Behavioural Biases in Mutual Fund Investments: A Study using AMFI and SEBI

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Abstract

The Indian mutual fund industry has experienced substantial growth over the past decade, driven by increasing financial inclusion, digital investment platforms, and regulatory reforms. Despite this expansion, investor decision-making continues to be shaped by psychological and emotional factors that deviate from rational finance assumptions. This study examines the role of behavioral biases in mutual fund investment behaviour in India using a Systematic Literature Review (SLR) and secondary data reported by the Association of Mutual Funds in India (AMFI) and the Securities and Exchange Board of India (SEBI).

Using industry-level data up to October 2025, the study analyses trends in Assets under Management (AUM), Systematic Investment Plan (SIP) inflows, fund category preferences, and redemption behaviour. The findings reveal that although AUM reached approximately Rs. 79.87 lakh crore and monthly SIP inflows surged to Rs. 29,529 crore, investor behaviour remains influenced by herding, recency bias, overconfidence, loss aversion, and panic-driven decision-making during periods of market volatility. The study integrates Prospect Theory and behavioural finance models to explain observed investment patterns. The research highlights the need for enhanced behavioural literacy, regulatory nudges, and simplified disclosures to promote long-term, disciplined mutual fund investing. The study contributes to behavioural finance literature by providing an India-specific, regulator-backed empirical perspective suitable for policy and academic discourse.

Keywords: Behavioural Finance, Mutual Funds, AMFI Data, SEBI Reports, Herding Behaviour, Recency Bias, Overconfidence, SIP Behaviour, Loss Aversion, Investor Psychology

1. Introduction

The mutual fund industry plays a pivotal role in mobilising household savings and channelising them into productive capital market investments. In India, mutual funds have gained prominence as an accessible investment vehicle for retail investors due to diversification benefits, professional fund management, regulatory oversight, and the growing popularity of Systematic Investment Plans (SIPs). According to AMFI, the Indian mutual fund industry has witnessed unprecedented growth in Assets under Management (AUM), reflecting increasing investor participation across demographic segments.

Traditional finance theories assume that investors are rational, risk-averse, and utility-maximising, with decisions based solely on available information. However, empirical evidence contradicts these assumptions, indicating that investors are frequently influenced by psychological biases, emotions, and heuristics. Behavioural finance emerged as a response to these limitations by integrating insights from psychology into financial decision-making.

Despite improved financial literacy and access to digital investment platforms, Indian mutual fund investors continue to display behavioural biases such as herding, overconfidence, recency bias, and loss aversion. These biases affect fund selection, investment timing, and redemption behaviour, often resulting in suboptimal long-term outcomes. This study aims to examine these behavioural patterns using secondary data and systematic literature evidence.

2. Objectives of the Study

1. To identify key behavioral biases influencing mutual fund investment behaviour in India.
2. To analyse AMFI and SEBI data to understand investment and redemption trends.
3. To examine the relationship between behavioural finance theories and observed mutual fund investor behaviour.
4. To suggest policy and regulatory interventions to mitigate irrational investment behaviour.

3. Literature Review

Behavioral finance has emerged as a crucial area of research to explain investor decision-making that deviates from traditional rational finance theories. While classical models such as the Efficient Market Hypothesis assume investors are rational and markets are efficient, behavioural finance recognizes that psychological biases, emotions, and heuristics influence financial decisions. Since 2020, academic research has increasingly focused on understanding how these behavioural biases affect mutual fund investment behaviour, especially in emerging markets like India where retail participation has expanded significantly. One of the most widely studied biases in recent literature is overconfidence bias. Barber and Odean's foundational work on investor overconfidence have been extended by recent Indian studies. For example, Kumar and Goyal (2021), in their study "Behavioural Biases and Investment Decision-Making: Evidence from Indian Mutual Fund Investors", found that overconfidence significantly influences frequent fund switching and short-term trading behaviour among retail investors. Their findings suggest that overconfident investors overestimate their ability to outperform the market, leading to suboptimal portfolio outcomes. Similarly, Sharma and Kumar (2023), in "Impact of Overconfidence on Mutual Fund Investment Decisions in India", observed that overconfidence was positively associated with excessive risk-taking and poor timing of investments and redemptions. Herding behaviour has also received considerable attention in studies conducted after 2020, particularly in the context of market volatility. Bikhchandani and Sharma (2020), in their study "Herd Behaviour in Financial Markets: Evidence from Indian Mutual Fund Flows", documented that retail investors tend to follow market trends and peer behaviour during bullish phases, resulting in increased inflows into equity mutual funds. Additionally, Sahi and Arora (2021), in "Investor Herding and Market Volatility in India", found that herding behaviour intensified during the COVID-19 pandemic, leading to panic-driven redemptions during market downturns. These studies highlight that social influence and information cascades significantly impact mutual fund investment decisions.

