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Determinants of Assets Under Management Growth in Indian Mutual Fund: Evidence from Ratings, Performance, and Fund Characteristics

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Abstract

This paper investigates the determinants of Assets Under Management (AUM) growth in Indian mutual funds, with a focus on the role of information signals, past performance, and fund characteristics in a retail-dominated emerging market context. Drawing on signaling theory, the fund flow–performance literature, and behavioural finance, the analysis investigates how third-party ratings, historical returns, fund size, and expense ratios influence investor capital allocation decisions. Using cross-sectional data on mutual funds and multiple regression analysis with robustness checks, the findings show that fund ratings, past long-term performance, and fund size exert a positive and statistically significant effect on AUM growth, while expense ratios do not significantly influence investor flows. The results underscore the significance of information intermediaries and visibility effects in reducing information asymmetry in emerging capital markets, where retail investors heavily rely on simplified quality signals. By offering evidence from India on how behavioral biases and informational cues work together to influence mutual fund capital allocation, the study adds to the growing body of research on emerging market finance. This has consequences for investor protection laws, fund managers, and regulators.

Introduction

The rapid expansion of the mutual fund industry in emerging markets has transformed household participation in capital markets, shifting retail investors from direct equity investments toward professionally managed investment vehicles. In countries such as India, mutual funds play a significant role in mobilising household savings, deepening financial markets, and improving access to diversified portfolios. However, the growth of mutual fund Assets Under Management (AUM) in emerging economies remains uneven across funds and categories, raising important questions about how investors allocate capital under conditions of information asymmetry, heterogeneous financial literacy, and market volatility. The AUM of Indian mutual industry grown at 24 percent compound annual growth rate during the period of 2020 to 2025.

Unlike developed markets, where institutional investors dominate fund flows, emerging markets are characterised by a high proportion of retail participation and relatively limited investor sophistication. In such contexts, investors face significant challenges in evaluating fund quality due to information constraints, limited disclosure literacy, and the complexity of performance metrics. Prior research suggests that investors rely on simplified informational cues and reputational signals when making allocation decisions (Sirri & Tufano, 1998; Del Guercio & Tkac, 2008). The fund flow–performance literature documents a strong and asymmetric relationship

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between past returns and investor inflows, whereby top-performing funds attract disproportionately higher capital allocations (Ippolito, 1992; Sirri & Tufano, 1998). Berk and Green (2004) further argue that performance-based inflows persist until managerial skill is competed away through asset growth. In parallel, signaling theory posits that observable quality indicators such as ratings serve as credible signals in markets characterised by information asymmetry, enabling investors to infer underlying fund quality and managerial competence (Spence, 1973; Blake & Morey, 2000). Behavioural finance further suggests that investors exhibit familiarity bias, salience effects, and limited attention, leading them to overweight prominent cues such as fund size and ratings while underweighting less salient attributes such as expense ratios (Barber & Odean, 2000; Barberis et al., 1998).

Existing studies are predominantly concentrated in developed market settings, where market efficiency, disclosure standards, and investor sophistication differ substantially from those in emerging economies. India offers a compelling laboratory to examine these dynamics, given its rapidly expanding mutual fund industry, increasing retail participation, and the growing prominence of third-party rating agencies that disseminate simplified quality signals to investors.

Against this background, this study examines the determinants of AUM growth in Indian mutual funds by analysing the effects of third-party fund ratings, past long-term performance, fund size, and expense ratios.

By integrating signaling theory, the fund flow–performance framework, and behavioral finance perspectives, this study makes three significant contributions to the literature on mutual funds and emerging market finance. First, it provides empirical evidence from India on how information signals, specifically third-party fund ratings, shape investor capital allocation and AUM growth in a retail-dominated emerging market characterised by information asymmetry. This extends fund flow–performance research beyond developed market settings, where investor sophistication and disclosure environments differ substantially. Second, by jointly examining fund ratings, past performance, fund size, and expense ratios within an integrated empirical framework, the study highlights how informational cues and behavioural biases interact in influencing investor decisions. The findings demonstrate that visibility and reputational effects associated with fund size and ratings exert a significant influence on asset growth, while cost considerations play a limited role, reflecting bounded rationality among retail investors in emerging markets. Third, despite a growing body of research on mutual fund flows and performance, empirical evidence from emerging markets remains relatively limited**,** particularly regarding how informational signals interact with behavioural biases in shaping AUM growth.

