

THE ROLE AND IMPORTANCE OF INVESTMENT FUNDS IN DEVELOPING OF SERBIAN FINANCIAL MARKET

ULOGA I VAŽNOST INVESTICIJSKIH FONDOVA U RAZVOJU SRPSKOG FINANCIJSKOG TRŽIŠTA

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Abstract: *Investment funds are nonbanking financial institutions that collect savings of individual investors and place collected capital on the financial market. There are a lot of benefits that investment funds provide: professional management, diversification, simple (re)investing. Investment funds are new institutional investors on the Serbian financial market. Their important role is to increase number of financial intermediaries on the market and to cumulate a lot of other positive financial effects. If funds make possible rate returns above the interest rates for the deposits in the banks, it will be the best way to proof their appearance on the Serbian financial market.*

Key words: *Investment funds, Emerging financial markets, Institutional investors, Capital markets*

Sažetak: *Investicijski fondovi su nebankarske finansijske institucije koje prikupljaju uštedevine individualnih ulagača i plasiraju taj kapital na finansijsko tržište. Investicijski fondovi omogućuju brojne pogodnosti: profesionalno upravljanje, diversifikaciju, jednostavno ulaganje. Investicijski fondovi su novi institucijski ulagači na srpskom finansijskom tržištu. Važna im je uloga povećati broj finansijskih posrednika na tržištu i ostvariti brojne druge pozitivne finansijske učinke. Ukoliko fondovi ostvare stope prinosa veće od kamatnih stopa na depozite u bankama to će biti najbolji dokaz za opravdanost njihovog pojavljivanja na srpskom finansijskom tržištu.*

Ključne riječi: *investicijski fondovi, otvaranje finansijskih tržišta, institucionalni ulagači, tržište kapitala*



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1. Introduction

Investment funds are non banking financial institutions, that collect savings of individual investors and place collected capital on the financial market. So, investors become co owners of the investment fund portfolio. Investment funds (usually mutual funds) are the most appropriate form of the capital mobilisation. They appeared later in the comparison with the commercial banks, but when we consider them like financial institutions, they contributed a lot to the capital market deepening and developing.

There are a lot of benefits that investment funds supply:

1. Professional management - professionals manage portfolio better than anyone individual investor, even after detailed market analyse
2. Diversification - means that in the investment fund's portfolio are securities issued by companies from different industries and companies, in order to decrease risk; in case that some companies do business badly, there are no huge consequences on the whole portfolio
3. Simple (re)investing - means that there is no minimum amount of investment, than there is possibility to buy additionally new shares, even if investor doesn't have bigger amount of money; there is also possibility for automatic dividend reinvestment, so as withdrawal plans.

Phenomenon of investment funds is so spread, so their assets across the world is more than 20 trillions \$. Almost half of total funds number are equity funds, bond funds and money market funds. They are equally represented, and the rest are balanced and other fund types. More than a half funds are from USA, one third is from Europe, and others are from Asia. Great results are also realised in the former socialistic European countries, where funds exist about 10 to 15 years, and their assets is nearly a dozen billions \$ worth, number of funds is almost hundred, and great number of citizens in these countries are shareholders in funds.

Objectives of this paper is to explain how investment funds, as a new financial intermediaries on the Serbian financial market, can accelerate development of the mentioned market, through presenting performances and results of investment funds on the developed financial markets.

2. Establishing mutual Funds in Serbia

During the nineties method of mass voucher privatization (MVP) was applied in almost all former socialistic Central and East European countries, as a model for privatization of state enterprises. Model was implemented in Czechoslovakia, Poland, Hungary, Soviet Union, Romania, Bulgaria and almost in all former Yugoslav Republics. Serbia is the only country in that region, that had not implemented MVP method. There is still a question why in Serbia are applied other methods for privatization state property, and would MVP method give more justified effects of privatization, regarding inclusion of citizens majority.

There was no commitment of checking out capital roots, that was used in buying a lot of domestic enterprises. A few years ago, some Serbian enterprises, that have great potential, but they were in financial and management difficulties, were very interesting for foreign venture funds, and some of these enterprises were bought. So lack of law regulative caused appearance of venture funds, before appearance of mutual funds.

3. Law regulative

After a decade of being late, in comparison with countries in the region, in Serbia, in December 2006., was implemented Investment funds law. This law allows three funds types on the Serbian financial market: open-end funds (that are being organized), closed-end funds (that are being founded) and private funds. For open-end and closed-end funds minimal money amount of capital is 200.000 € (in dinar's counter value), and 50.000 € for capital of private funds. Fund's capital can be invested in equities and debt securities issued by government and its institutions, domestic and foreign companies, and it's important that those securities are being traded on organized markets in the country and abroad. Fund can invest in money deposits, financial derivatives and real estates. Limits of investing in some types of securities issued by one business, government or institutions are strictly defined, so as costs and incomes of fund, managing the fund, commitment of publishing prospect and minimum of its information's content and all other question important for investment funds' business.

