

An Analysis of the Factors Determining Investors' Decisions on Mutual Funds

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Abstract

An investment refers to an item or asset purchased with the expectation of generating income or increasing in value over time. Appreciation occurs when the value of the asset rises. The survey is based on a convenience sample of 431 respondents chosen to better understand individual investors' mutual fund purchasing habits. The article describes the many attributes that investors deem vital while investing in mutual funds. The two most important underlying factors extracted are the fund's credibility and its miscellaneous traits. The link between these characteristics and demographic variables is determined. The essay makes recommendations for mutual fund companies and suggests areas for future investigation.

Keywords: Mutual Funds, Investors, Decisions etc.

1. Introduction

A country's economic development is heavily reliant on its financial markets. They facilitate the allocation of scarce resources by shifting them from savers to borrowers, hence increasing economic investment activity. Mutual funds are one of the most popular financial investments because they pool the money of a large number of investors who have a same financial aim and trust each other. The funds raised are invested in capital market instruments such as shares, debentures, and other securities. Investors receive the number of units based on their investment and the net asset value of the units. The money earned is distributed in proportion to the number of units held by the investors. A mutual fund is an investment that meets the demands of the average person. It is an indirect form of capital market investment that offers diversity, skilled management, low-cost investment, liquidity, and tax advantages. The fundamental goal is to give greater returns to investors while limiting the risks associated with capital markets. The most prevalent aspect of mutual fund units is their low cost. The Unit Trust of India (UTI) introduced the first mutual fund in India in the mid-1960s, and mutual funds have evolved significantly as an investment choice since then.

2. History of Mutual Funds in India

A strong financial market with broad participation is essential for a developed economy. With this broad objective India's first mutual fund was establishment in 1963, namely, Unit Trust of India (UTI), at the initiative of the Government of India and Reserve Bank of India 'with a view to encouraging saving and investment and participation in the income, profits and gains accruing to the Corporation from the acquisition, holding, management and disposal of securities'.

In the last few years the MF Industry has grown significantly. The history of Mutual Funds in India can be broadly divided into five distinct phases given in Table 1:

Table – 1 history of Mutual Funds in India

Phases	Evaluation
First Phase 1964 - 1987	The mutual fund sector in India began in 1963 with the foundation of UTI by an Act of Parliament, and it operated under the regulatory and administrative jurisdiction of the Reserve Bank of India. In 1978, UTI was delinked from the RBI, and the Industrial Development Bank of India (IDBI) assumed regulatory and administrative authority in its place. UTI introduced its first scheme, Unit Scheme 1964 (US '64). In 1988, UTI had ₹ 6,700 crores of assets under management (AUM).
Second Phase 1987 – 1993 Entry of public sector mutual funds	The year 1987 saw the introduction of public sector mutual funds established by public sector banks, the Life Insurance Corporation of India (LIC), and the General Insurance Corporation of India. SBI Mutual Fund was the first 'non-UTI' mutual fund created in June 1987, followed by Canbank Mutual Fund in December 1987, Punjab National Bank Mutual Fund in August 1989, Indian Bank Mutual Fund in November 1989, Bank of India in June 1990, and Bank of Baroda Mutual Fund in October 1992. LIC created its mutual fund in June 1989, whilst GIC did it in December 1990. In 1993, the mutual fund sector managed assets worth ₹ 47,004 crore.
Third Phase 1993 – 2003 Entry of private sector mutual funds	The Indian securities market gained prominence with the founding of SEBI in April 1992, which was created to protect the interests of investors in the securities market, promote its development, and regulate it. The first set of SEBI Mutual Fund Regulations, with the exception of UTI, became effective in 1993. In July 1993, the Kothari Pioneer (now Franklin Templeton MF) became the first private sector mutual fund to be registered. With the introduction of private sector funds in 1993, a new era began in the Indian mutual fund market, providing Indian investors with a broader range of MF products. The initial SEBI MF restrictions were updated and replaced in 1996 by a comprehensive set of restrictions known as the SEBI (Mutual Fund) Regulations of 1996, which are still in effect today. The number of MFs has grown throughout the years, with many international sponsors establishing mutual funds in India. During this time, there were also significant mergers and acquisitions in the mutual fund business. As of January 2003, 33 mutual funds had a total AUM of ₹ 1,21,805 crores, with UTI alone accounting for ₹ 44,541 crore.

