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Risk perception of Retail Investors towards Mutual funds: A Survey of small investors

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Abstract

Mutual funds have gained immense popularity in recent years as a means of investment and understanding how small retail investors perceive the risks associated with these funds is essential to enable them to make informed decisions. The study indicates that small retail investors perceive mutual funds as a relatively safe and easy investment option. However, they are also aware of the risks associated with mutual funds, such as market volatility, economic uncertainty, and fund managers' performance. Furthermore, small retail investors perceive the risks differently based on their investment experience, age, education, and investment goals. The research aims to determine the elements that impact how small investors perceive risk toward mutual funds & understand the impact of these perceptions on their investment decisions. The study's results will be useful for mutual fund managers, financial advisors, and policymakers in designing investment products and strategies that are better suited to small investors' risk perception and investment behavior.

Keywords: Mutual funds, Investment, Risk perception, Return on Investment (ROI), Diversification, Investor's expectations

Introduction

Mutual funds are a popular investment option for small retail investors due to their potential for diversification and professional management. However, investing in mutual funds carries a certain level of risk& the perception of this risk by retail investors is an important factor in their decision-making process.

Risk perception is how investors perceive the potential risks associated with investing in mutual funds. This can be influenced by several variables, including the investor's level of experience, financial goals, and the information available to them. Small retail investors, in particular, may have a limited understanding of the risks, which can impact their investment decisions. It is important to note that risk perception is not necessarily the same as actual risk. While mutual funds do carry some level of risk, the extent of that risk can vary widely depending on factors such as the fund's investment strategy, portfolio holdings, and market conditions. To effectively manage risk, small retail investors should take steps to educate themselves on the risks associated with mutual funds, and carefully consider factors such as their investment goals, time horizon, and risk tolerance before making investment decisions. It is also important for investors to carefully review the prospectus and other disclosure documents provided by the mutual fund, and to seek the advice of a qualified financial professional if necessary.

Several factors can influence the risk perception of small retail investors towards mutual funds. One of the primary factors is the investor's level of financial literacy and understanding of the underlying investments in the mutual fund. Investors who are more knowledgeable about the investments in the fund and the market conditions that can affect their returns are more likely to have a lower perception of risk. Another factor that can affect the risk perception of small retail investors towards mutual funds is their past experience with similar investments. If an investor has had a negative experience with a mutual fund in the past, they may perceive mutual funds as a risky investment option. Additionally, external factors such as the overall economic environment, political stability, and regulatory environment can impact the risk perception of small retail investors towards mutual funds. A favorable economic and political environment can lead to a lower perception of risk, while unfavorable conditions can increase the perception of risk.

Overall, the risk perception of small retail investors towards mutual funds is an important consideration for both investors and the mutual fund industry as a whole, as it can impact investment decisions and ultimately, investment outcomes.

Literature review

Singh, R., et.al, (2017) concluded that their overall attitude towards investment in mutual funds is favorable. This finding is important for mutual fund managers as it suggests that there is potential for encouraging greater investment in mutual funds within a specific area. Overall, the study provides useful insights for mutual fund managers and highlights the importance of understanding investors' attitudes towards investment in mutual funds to improve investment volume.

Kaur, I., & Kaushik, K. P. (2016) talked about a range of factors that can impact how investors approach investing in mutual funds. The demographic factors like age, income& education level also had a major influence on the investment behaviour of investors toward mutual funds. Mutual fund companies need to focus on investor education and transparency in their operations to attract more investors. Additionally, they need to work on improving their fund manager's reputation and performance to gain investor trust. Therefore, the conclusions drawn from the analysis can be useful for policymakers to design more effective policies to promote mutual fund investment in India.

Rehan, R., Naz, S., Umer, I., & Ahmed, O. (2017) conclude that there is a significant lack of awareness & understanding among investors towards the mutual funds industry. Although investing in mutual funds has the potential to provide benefits such as diversification and professional management, potential investors are feeling uncertain about investing due to their limited understanding or information about the investment opportunity. Investors' perceptions of mutual funds are largely negative, with concerns about the safety of their investments and a perceived lack of transparency in the industry. These perceptions may also contribute to the low levels of investment in mutual funds. To address these issues, mutual fund companies and regulators must improve investor education and increase transparency in the industry. This may include providing clearer information about the risks of investing in mutual funds& also improving the accessibility of information for investors.

