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FACTORS AFFECTING THE INVESTMENT DECISIONS OF INVESTORS IN MUTUAL FUNDS- AN OVERVIEW

Dr. K. Kulanjiammal
Assistant Professor of Commerce
Idhaya College for Women, Kumbakonam.
(Affiliated to Bharathidasan University)
Email : kulanjis@gmail.com

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ABSTRACT

A mutual fund can be a great place to start your investments. It offers individual investors the opportunity to invest in a diversified portfolio that is managed by professional fund managers, even with relatively small amounts of money. However, what are the factors the investor should consider before selecting a mutual fund investment. This articles various factors that will aid your decision-making while investing in mutual funds.

Introduction:

A mutual fund is a specialized investment mechanism where multiple investors pool money to invest collectively in a diversified portfolio of bonds, stocks and/or other securities. There are several benefits of investing in mutual funds. For example, they offer individual investors the opportunity to invest in a diversified portfolio that spreads the risk around. So, even if one of the security investments is heading south, other better-performing securities can help make up for it. Also, mutual funds are managed by investment professionals who make decisions on your behalf about which securities to buy, hold, and sell within the fund's portfolio. Investors buy shares of the mutual fund and the money collected from these investors is used to purchase a mix of assets according to the fund's investment objectives and strategy. This makes the process easier as investor don't have to go too deep into the intricacies of the market. And the fact that your investments can even be started with relatively small amounts of money just makes it an even better proposition.

The subject of investment has always been quite fascinating. It offers investors the chance to make money and broaden their financial horizons. Without a doubt, since the beginning, we have all been captivated by the appeal of investing. Additionally, making an investment decision requires taking into account a number of important factors, including investor personal financial objectives, risk tolerance, and budgeting abilities. It's critical to make the right choices today because they could have a big impact on investor's financial future.

A variety of factors influence the choices and decisions of investors in the aspect of Mutual Funds. In this we've compiled a list of factors affecting investment decisions and investment choices of investors.

(I) Risk Factor

Investments are always fraught with danger. For example, while Mutual Funds provide benefits such as value for money and diversification to investors, they also carry some risks.The best thing an investor can do to reduce Mutual Fund risks is to learn more about them and practice strategies for mitigating them.

Below are the Risk Factors associated with investments that may affect a person's investment decisions or may contribute to factors affecting investment decisions:

1) Market Risk

Many events, including those directly involving the companies whose scripts are owned by the funds, have the potential to cause the prices and income generated by the script held by Mutual Fund schemes to decline.In general, changes in currency and interest rates, regional or global economic instability, and economic and market conditions are some of the factors.

a. **Interest Risk:** Investors are plagued by interest risk, which appears as fluctuating interest value over the course of the investment horizon. The uncertainties surrounding the capital an investor is likely to access at the end of the investment horizon are largely to blame. In other words, the cost of the debt instrument will change if the interest rate does. For instance, the price of bonds declines when interest rates do, which causes the value of bonds to decline as well.
b. **Inflation Risk:** The risk of losing one's purchasing power, primarily as a result of rising inflation, is the best way to describe risks led by inflation. Investors are typically exposed to the effects of this risk when the rate of returns on investments falls short of the rate of rising inflation. For example, if the rate of returns is 5% and the rate of inflation is 3%, investors will only receive a return of 2%.

c. **Currency Risk:** The risk in question is the worry that falling exchange rates will result in lower investment returns. To explain, it is presumed that when the value of funds denominated in foreign currencies rises, the value of foreign currencies will fall. As soon as it is converted into INR, the rate of return will be directly lowered.

d. **Volatility Risk**: Equity-based funds typically make investments in the stock of corporations that are listed on stock exchanges. The value of these funds depends on how well businesses perform, which is frequently impacted by the predominant microeconomic factors. These variables include shifting governmental directives, SEBI rules, the state of the economy, RBI policies, etc. Notably, these variables have an impact on stock price and can change the share value.