Fourth Phase 2003 - 2014	Following the repeal of the Unit Trust of India Act 1963 in February 2003, UTI was divided into two different entities: the Specified Undertaking of the Unit Trust of India (SUUTI) and the UTI Mutual Fund, which is governed by the SEBI MF regulations. With the dissolution of the former UTI and multiple mergers among several private sector funds, the MF business entered its fourth phase of consolidation. Following the worldwide meltdown in 2009, stock markets around the world collapsed, including in India. Most investors who had entered the capital market during the peak had lost money, and their trust in mutual funds had been severely undermined. The elimination of Entry Load by SEBI, combined with the aftermath of the global financial crisis, exacerbated the negative impact on the Indian MF Industry, which struggled to recover and remodel itself for more than two years in an attempt to maintain its economic viability, as evidenced by the sluggish growth in MF Industry AUM between 2010 and 2013.
Fifth Phase (Current) 2014 –	Recognizing the lack of penetration of MFs, particularly in tier II and tier III cities, and the need for greater alignment of the interests of various stakeholders, SEBI introduced several progressive measures in September 2012 to "re-energize" the Indian Mutual Fund industry and increase MF penetration. In the end, the measures were successful in reversing the downward trend that had begun during the global meltdown, and things improved dramatically after the new government was created at the center. Since May 2014, the Industry has witnessed steady inflows and increase in the AUM as well as the number of investor folios (accounts). In May 2014, the industry's AUM reached ₹ 10 Trillion (₹ 10 Lakh Crore) for the first time. Within three years, the AUM grew to above ₹ 20 trillion (₹ 20 Lakh Crore) in August 2017. In November 2020, AUM reached ₹ 30 trillion (₹ 30 lakh crore) for the first time. The Indian mutual fund industry has risen from ₹ 10.90 trillion on November 30, 2014 to ₹ 68.08 trillion by November 30, 2024, a more than 6-fold increase in 10 years. The MF Industry's AUM has increased from ₹ 27.05 trillion on November 30, 2019 to ₹ 68.08 trillion. The number of investor folios has increased more than twofold during the last five years, from 8.65 crore on November 30, 2019 to 22.08 crore on November 30, 2024. Since November 2019, an average of 22.38 lakh new folios have been added per month during the last five years. The growth in the size of the industry has been possible due to the twin effects of the regulatory measures taken by SEBI in re-energising the MF Industry in September 2012 and the support from mutual fund distributors in expanding the retail base. MF Distributors have been providing the much-needed last-mile connection with investors, particularly in smaller towns, and this is not only about enabling investors to invest in appropriate schemes, but also about assisting investors to stay on track during periods of market volatility and thus reap the benefits of investing in mutual funds. MF distributors have also played an important role in popularizing Systematic Investment Plans (SIPs) over the years. In April 2016, the no. of SIP accounts has crossed 1 crore mark and as on 30th November 2024 the total no. of SIP Accounts are 10.23 crore.

Source: <https://www.amfiindia.com/investor-corner/knowledge-center/history-of-MF-india.html#accordion5>

2.1 Growth of Mutual Fund in India

The mutual fund industry's net Assets Under Management (AUM) increased 33.11% year on year to Rs 52.74 lakh crore in January 2024, compared to Rs 39.62 lakh crore in January 2023. The increase in AUM is the largest since September 2021, when the year-on-year growth rate was 36.78%.

According to ICRA Analytics, the industry received net inflows of Rs. 1.23 lakh crore in January 2024, compared to net outflows of Rs. 0.41 lakh crore in December 2023. On a year-over-year basis, net inflows into the industry increased by 983% to Rs 0.11 lakh crore in January 2023. The Average Assets Under Management (AAUM) rose 29.62% on a year-on-year basis to Rs. 52.89 lakh crore in January 2024.