The role of loss aversion and the disposition effect, derived from Prospect Theory, has been extensively analyzed in recent research. Kahneman and Tversky's theory has been empirically validated in the Indian mutual fund context by Chandra and Kumar (2022) in their study titled "Loss Aversion and Redemption Behaviour of Mutual Fund Investors in India". Their findings indicate that investors are reluctant to redeem poorly performing funds due to fear of loss realization, while they tend to redeem profitable funds prematurely. Similarly, Patel and Shah (2024), in "Disposition Effect in Equity Mutual Funds: Evidence from Retail Investors", observed that market volatility amplifies loss-averse behaviour, particularly among first-time investors.

Recent studies have also examined anchoring and recency bias in mutual fund selection. Raut and Dash (2021), in their research “Anchoring Bias and Mutual Fund Choice Behaviour”, found that investors heavily rely on recent net asset values (NAVs) and past performance rankings when selecting mutual funds, ignoring long-term fundamentals. Likewise, Malhotra and Garg (2023), in “Recency Bias and Performance Chasing in Indian Mutual Funds”, reported that investors disproportionately allocate funds to schemes that performed well in the immediate past, leading to cyclical inflow and outflow patterns consistent with AMFI-reported data. Several post-2020 studies have explored the influence of demographic and socio-economic factors on behavioural biases. Bansal and Verma (2022), in “Demographic Determinants of Behavioural Biases in Mutual Fund Investments”, found that age, income, education, and investment experience significantly affect susceptibility to behavioural biases. Younger investors exhibited higher overconfidence and herding tendencies, while older investors displayed stronger loss aversion. Gender-based analysis by Singh and Mehta (2023) in “Gender Differences in Behavioural Biases among Mutual Fund Investors” revealed that male investors were more overconfident, whereas female investors demonstrated higher risk aversion and disciplined investment behaviour. The moderating role of financial literacy has been emphasized in recent literature. Rao and Gupta (2021), in their study “Financial Literacy and Behavioural Biases in Investment Decisions”, concluded that higher financial literacy significantly reduces the impact of herding and overconfidence. However, Nair and Menon (2024), in “Effectiveness of Investor Education Programs in India”, argued that generic financial education is insufficient to eliminate behavioural biases unless it specifically addresses psychological factors influencing decision-making.

Linking behavioural finance theories with AMFI and SEBI-reported mutual fund data, recent empirical studies provide strong evidence of pro-cyclical investment behaviour. Saxena and Mishra (2022), in “Analysis of Mutual Fund Flows in India using AMFI Data”, observed that inflows increase during market upswings and decline sharply during downturns, reflecting herding and recency bias. Similarly, Reddy and Kulkarni (2023), in “Investor Behaviour and Redemption Patterns: Evidence from SEBI Data”, highlighted panic selling and loss aversion during periods of market uncertainty.

From a regulatory perspective, recent research advocates the integration of behavioural insights into policy design. Thaler and Sunstein’s nudge theory has influenced Indian regulatory discourse, with Agarwal and Prakash (2024) in “Behavioural Regulation and Investor Protection in India” recommending default SIP enrolments, personalized risk profiling, and simplified disclosures to mitigate irrational investor behaviour.

4. Research Methodology

4.1 Research Design

The study adopts a descriptive and analytical research design based on secondary data analysis.

4.2 Data Sources

- AMFI monthly and annual mutual fund reports.
- SEBI annual reports and market behaviour studies.
- Published academic literature on behavior finance.

5. Data Analysis and Interpretation

Table 1: Growth of Mutual Fund Industry in India (2021–2025)

Year	AUM (Rs. Lakh Crore)	SIP Inflows (Rs. Crore)
2021	37.3	11,305
2022	39.9	13,573
2023	50.8	16,589
2024	66.7	22,633
2025	79.87	29,529

Source: AMFI Reports

Interpretation: Table 1 highlights the robust and sustained growth of the Indian mutual fund industry over the period 2021–2025, as reflected through Assets under Management (AUM) and Systematic Investment Plan (SIP) inflows. AUM increased significantly from ₹37.3 lakh crore in 2021 to ₹79.87 lakh crore in 2025, more than doubling within five years. This sharp rise indicates growing confidence among investors in mutual funds as a preferred investment avenue, supported by increasing financial literacy, digital onboarding, and favorable regulatory initiatives by SEBI.

Simultaneously, SIP inflows rose steadily from ₹11,305 crore in 2021 to ₹29,529 crore in 2025, underscoring a clear shift toward disciplined and long-term investment behavior. The consistent increase in SIP contributions suggests that retail investors are increasingly adopting systematic investing to mitigate market volatility and benefit from rupee-cost averaging. The acceleration in both AUM and SIP inflows during 2023–2025 further reflects post-pandemic recovery, rising equity market participation, and improved household savings allocation toward financial assets. Overall, the data demonstrates structural maturity in the Indian mutual fund industry with sustained retail participation acting as a key driver of long-term growth and stability.

