fund characteristics cannot be too generalised.

**Table 1.1 : List of Unit Trust Funds in the Sample**

<b>Fund Identification (ID) Number</b>	<b>Name of Fund</b>
1	Kumpulan Modal Bumiputra yang Pertama
2	Kumpulan Modal Bumiputra yang Kedua
3	Kumpulan Modal Bumiputra yang Ketiga
4	Kumpulan Modal Bumiputra yang Keempat
5	Kumpulan Modal Bumiputra yang Kelima
6	Kumpulan Modal Bumiputra yang Keenam
7	Kumpulan Modal Bumiputra yang Ketujuh (Perolchan)
8	Kumpulan Modal Bumiputra yang Ketujuh (Pertambahan)
9	Kumpulan Modal Bumiputra yang Kelapan
10	Kumpulan Modal Bumiputra yang Kesembilan
11	Kumpulan Modal Bumiputra yang Kesepuluh
12	Kumpulan Modal Bumiputra yang Kesebelas
13	Kumpulan Bumiputra Pelaburan Perwira
14	Malaysian Investment Fund
15	Malaysia Progress Fund
16	Tabung Amanah Bakti (Malaysia Security Fund)
17	Malaysia Berjaya Fund
18	Malaysia Equity Fund
19	Malaysia Commerce Fund
20	Kuala Lumpur Savings Fund
21	Kuala Lumpur Growth Fund

## **Organisation of the Report**

This report consists of five chapters. Chapter I provides a brief introduction to the unit trust funds in Malaysia, the purpose, sources of the data, scope and limitations of the study.

Chapter II highlights some studies done in the mutual fund industry in the West specifically the United States and the United Kingdom and the unit trust industry in Singapore and Malaysia. Empirical findings and method of analysis of such studies are presented as well.

In Chapter III, the methodology of the study is presented. In this chapter the various methods, formulae and tools of analysis used in the study are described and explained.

Chapter IV provides a concise summary of the empirical findings with regards to the investment performance of the unit trust funds and how well they performed when compared to the market. In addition to this, the sample funds' risks characteristics and diversification, how well the various types of funds performed and whether they adhere to their stated objectives are presented. The consistency of their performance and the stability of their systematic risks over time, the forecasting ability of investment managers and the impact of the funds' characteristics on the investment performance and their systematic risks are presented as well.

Chapter V summarises the research findings and attempts to draw some conclusion and implications from the study. In the final section, suggestions for future studies in the area are highlighted.