Literature Review and Hypothesis Development

Investing directly in the stock market involves considerable risk and requires extensive knowledge, continuous monitoring, and patience, making it unsuitable for many retail investors. Mutual funds have therefore emerged as an important alternative investment vehicle, enabling investors to participate in capital markets while benefiting from professional fund management and portfolio diversification. Although mutual funds generally involve lower risk than direct equity investments, their returns are also relatively moderate. Even though the mutual fund sector in India is expanding quickly, there is still a dearth of scholarly research on investor behavior, fund growth, and mutual fund performance, especially when it comes to particular fund categories.

Mutual Fund Performance and Risk-Adjusted Measures

Assessing mutual fund performance has long been central to financial research. Early approaches evaluated fund effectiveness using average returns in conjunction with measures of risk (Sharpe, 1966**).** Subsequent developments introduced risk-adjusted performance metrics that isolate

managerial skill by accounting for systematic market movements, most notably Jensen's alpha (Jensen, 1968**).** These measures provide a more refined assessment of whether fund managers generate returns beyond what can be explained by market exposure alone. Empirical applications of such metrics in the Indian mutual fund context reveal substantial variation in performance across schemes and fund houses, highlighting differences in managerial efficiency and portfolio construction strategies (Dhandaudhyam & Pratheep, 2018**).** More recent evidence suggests that fund size does not necessarily translate into superior risk-adjusted returns, indicating that scale alone is insufficient to guarantee better performance (Kumar, 2021**).** Overall, risk-adjusted indicators such as the Sharpe and Treynor ratios offer more meaningful insights into fund quality than simple return measures, particularly for evaluating long-term investment performance.

Fund Flow-Performance Relationship

A substantial stream of research has explored how mutual fund returns influence subsequent investor flows. Early empirical work established that investors tend to direct more capital toward funds with superior historical returns, resulting in a convex relationship between performance and inflows **(**Ippolito, 1992; Sirri & Tufano, 1998**).** This pattern indicates that high-performing funds receive disproportionately large allocations compared to average or poorly performing funds. Evidence from the Indian mutual fund industry also supports the presence of return-chasing behaviour, where investors reallocate capital toward schemes that have recently delivered stronger performance **(**Singh, 2018; Sahi, Arora & Dhameja, 2013**).** Theoretical explanations suggest that such inflows persist until fund size expands to a level at which managerial skill is fully absorbed by scale, reducing the ability to sustain abnormal performance **(**Berk & Green, 2004**).** Collectively, these findings imply that past performance serves as a key heuristic guiding investor capital allocation decisions, particularly in retail-dominated markets

Signaling Theory and the Role of Fund Ratings

In investment environments characterised by information asymmetry, investors rely on observable indicators to infer underlying fund quality (Spence, 1973**).** Third-party fund ratings condense complex information on performance consistency, risk exposure, and managerial competence into simplified signals that are easier for retail investors to interpret **(**Blake & Morey, 2000; Del Guercio & Tkac, 2008). In emerging markets, where financial literacy levels vary widely and access to detailed fund information is uneven, such ratings play an especially influential role in shaping investor perceptions (Sahi et al., 2013; Singh, 2018**).** These signals reduce information-processing costs and help investors differentiate between funds in a crowded marketplace (Sirri & Tufano, 1998). Consequently, ratings not only influence capital allocation decisions directly but also enhance fund visibility and credibility, thereby reinforcing reputational advantages that contribute to differential growth in assets under management across funds.

Behavioural Finance and Investor Awareness

Conventional finance makes the assumption that investors behave rationally, but behavioral finance research emphasizes how psychological biases affect financial judgment. When deciding which investments to make, investors frequently look to heuristics, current performance, and prominent indicators like ratings. Barberis, Shleifer, and Vishny (1998) and Barber and Odean (2000) argue that such behavioural biases can lead investors to overreact to recent information and chase perceived winners. Evidence from India supports this perspective. Anand (2023), using primary survey data, found that a majority of investors possessed limited or no awareness of mutual fund products. This lack of awareness increases reliance on simplified indicators such as ratings and past returns, while factors such as expense ratios and risk diversification are often

overlooked. Behavioural explanations therefore, complement fund flow–performance theory by explaining why investors prioritise performance and ratings over cost efficiency.