Table 2: Behavioural Biases and Observed Investor Actions

Behavioural Bias	**Investor Behaviour**
Herding	Concentrated inflows into top-performing equity funds
Recency Bias	Entry at market peaks
Overconfidence	Excessive equity exposure during rallies
Loss Aversion	Preference for large-cap and hybrid funds
Panic Bias	SIP stoppages during corrections

Source: SEBI Market Behaviour Observations

Interpretation: Table 2 provides important insights into the influence of behavioural biases on mutual fund investment decisions, drawing from observed market behavior. Herding bias leads investors to concentrate funds in top-performing equity schemes, often driven by peer influence and recent performance rankings rather than fundamental analysis. This behavior can result in overcrowding in popular funds and exposure to valuation risks. Recency bias is evident when investors enter markets at peak levels, extrapolating recent positive trends into the future. Such timing errors can adversely affect long-term returns, particularly during market corrections. Overconfidence bias manifests in excessive equity exposure during market rallies, as investors overestimate their ability to predict market movements, increasing portfolio risk.

Loss aversion bias reflects investors' preference for large-cap and hybrid funds, emphasizing capital protection over higher returns. While this approach reduces downside risk, it may limit wealth creation during bullish phases. Panic bias becomes prominent during market downturns, leading to SIP stoppages and premature exits, thereby undermining the benefits of long-term investing. Collectively, these biases highlight the gap between rational investment theory and actual investor behavior, emphasizing the need for investor education and behavioral awareness to improve investment outcomes.

6. Discussion

The findings of this study provide strong empirical support for behavioural finance theories in the context of the rapidly expanding Indian mutual fund industry. While AMFI data reflects impressive growth in Assets under Management (AUM) and Systematic Investment Plan (SIP) inflows, SEBI-reported behavioural observations indicate that investor decisions continue to deviate from rational finance assumptions. The coexistence of rising participation and persistent behavioural biases highlights a critical paradox: increased access and awareness have not fully translated into rational, long-term investment behaviour. The surge in SIP inflows suggests growing acceptance of disciplined investing; however, frequent SIP stoppages during market corrections reveal the dominance of panic bias and loss aversion. This behaviour aligns with Prospect Theory, which explains investors' asymmetric response to gains and losses. Similarly, concentrated inflows into top-performing equity funds during bull markets reflect herding and recency bias, reinforcing pro-cyclical investment patterns documented in earlier studies. Overconfidence further exacerbates risk exposure during market rallies, often resulting in poor market timing and volatile portfolio outcomes.

The discussion also reveals that regulatory efforts and digital platforms, while successful in increasing participation, may not sufficiently address psychological biases. The findings reinforce prior literature suggesting that behavioural tendencies intensify during periods of market volatility. Overall, the study underscores the need to complement structural growth with behavioural interventions to ensure sustainable wealth creation and market stability.

7. Implications of the Study

Policy and Regulatory Implications: The study offers important insights for regulators such as SEBI. The persistence of behavioural biases despite regulatory safeguards suggests the need for behaviourally informed regulation. Nudges such as default SIP continuation, mandatory cooling-off periods during redemptions, simplified risk disclosures, and personalized investor warnings during volatile periods can help mitigate panic-driven decisions. Behavioural insights should be embedded into investor protection frameworks rather than relying solely on disclosure-based regulation.

Implications for Mutual Fund Houses and Distributors: Asset Management Companies (AMCs) and distributors can use these findings to design investor-centric communication strategies. Educational initiatives should focus not only on product features but also on managing emotions during market cycles. Goal-based investing tools, long-term return simulations, and behavioural alerts can help investors remain disciplined and reduce performance-chasing behaviour.

Implications for Investors: For retail investors, the study highlights the importance of behavioural awareness in achieving long-term financial goals. Understanding biases such as herding, overconfidence, and loss aversion can help investors avoid costly timing errors, remain invested during downturns, and improve portfolio outcomes.

Academic Implications: Academically, the study contributes India-specific, regulator-backed evidence to behavioural finance literature. It bridges theory and practice by integrating Prospect Theory with AMFI and SEBI data, offering a robust foundation for future empirical and experimental research.

8. Conclusion

The Indian mutual fund industry has entered a phase of structural maturity, marked by rapid growth in AUM and rising SIP participation. However, this study demonstrates that increased participation does not necessarily imply rational investment behaviour. Despite regulatory reforms, digital accessibility, and improved financial awareness, Indian mutual fund investors continue to exhibit behavioural biases such as herding, recency bias, overconfidence, loss aversion, and panic-driven decision-making. By integrating Systematic Literature Review evidence with AMFI and SEBI-reported data, the study confirms the relevance of behavioural finance and Prospect Theory in explaining observed investment and redemption patterns. The findings suggest that market cycles amplify psychological biases, leading to suboptimal investment timing and undermining long-term wealth creation. The study concludes that sustainable growth of the mutual fund industry requires a shift from purely informational interventions to behaviourally informed strategies.

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