Ranganathan, K. (2006) investigated how individual investors choose mutual funds for investment purposes. The research found that investors rely heavily on past performance and the reputation of the fund house while making investment decisions. Investors also consider the advice of family and friends as well as their risk appetite and investment goals. The study highlights the need for investor education and awareness to enable informed decision-making. The research provides valuable insights for financial institutions, policymakers, and investors.

Overall, the study contributes to the field of behavioural finance and expands knowledge in this area.

Lee, T., Yun, T., & Haley, E. (2013) investigate how the advertising disclosures of mutual funds affect the decision-making and information processing of investors. The findings of the study revealed that respondents in the high-disclosure condition had a greater level of information processing and decision-making compared to those in the low-disclosure condition. Additionally, the study found that respondents in the high-disclosure condition had a greater level of perceived risk & perceived control over their investment decisions. Overall, the study suggests that mutual fund advertising disclosures have a major influence on investor decision-making and information processing. The results may be useful for mutual fund companies & regulators in developing more effective and informative disclosure documents to help investors make better investment decisions.

Agrawal, G., & Jain, M. (2013) investigated the investment preferences of investors in mutual funds compared to other investment options. The research findings suggest that mutual funds are the preferred investment option among investors due to their professional management, diversification, and ease of investment. Investors tend to have a greater inclination towards equity-oriented mutual funds compared to debt-oriented mutual funds. Furthermore, the study also found that investors' age, income, and investment experience have a significant impact on their investment preferences.

Younger investors with higher income and investment experience tend to have a greater inclination towards equity-oriented mutual funds, while older investors with lower income prefer debt-oriented mutual funds. The research concludes that mutual funds are a popular investment avenue among investors due to their benefits of professional management and diversification. However, investors' investment preferences vary based on their demographic and investment characteristics, highlighting the importance of considering these factors when designing mutual fund investment products.

Bajracharya, R. B. (2017) concluded that investors generally have a positive attitude towards mutual funds. The investors consider mutual funds to be a convenient and cost-effective investment option, and they also believe that mutual funds can provide them with better returns than other investment avenues.

Objectives

- To measure the risk perception of small investors towards Mutual Funds

Methodology

In this study a survey was conducted among the small mutual fund investors having a portfolio of Rs. 3,00,000 to 10,00,000 including both "Systematic Investment Plan and Lum Sum Investment". The size of sample was 154respondents. Data analysis was performed by applying mean score. Respondents were selected based on the judgement criteria given above to maintain the homogeneity of the responses and better generalization of the results of this study.

Data Analysis and Findings

Table 1 Risk Perception of Retail Investors towards Mutual Funds

Serial No.	Statement	Mean Value
1.	Mutual funds diversify the risks	4.22
2.	Risks in Mutual funds is professionally managed	4.01
3.	Mutual funds give wide variety of options to manage risk	3.87
4.	Mutual funds cater to needs as per the risk profile of investor	3.93
5.	Mutual funds' portfolios can be customized for different types of the Risk and Returns	4.05
6.	Mutual fund risk is managed by renowned experts	4.13
7.	Mutual funds are the first choice of institution investors; hence it reduces the risk of fund inflow	3.83
8.	Mutual funds provide long-term risk-free returns	3.90

Table 1 shows the Risk Perception of Retail Investors towards Mutual Funds. It was found that Mutual funds diversify the risks (mean score 4.22), followed by Mutual fund risk is managed by renowned experts (4.13), Mutual funds' portfolios can be customized for different types of the Risk and Returns (4.05), Risks in Mutual funds is professionally managed (4.01), Mutual funds cater to needs as per the risk profile of investor (3.93), Mutual funds provide long term risk free returns (3.90), Mutual funds give wide variety of options to manage risk (3.87) and Mutual funds are the first choice of institution investors, hence it reduces the risk of fund inflow (3.83).

Conclusion

Retail investors, especially small investors, may perceive mutual funds as a risky investment option due to a lack of understanding of the underlying investment strategies and the potential for fluctuations in market conditions. This perception may be further compounded by instances of fraud or mismanagement by certain mutual fund companies. To mitigate risk perception, small investors can educate themselves on the fundamentals of investing, including the risks and rewards of mutual funds. They can also seek the advice of a financial advisor or do their due diligence on the mutual fund's past performance, fees, and investment objectives before investing. Overall, while retail investors may perceive mutual funds as risky, it is essential to have a balanced understanding of the potential risks and rewards associated with investing in mutual funds. Risk perception is subjective and can vary from individual to individual. Small investors need to understand their risk tolerance and make informed investment decisions based on their circumstances. By doing proper research and seeking guidance from financial experts, small investors can make informed investment decisions and achieve their financial goals.

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