Research Gap

Although existing literature provides valuable insights into mutual fund performance, investor flows, and the role of fund ratings, several important gaps remain. First, prior studies often examine these factors independently rather than integrating them within a unified empirical framework that simultaneously considers risk-adjusted performance, third-party ratings, and behavioural influences on investor decision-making. Second, most empirical evidence is concentrated in developed markets, while relatively limited research examines these dynamics in emerging economies such as India, where retail investor participation is high and information asymmetry is more pronounced. Furthermore, the evolving dynamics of financial markets in the post-COVID period have altered investor behaviour and capital allocation patterns, yet empirical evidence on how these changes affect mutual fund asset growth remains limited. Addressing these gaps, this study empirically investigates the determinants of Assets Under Management (AUM) growth in Indian mutual funds by integrating insights from Signaling Theory, the fund flow–performance framework, and Behavioural Finance.

Hypotheses Development

Drawing on Signaling Theory, the fund flow–performance literature**,** and insights from Behavioural Finance, this study develops four testable hypotheses to examine the determinants of Assets under Management (AUM) growth in Indian mutual funds.

Fund Ratings and AUM Growth (Signaling Theory)

Signaling theory suggests that in markets characterized by information asymmetry, observable signals help investors infer the underlying quality of financial assets. According to Michael Spence (1973), credible signals can reduce information gaps between market participants. In the mutual fund industry, third-party ratings summarize complex information regarding performance consistency, risk exposure, and managerial capability into easily interpretable indicators.

Empirical studies show that fund ratings significantly influence investor capital allocation decisions beyond the explanatory power of past performance (Blake & Morey, 2000; Del Guercio & Tkac, 2008). In the Indian mutual fund market, where retail investor participation is substantial and financial literacy levels vary widely, rating agencies such as CRISIL provide simplified signals that help investors evaluate fund quality. Higher-rated funds are therefore expected to attract greater investor inflows.

H1: Mutual fund ratings have a positive and significant effect on AUM growth.

Past Performance and AUM Growth (Fund Flow–Performance Theory)

The fund flow–performance literature consistently demonstrates that investors allocate capital based on historical performance. Early studies such as those by Franklin Ippolito (1992) and Erik R. Sirri and Peter Tufano (1998) document a strong relationship between past returns and subsequent investor inflows. Funds that deliver superior performance tend to receive disproportionately higher capital allocations.

Furthermore, Jonathan Berk and Richard Green (2004) argue that investors continue to direct capital toward high-performing funds until managerial skill becomes fully reflected in fund size and performance outcomes. Consistent with this theoretical framework, investors in the Indian mutual fund market are expected to reward funds with strong historical returns.

H2: Past performance has a positive and significant effect on AUM growth.

Fund Size and AUM Growth (Visibility and Reputation Effects)

Insights from behavioural finance suggest that investors often exhibit familiarity bias and tend to favor investment options that are more visible and widely recognized. Larger mutual funds typically benefit from stronger brand recognition, broader distribution networks, and greater investor trust. These characteristics can increase fund visibility and attract additional investor inflows even when performance differences are relatively small.

Empirical research indicates that fund size may influence investor behavior through scale and reputation effects, particularly in emerging markets where information asymmetry is more pronounced. Consequently, larger funds may experience higher asset growth due to enhanced credibility and investor familiarity.

H3: Fund size has a positive and significant effect on AUM growth.

Expense Ratio and AUM Growth (Behavioural Perspective)

Traditional finance theory predicts that investors should prefer funds with lower costs because higher expenses reduce net investment returns. However, behavioural finance research suggests that investors often pay limited attention to expense ratios and instead rely on more salient information cues such as ratings and historical performance.

Studies indicate that retail investors frequently underweight cost considerations when making investment decisions (Sirri & Tufano, 1998; Sahi et al., 2012). This behaviour may be particularly evident in emerging markets where financial literacy varies across investors. As a result, expense ratios may not exert a strong influence on capital allocation decisions once other informational signals are considered.

