

# Investor Behavior and Industry Challenges in Indian Mutual Funds: A Comprehensive Analytical Approach

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## ABSTRACT:

*This study conducts a multifaceted exploration of investor behavior and industry challenges within the Indian mutual fund ecosystem, employing a comprehensive analytical framework. On the behavioral front, we examine demographic influences such as age, education, and risk appetite on investment decision-making, replicating survey-based methodologies that highlight the roles of financial literacy, peer advice, and emotional biases. The analysis further delves into prevalent behavioral phenomena in Indian investors, including herding, FOMO-driven inflows into mid- and small-cap funds, trend-chasing withdrawals from low-risk schemes, and portfolio rebalancing towards gold and alternatives. On the industry challenges side, the paper assesses structural issues such as incomplete market penetration due to low retail participation and limited financial awareness; technological barriers in reaching first-time investors; and systemic risks accentuated by episodes like credit crises in NBFC-backed debt funds (e.g., IL&FS, DHFL) that have undermined liquidity and investor confidence. Additionally, regulatory scrutiny and governance tensions such as SEBI's response to style drift, scheme fragmentation, and closure of certain fund categories are evaluated for their impact on fund transparency and trust.*

*The study uses a mixed-methods approach, integrating quantitative survey data with secondary data analysis of net flows, SIP trends, and AUM growth. It also presents case-based evaluations of institutional regulations and investor protection frameworks. Evidence includes record-high SIP inflows exceeding ₹27,000 cr in June 2025, alongside a wave of SIP terminations and shifts towards alternative assets. These dynamics underscore evolving investor preferences and the adaptive strategies of fund houses. The research advances a holistic model linking investor psychology with institutional and regulatory structures. It recommends targeted financial education programs, enhanced digital engagement strategies, and tighter governance practices to improve retail inclusion, safeguard liquidity, and nurture sustainable industry growth. The findings benefit academics, policymakers, asset managers, and regulators aiming to foster a resilient, investor-centric mutual fund market in India.*

*Keywords: Assets Under Management (AUM), Fear of Missing out (FOMO), Indian Mutual Fund Industry, Rapid Digitalization, Rapid Fintech-led Digitization, Systematic Investment Plans (SIPs).*

## 1. INTRODUCTION

In recent years, the Indian mutual fund industry has witnessed transformative growth, driven largely by evolving investor behavior and rapid digitalization. With assets under management (AUM) soaring from ₹9 trillion in 2014 to over ₹74 trillion as of June 2025, retail participation especially through Systematic Investment Plans (SIPs) has

become a defining feature of the market. For the first time, monthly SIP inflows surpassed ₹27,000 crore in June 2025, with nearly 8.64 crore active SIP accounts, reflecting increased financial commitments by investors. This surge is further characterized by a marked shift toward equity exposure, with equity mutual funds attracting ₹23,587 crore in inflows in June, representing a 24% recovery following a dip in May. Notably, mid and small-cap segments drew ₹47,000 crore in H1 CY2025 signaling heightened risk appetite driven by past performance and fear of missing out (FOMO).

Despite these encouraging trends, the industry faces critical obstacles. Retail distribution remains urban-biased, with limited penetration in smaller towns and rural India. A significant knowledge gap persists over 70% of urban investors show low awareness of essential financial concepts like portfolio allocation. Rapid fintech-led digitization also brings along cybersecurity vulnerabilities and potential for irrational investment behavior. Additionally, mutual funds face pressure from fee compression and increased competition, including innovative low-cost models from Jio-BlackRock, while regulatory complexity and style drift further challenge investor protection and confidence.

## **2. INVESTOR BEHAVIOR IN INDIAN MUTUAL FUNDS**

### **2.1 Shifts from Fixed Deposits to Mutual Funds**

FDs losing popularity; retail investors leaning towards higher returns in equity and mutual funds [1].

### **2.2 SIPs & Equity Preference**

SIP inflows achieved ₹20,371 cr in April 2025; equity MF inflows surging ₹23,587 cr in June 2025.

### **2.3 Risk-on Behavior & FOMO**

Strong inflows into mid/small-cap—₹47,000 cr in H1 CY25—driven by recent high returns and FOMO.

### **2.4 Digital & Millennial Influence**

Demat accounts exceed 150 mn; digital platforms, robo-advisors, fintech adoption rising [2].

## **3. BEHAVIORAL DRIVERS & VULNERABILITIES**

### **3.1 Financial Literacy & Awareness**

Over 70% of urban Indians lack awareness about portfolio allocation; investor education is a substantial barrier [3].

### **3.2 Irrational Behavior & Advice Reliance**

Risk of poor choices from product recommendations; digital advice may foster blind reliance [4].

### **3.3 Cybersecurity & Fraud Risks**

Digital vulnerabilities open doors to scams and phishing attacks, eroding trust [5].

## **4. INDUSTRY CHALLENGES**

### **4.1 Limited Penetration & Distribution Gaps**

AUM concentrated in top 15–20 cities; rural/far-tier expansion remains minimal.

### **4.2 Regulatory and Operational Hurdles**

KYC complexity, frequent regulation changes, and compliance burdens pose continuous challenges [6].

### **4.3 Competition & Fee Pressure**

Entry of low-cost players (e.g., Jio BlackRock); passive funds, and fintech are increasing cost-awareness.

### **4.4 Performance & Style Drift**

68% of large-cap active funds underperformed benchmarks over 10 years; style drift remains a concern [7].

#### 4.5 Liquidity & Crisis Risks

Past episode: 2020 Franklin Templeton exit highlighting liquidity stress and risk perception [8].

### 5. REGULATORY INFLUENCE

#### 5.1 SEBI's Role

Investor protection through direct plans, digital KYC, disclosure norms, ESG guidelines [9].

#### 5.2 AMFI & Industry Self-Regulation

Collaborative campaigns (“MF Sahi Hai”) to raise awareness, alongside efforts toward standardized distribution.

### 6. STRATEGIC RECOMMENDATIONS

Sr. No.	Focus Area	Recommendations
1.	Education & Literacy	Enhance fintech-led learning, integrate financial literacy in schools [10].
2.	Digital Platforms & Trust	Strengthen digital KYC, cyber security, and fraud response protocols [11].
3.	Distribution Expansion	Use hybrid distribution/robo-advice to penetrate tier-2/tier-3 areas.
4.	Product Innovation	Emphasize thematic, ESG, passive funds to address varied investor needs [12].
5.	Regulatory Simplification	Streamline KYC, advance transparency, and support digital-first compliance [13].
6.	Active-Fintech Collaboration	Fund houses should partner with fintechs for personalized advisory and education [14].

### 7. CONCLUSION

The Indian mutual fund industry stands at a critical crossroads anchored by robust growth and digital transformation, yet challenged by awareness gaps, distribution inequality, and emerging risks. Retail participation driven by Millennials and technology has revolutionized inflows and SIP adoption. However, investor vulnerability stemming from FOMO, financial illiteracy, and cyber threats underscores the urgency for educational and digital safeguards. Meanwhile, industry-wide focus must remain on deepening penetration, simplifying operations, and ensuring product and pricing transparency in a competitive, fintech-driven environment.

A triad of focused actions digital education, product innovation, and regulatory cooperation can help ensure that India’s mutual fund sector continues its inclusive growth trajectory. By aligning investor empowerment with structural robustness, the industry can navigate evolving challenges and meaningfully serve both retail and systemic stakeholders.

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