4. Problems and recommendation for investment funds on the Serbian financial market

In February 2007, the first investment fund was founded, and it was balanced fund. After fifteen months of funds existing on the Serbian financial market, there are nine open-end (mutual) funds, usually balanced funds and fund with investment aim to raise assets value. For a less than a year shares of some funds were for 30 or 40 % higher in comparison with their price at opening. Closed-end funds collect capital by selling shares through open call. There are also two funds on the Serbian financial market announced as a closed-end funds, that have got permission from the Security and Exchange Commission of Serbia. One of these funds will invest mostly in the SMEs with market capitalisation below 40 millions €, with the great growth potential. However, from the moment of declaring new parliamentary elections in Serbia, stock exchange indexes decrease constantly, so as value of funds shares. After the elections, shares of only three funds are above their value at opening, so the residual funds have negative yield. In such conditions, it's hard to attract new potential investors and to motivate them to invest in mutual funds, as a new financial intermediaries on the Serbian financial market. Nevertheless, investors should be aware that only on the long run, at least 3 to 5 years, higher yields can be achieved. Investment funds are not recommended for short term investment and investors should not expect yields above the average on a short run. Serbian financial market is

very „shallow“, i.e. there is no adequate supply of financial instruments, in which investment funds and other institutional investors could invest. Quality of securities supply could be dramatically improved when public utilities companies, would be listed on the stock exchange, because their shares are „blue chips“ . At the moment, there is a small number of companies that are attractive for investment funds. Possible scenario of that situation could be collecting capital on domestic financial market and place it on the capital markets abroad. That result would not be useful for development of domestic economy, regarding investment funds as a very important long term financial source of companies. Especially should be accented interest of investment funds for SMEs, that momentarily access to long term (banking) financial sources at the high price. It's needed to find common interest for fund management and for company management too, and that is above all - profit. At the beginning government has huge responsibility, but domestic companies and their management, too. They should attract domestic and foreign investment funds, by remarkable results and continuous profitable doing business.

In order to rise quantity and quality of financial instruments on the capital market, it would be very useful when municipalities, cities or government and its institutions would issue low risk bonds, well known as municipal bonds or „muni's“. It could be excellent way to decrease dependence of all above mentioned institutions from the common financial sources, like budget or bank loans are. It is strongly recommended for Serbian institutions, when we consider constant budget deficit and long term bank loans with high interest rates (because of different expressed risks).

In order to develop capital market, and to increase quality and quantity of securities supply and demand, it's necessary to rise corporate managing on the higher level. Transparency in business doesn't mean only obligatory publishing of financial statement. That means constant informing all present and future company shareholders about all happenings relevant for company and its business. Medium and big enterprises have law obligation for auditing of financial statements. Majority of activities important for corporate managing are also conditions for presence of some company on the A list on the Belgrade stock exchange. At the end of May, 2008 only three domestic companies are on that list.

It's also very important role of the portfolio manager and investment adviser. In the first period of investment funds on the Serbian financial market, there were only few portfolio manager. One of the reasons is very difficult passing exams for that licence. Now, situation is better, we have more licenced portfolio managers and it's very good paid, but also very responsible occupation. Usually stock exchange dealers and brokers decide for this challenge occupation.

For investor it is important to choose investment fund, toward own perception return and risk tolerance. As more diversified and deeper financial market is, as more possibilities for new different funds will be. Small investors that can invest only few thousands euro in shares, usually can not buy a lot of different shares, so for them diversification through the fund is very important. By investing in particular fund small investor participate in whole fund portfolio, that could consists of dozens and hundreds different shares. It is more secure for them, because they have equal rights with other fund investors, they confide their capital to the professionals that have

needed knowledge and experience, and what is the most important, they have relevant and the right time information about financial market trends.

5. Conclusion

Investment funds are new institutional investors on the Serbian financial market. Their important role is to increase number of financial intermediaries on the market and to accumulate a lot of other positive effects, from the point of capital owners, but also from the point of the whole society. However, time is necessary factor for fulfilling expectations and trust of small number of brave, curious, but solid informed and educated investors, that have confided their capital to the investment funds. If funds make possible rate returns above the interest rates for the deposits in the banks, it will be the best way to proof their appearance on the Serbian financial market. Possibility for bigger earning, with acceptable risk for investors, is certainly right instrument to attract new investors and their capital to the funds. If law regulative from this field would be respected, so as fund policy, positive results of funds' business on the Serbian financial market will be soon obvious and that would be the best instrument for funds promotion. On the financial markets in the region, investment funds operate longer that one decade and they have marked yearly return rates between 20 and 30 %. But it's very important to say that capital is very sensitive category and every change and uncertainty in the social-political situation in the country or region, at the moment reflects on the stock exchange indexes, investment fund shares, i.e. their returns.

6. References

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