H4: The expense ratio does not have a significant effect on AUM growth.

Data and Methodology

Data and Sample Selection

The empirical analysis is based on a sample of open-ended equity mutual funds operating in India**.** The study focuses on three fund categories—mid-cap, small-cap, and flexi-cap funds—as these categories have experienced substantial investor inflows and growing popularity in the post-COVID investment environment. These segments are particularly relevant for examining the determinants of asset growth because they represent actively managed equity strategies that attract considerable retail investor participation. The sample consists of 60 observations, selected based on the availability of complete and consistent data for key variables such as Assets under Management (AUM), fund ratings, historical returns, fund size, and expense ratios. To ensure comparability across schemes, only open-ended equity mutual funds with available CRISIL ratings were included in the analysis. Funds with incomplete information for the study variables were excluded from the final dataset. Restricting the sample to comparable fund categories improves internal validity by reducing heterogeneity in investment objectives, portfolio strategies, and risk profiles. The selected funds therefore represent the effective population of schemes within these categories for which reliable and consistent data were available during the study period.

Variables

The study examines the factors influencing the growth of Assets under Management (AUM) in mutual funds. AUM growth serves as the dependent variable, representing the expansion of investor capital allocated to mutual funds.

Dependent Variable

Log (AUMGR) – The logarithm of AUM growth is used as the dependent variable to reduce skewness and stabilize variance in the distribution of asset growth across funds.

Independent Variables

CRISIL Rating (CRISILRAT) – This variable represents the fund rating assigned by CRISIL. Fund ratings act as informational signals summarizing performance consistency, risk characteristics, and managerial effectiveness.

Five-Year Return (5YR Ret) – This variable captures the historical performance of mutual funds over a five-year period. Prior literature suggests that investors often allocate capital based on past performance.

Log (Fund Size) – The natural logarithm of fund size is included to control for scale effects, as larger funds may benefit from reputation, visibility, and investor trust.

Expense Ratio (Exp Rat) – This variable measures the operating costs charged by mutual funds to investors. Higher expense ratios may influence investor allocation decisions by affecting net returns.

Empirical Model

To examine the determinants of AUM growth, the study employs a multiple linear regression model estimated using ordinary least squares (OLS). The model specification is as follows:

$$\text{Log}(AUMGR_i) = \beta_0 + \beta_1 CRISILRAT_i + \beta_2 RET5YR_i + \beta_3 \text{Log}(FUND_i) + \beta_4 EXPRAT_i + \epsilon_i$$

where:

Log (AUMGR) represents the logarithm of AUM growth,

CRISILRAT denotes the fund rating,

RET5YR indicates the five-year return,

Log (FUND) represents the logarithm of fund size,

EXPRAT refers to the expense ratio, and

ε is the error term.

Diagnostic Tests

To ensure the reliability of the regression results, several diagnostic tests were conducted. Variance Inflation Factor (VIF) statistics were calculated to assess potential multicollinearity among explanatory variables. The results indicate that VIF values remain well below the commonly accepted threshold, suggesting no serious multicollinearity concerns. Residual plots and normality diagnostics were also examined to evaluate the assumptions of the regression model. Additionally, Cook's distance statistics were inspected to detect potential influential observations. The results indicate that no observations exert undue influence on the regression estimates. These diagnostic procedures confirm the validity and robustness of the estimated regression model.

Ethical Considerations

The study doesn't employ any human volunteers and only uses secondary data from publicly accessible sources. Therefore, no ethical approval was required. Proper attribution has been given to all data sources used in the study.

Limitations of the Methodology

The study has several limitations in spite of its contributions. The analysis does not account for fluctuations over time because it is based on a cross-sectional data set. Furthermore, the sample

size is restricted to particular kinds of equity mutual funds, which can limit how broadly the results can be applied. These restrictions open up possibilities for further study with panel data and more funds categories.

Empirical Results

Descriptive Statistics

Table 1 presents the descriptive statistics for the variables used in the empirical analysis, including the logarithm of AUM growth (Log AUMGR), CRISIL ratings, five-year returns (5YR Ret), the logarithm of fund size (Log Fund), and the expense ratio (Exp Rat). The statistics are calculated from a sample **o**f 60 observations, and no missing values are present in the dataset.