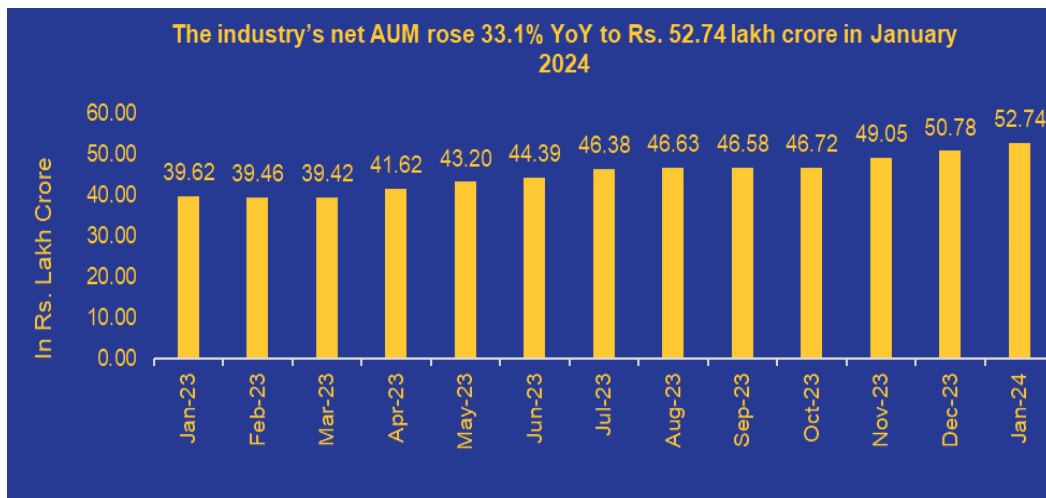


Figure: 1 Industry's net Assets Under Management (AUM)

Source: <https://smefutures.com/indian-mutual-fund-industry-aum-surges-33-11-to-rs-52-74-lakh-crore-in-jan-2024-icra/>

In January 2024, net inflows into open-ended equities mutual funds jumped by 28% month on month to Rs 0.22 lakh crore. Sectoral/thematic funds received the most net inflows of Rs. 4,805 crore among open-ended equity funds, followed by small-cap funds with net investments of Rs. 3,257 crore. In January 2024, the Flexi cap fund experienced the greatest monthly percentage increase in net flows. Aside from targeted funds, all other open-ended stock categories experienced net inflows in January 2024.

3. Review of Literature

According to Khababa (2024), older and less experienced investors tend to prefer mutual funds because of their convenience and limited financial expertise, whereas more experienced investors opt for direct investments, seeking higher returns and greater control over their portfolios.

Bhandari, D. R., & Subedi, D. P. (2024) findings of this study validated the set hypotheses that financial literacy, risk perception, and investment behavior have positive and significant effects on investment decisions among the investors in Nepalese mutual funds but the peer group has no any effect on investment decision.

Wilcox (2003) found that educated investors use basic financial information to make investing decisions. Mehry (2004), on the other hand, believes that mutual fund investors are uneducated. Furthermore, agents are more interested with the incentives and commissions they receive from selling schemes than with the quality of the products.

Badrinath and Gubellini (2012) investigate the performance of mutual funds over the business cycle. This is accomplished by dividing funds into several investment objectives to see whether funds exhibit cyclical performance. The results show that small-cap and mid-cap growth equity funds can add to performance, whereas value funds cannot. Chang et al. (2012) analyzed the financial performance of green and regular mutual funds. 131 green mutual funds were compared against standard mutual funds in their respective Morning Star categories based on a variety of performance indicators. Green mutual funds provided poorer returns than regular mutual funds in their respective Morning Star categories. Green mutual funds' performance has also been risk-adjusted. Trainor (2012), who investigated the risk-adjusted performance of individual mutual funds utilized by investors to participate in this asset class, discovered that past performance influenced future performance and that investors should invest in top-performing funds with the lowest expense ratio.

4. Objective of the Study

- To understand the evolution and growth of mutual fund industry in India.
- To gain insight into individual investors' mutual fund purchasing habits.
- Identify key features that investors consider relevant when investing in mutual funds.
- To determine the key underlying causes and their respective importance to investors.
- To find out whether these extracted components vary with demographic characteristics.

5. Research Methodology

An exploratory study was undertaken by studying the literature on the subject, followed by unstructured interviews with investors and investment consultants who work with mutual funds. All of these helped to discover the factors on the subject. These characteristics served as the basis for a structured questionnaire. Eleven criteria were recognized as significant to investors when investing in a mutual fund. These were scored on a 5-point scale: 1 = very unimportant, 2 = unimportant, 3 = neither important nor unimportant, 4 = important, and 5 = very important. Aside from demographic inquiries, there were questions about investment behaviour. The survey instrument was pretested with 15 respondents, and the questionnaire was changed based on their input. The replies were obtained through an online survey. Some responders were individually approached to complete the questionnaire. A total of 431 usable responses were gathered. Some of the questions were left blank by the responders. Such questions were excluded from the study, and the sample size was lowered appropriately. A reliability test using Cronbach's alpha was performed on the relevance of 11 qualities measured on an interval scale. Cronbach's alpha was calculated to be 0.781, which is fairly high. A factor analysis was performed on these items. The relevance of factors was determined by calculating the average factor score for each component. The factor scores for each demographic variable are compared using one-way ANOVA.