2) Liquidity Risk:

Liquidity risk is frequently associated with Mutual Funds like ELSS that have a rigid and lengthy lock-in period. Such a risk indicates that it is frequently difficult for investors to sell their investments without suffering a loss.For example, ELSS has a strict lock-in period during which investors are limited in what they can do with their investments. Furthermore, it can be difficult to sell investments at a time that investors deem appropriate because there are frequently not enough buyers in the market.

3) Credit Risk

In Mutual Fund investments, credit risk frequently arises from a circumstance in which the issuer of the scheme fails to pay the promised interest. Typically, fund managers include investment-grade securities with strong credit ratings in debt funds. The fund manager does, however, include lower credit-rated securities to increase the rate of returns. This action frequently increases the chance of not receiving the promised payment.

(II) The Liquidity Factor

This is one of the most crucial factors influencing investment decisions. The ease with which an asset (such as equity shares, debentures, etc.) can be exchanged for money on the stock market is referred to as liquidity. Liquidity risk thus represents the risks involved in such trades since the successful conversion of stock into money depends on a number of factors, including a company's book value, the bid-ask spreads for its shares on the market, etc.

High liquidity risk typically means that a particular security is difficult to buy or sell on the stock market. This is due to the possibility that an issuing company's current liabilities may prove difficult to satisfy as a result of decreased cash flow.

a. **Funding Liquidity Risk** – Such risks are related to a company's intrinsic values, which reflect its capacity to pay off short-term debt with operating cash flows. Failure to pay current obligations (defaulting on loans) can damage an organization's reputation in the market, which can cause a sharp decline in the share price as investors lose faith in the organization's credibility and potential for success. A company's ability to generate future revenue may be significantly impacted if it must liquidate (sell) its current asset base to pay off rising debt levels and declining current assets.

b. **Market Liquidity Risk** - Such liquidity risks address the systematic risk element connected to market investments and resulting from stock market volatility. Because corresponding changes in share prices have an impact on the trading patterns of particular securities listed on stock exchanges, market forces are a significant factor in determining such trading liquidity risk. A high market liquidity risk means that it might be difficult to sell the specified securities, which would lead to low demand for them. There are a number of causes for this decreased demand, including:

- Highly volatile stocks are readily susceptible to price fluctuations.
- Ongoing economic crisis/ recession.
- A discredited reputation of a company due to certain events.
- Global economic scenario.

(III) Uniformity Factor

A good Mutual Fund is one that consistently outperforms its benchmark over the long term, as every investor is aware. The excess return is referred to as the fund's "alpha" when it exceeds the benchmark.Most importantly, it's the hard-earned money investors investing in a mutual fund with. The fund should surpass its benchmark and generate a higher alpha, as you should anticipate. It may be the first parameter you use.Furthermore, fund performance is important. It should be taken into account for a suitable amount of time. This is done to make sure the investments have experienced several market cycles.

This would make it possible to get a steady return over time. This is one of the most important factors that any investor takes into account while making an investment decision.

(IV) Quality of Returns Factor

When investing in a high-return Mutual Fund, one of the first things a retail investor considers is that the return should be both high and steady. Thus, investor should avoid Mutual Funds that have recently offered very high returns but have otherwise not offered great returns, as the quality and consistency of returns of a fund are some of the factors favoring investment decisions.

(V) Research Factor:

This might seem like a no-brainer, but you'd be surprised at how many people invest in the wrong fund only to discover later that it doesn't meet their needs. So, please, do not commit this error. A good investor will always place a high priority on their research.Make sure it is mutual funds want to invest in before investment start. Don't get sucked in because investor overheard investor friends talking about them, even though they are a fantastic option for most people. It's possible that all have different needs and demands from them. There is little benefit to investing in funds that don't give the security.

Conclusion

One of the best ways to utilize your extra income and earn some money is by investing in Mutual Funds. And there's no reason why you shouldn't make good profits as long as you maintain focus and exercise caution regarding the potential mistakes we discussed.The factors influencing retail investors' decisions to invest in Mutual Funds were properly covered in these articles. We hope that this articles pointsinvestors in the right direction and helps theyget a better picture of the investing situation.

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