6. Data Analysis and Outcomes

Table 2 reveals that 64.7% of respondents fall within the age group of 25–35 years. The majority are male (87.4%), with 71.9% holding postgraduate qualifications. Most respondents are married (80.3%) and employed in the private sector (79.8%). Additionally, 45.7% report an annual family income of ₹ 10 lakh or more, and 85.5% reside in metropolitan cities. On average, there are 2.15 earning members per family, while 1.42 individuals are financially dependent on each respondent.

Table 2 Demographic Profile of the Respondents

Variable	Description	Percentage
Age (years)	< 25	11.1
	25–35	62.7
	36–50	21.6
	More than 50	4.6
Sex	Male	82.4
	Female	17.6
Educational qualification	Graduation	28.1
	Postgraduation and above	69.9
Marital status	Single	41.7
	Married	60.3
Profession	Private sector	79.8
	Public sector and government	11.7
	Business	4.5
	Self-employed	1.0
	Any other	3.1
Annual family income	Up to ₹ 250,000	3.4
	₹ 250,001–500,000	16.8
	₹ 500,001–750,000	17.3
	₹ 750,001–1,000,000	16.8
	Above ₹ 1,000,000	45.7
Place of current residence	Metropolitan city	85.5
	Non-metropolitan city	14.5
Source: Authors' findings.		

The demographic profile of the respondents reveals several key insights. The majority (62.7%) are aged between 25–35 years, indicating a sample primarily in their early to mid-career stages, with smaller proportions below 25 years (11.1%) and above 50 years (4.6%). There is a notable gender imbalance, with 82.4% being male and only 17.6% female. The respondents are highly educated, with 69.9% holding postgraduate degrees or higher and 28.1% being graduates. Most are married (60.3%), suggesting family responsibilities are prevalent among the group. Professionally, 79.8% are employed in the private sector, with smaller percentages working in the public sector (11.7%), business (4.5%), or self-employment (1.0%). Income distribution shows a skew towards higher-income groups, with 45.7% earning above ₹ 1,000,000 annually, while only 3.4% fall into the lowest income category (up to ₹ 250,000). Geographically, the majority (85.5%) reside in metropolitan cities, indicating urban dominance, with only 14.5% living in non-metropolitan areas. Overall, the respondents represent a predominantly male, urban, affluent, and well-educated demographic, potentially influencing the perspectives reflected in the findings.

Table 3 Source of Information for Purchase of Mutual Funds

Investment Instrument	Numbers	Percentage* (per cent)
Recommendation of friends and family members	175	40.9
Recommendation of the broker	147	34.3
Performance record of the issuing company	242	56.5
Radio	3	0.7

Television	55	12.9
Newspaper	122	28.5
Others	88	20.6
Total	428	
Source: Authors' findings.		
Note: *Total exceeds 100 per cent because of multiplicity of answers.		

The performance record of the issuing company is the most common source, cited by 56.5% of respondents, reflecting the importance of historical performance in investment decisions. Recommendations from friends and family (40.9%) and brokers (34.3%) also play a substantial role, indicating a reliance on personal networks and professional advice. Traditional media, such as newspapers (28.5%) and television (12.9%), contribute moderately to information dissemination, whereas radio has minimal impact, with only 0.7% citing it as a source. Additionally, 20.6% of respondents rely on other unspecified sources, showcasing diverse influences. The total percentage exceeds 100% due to multiple answers, underscoring that investors often use a combination of sources to make informed decisions.

Table 4 Two Most Important Funds of the Investors

Investment Instrument	Numbers	Percentage* (per cent)
Balanced fund	87	20.2
Growth fund	336	78.1
Debt funds	11	2.6
Tax saving funds	294	68.4
Sectoral funds	70	16.3
Income fund	25	5.8
Others	9	2.1
Total	430	

The data on the two most important funds for investors reveals a strong preference for growth and tax-saving funds. Growth funds are the most favored, with 78.1% of respondents identifying them as a priority, reflecting investors' inclination toward high-return, equity-based investment options. Tax-saving funds are also highly significant, chosen by 68.4%, indicating the dual importance of financial growth and tax benefits. Balanced funds, preferred by 20.2%, appeal to those seeking a mix of stability and moderate returns. Sectoral funds (16.3%) attract investors interested in specific industries, while income funds (5.8%) and debt funds (2.6%) cater to those with a lower risk appetite. A small proportion (2.1%) selected other types of funds. The total percentage exceeds 100% due to multiple responses, highlighting that investors diversify their preferences across different fund types to achieve varied financial goals. Overall, the data underscores the dominance of growth and tax-saving funds in investment priorities.

Out of the 11 attributes considered, the most important factors identified by respondents were past performance (93%), reputation of the company issuing the fund (84.9%), portfolio of the investment (84.6%), tax benefits (71.9%), and transparency of the fund manager (71.5%). Add-ons provided by the funds were deemed important by only 24% of respondents.

A factor analysis was conducted on these 11 attributes to identify underlying dimensions. The Kaiser-Meyer-Olkin (KMO) statistic was calculated at 0.85, exceeding the threshold of 0.5, and Bartlett's test of sphericity was found to be significant. These results confirmed the suitability of the dataset for factor analysis. Using the principal component method, two factors were

extracted, explaining 45.256% of the total variance. A rotated component matrix was generated, and factor loadings greater than 0.5 were used to interpret and name the factors.

The first factor included attributes such as past performance record, performance of the portfolio manager, reputation of the company issuing the fund, portfolio of the investment, and favorable ratings by rating agencies. The details of the rotated component matrix are provided in Table 5.

Table 5 Rotated Component Matrix

Attribute	Component 1	Component 2
Past performance record	0.773	0.123
Entry and exit load	0.125	0.527
Performance of the portfolio manager	0.678	0.120
Reputation of the company issuing the fund	0.571	0.311
Portfolio of the investment	0.759	0.118
Favourable rating by rating agency	0.611	0.098
Transparency of fund manager	0.698	0.140
Add-ons provided by the funds	-0.013	0.671
Declaration of NAV on daily basis	0.359	0.407
Lock in period of the closed-ended funds	0.109	0.735
Tax benefits available on MF	0.313	0.549

7. Findings and Recommendations

It has been found that past performance of the issuing company, tax-saving funds and growth funds with capital appreciation are the important considerations for investors in a mutual fund. It is surprising to know from our study that more than 54 per cent of investors want a capital appreciation and higher return along with tax savings and low risk. This shows that investors have very high expectations from the fund managers, whom they expect to generate a high return with minimum possible risk. This is contradictory to the famous theory in finance that 'high return is associated with high risk'. Since the mutual funds face under constant pressure to invest in securities that are likely to give much higher returns than the risk-free instruments. As the cost of capital to the investor is much less in risk-free investments, which is just the risk-free rate, the return from mutual fund is risk-free rate plus risk premium. Mutual fund companies would succeed if they are able to provide premium to the investors. Otherwise, it will be difficult for them to compete with the risk-free instruments. This is more the case with equity schemes and growth schemes. Our result is concurrent with many researchers who have conducted research in different periods, which shows that past performance is an important factor for investment by the investors and majority of the investors themselves take investment decisions. Therefore, fund managers put all their efforts to generate high returns to have a stable record of performance and have competitive advantage. It may be worth noting that investment in mutual funds if redeemed after one year of investment is tax free. This aspect may be highlighted while advertising for mutual funds.

The results indicate that two factors are considered important by investors while investing in mutual funds. These, in order of importance, are credibility of fund and miscellaneous features of fund. Since the results have indicated that the general public, business people and employees of public sector and government attach a lot of importance to the credibility of the fund, the credibility factor should be emphasized at the time of issuing mutual funds.

The second factor, namely, the miscellaneous features of the fund, is considered important by younger, unmarried people. This factor comprises of variables like entry and exit load, add-ons provided by the funds, lock-in period of the closed-ended funds and tax benefits available on mutual funds. All these variables are considered very important by most of investors with the exception of add-ons provided by the mutual funds which is considered important by slightly above 50 per cent respondents.

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