The mean value of Log AUM growth is 1.25, with a median of 1.21 and a standard deviation of 0.307, indicating moderate variation in asset growth across the sampled mutual funds. The minimum and maximum values range from 0.55 to 1.96, suggesting noticeable differences in growth performance among funds. For CRISIL ratings, the average rating is 3.29, with values ranging between 1 and 5. The median rating of 3 indicates that most funds fall within the middle rating categories, reflecting moderate variation in perceived fund quality. The five-year return variable shows a mean of 19.0% with a standard deviation of 3.69, indicating variation in long-term performance among the funds. Returns range from 12.3% to 27.8%**,** highlighting differences in historical investment performance across the sample. The logarithm of fund size has a mean of 4.06 and a median of 4.11, with a standard deviation of 0.526**,** suggesting moderate dispersion in fund size across the selected schemes. Finally, the expense ratio has an average value of 0.715, with values ranging from 0.37 to 1.44. The relatively small standard deviation (**0**.233) indicates limited variation in expense ratios among the sampled mutual funds. Overall, the descriptive statistics suggest that while mutual funds in the sample exhibit noticeable variation in performance, ratings, and asset growth, the dispersion of the explanatory variables remains within reasonable bounds for regression analysis.

Table 1. Descriptive Statistics

	Log (AUMGR)	CRISILRAT	5YR Ret	Log (Fund)	Exp Rat
N	60	60	60	60	60
Missing	0	0	0	0	0
Mean	1.25	3.29	19.0	4.06	0.715
Median	1.21	3.00	19.0	4.11	0.670
Standard deviation	0.307	0.955	3.69	0.526	0.233
Minimum	0.55	1	12.3	2.54	0.370
Maximum	1.96	5	27.8	5.13	1.44

Analysis of Correlation Coefficient

A Pearson correlation analysis was conducted to examine the bivariate relationships among AUM growth and the key explanatory variables, including fund ratings, past performance, fund size, and expense ratio.

The results indicate a strong and statistically significant positive correlation between AUM growth and CRISIL fund ratings ($r = 0.646$, $p < 0.001$). This suggests that higher-rated funds tend to experience greater growth in assets under management, highlighting the importance of

third-party ratings as a signal of fund quality. Similarly, AUM growth is positively and significantly correlated with five-year returns ($r = 0.550$, $p < 0.001$), indicating that funds with better historical performance attract higher investor inflows. This finding provides preliminary support for the performance-chasing behavior of investors.

In contrast, the correlation between fund size and AUM growth is positive but statistically insignificant ($r = 0.213$, $p = 0.182$), suggesting that fund size alone does not have a strong linear association with growth in assets. The expense ratio exhibits a negative but statistically insignificant correlation with AUM growth ($r = -0.257$, $p = 0.105$). This implies that although higher expenses may be associated with lower fund growth, the relationship is not strong enough to be statistically meaningful.

With respect to interrelationships among independent variables, the correlations are generally low and statistically insignificant. For instance, the correlation between CRISIL ratings and five-year returns is weak ($r = 0.178$, $p = 0.267$), indicating that ratings and performance capture different aspects of fund characteristics.

Importantly, the magnitude of correlations among the independent variables remains below commonly accepted thresholds, indicating the absence of serious multicollinearity concerns. This is further corroborated by the variance inflation factor (VIF) diagnostics reported in the regression results. Overall, the correlation analysis provides preliminary support for the hypothesised relationships and confirms the suitability of the variables for inclusion in the multiple regression model (Sirri & Tufano, 1998; Berk & Green, 2008). These preliminary findings are further examined using multivariate regression analysis in the following section.

Table 2. Correlation Analysis

		Log(AUMGR)	CRISIL	5Yr Rating	Log(fund)	Expense Ratio
Log(AUMGR)	**Pearson's r**	—				
	df	—				
	p-value	—				
	95% CI Upper	—				
	95% CI Lower	—				
CRISIL	**Pearson's r**	0.646***	—			
	df	58	—			
	p-value	<.001	—			
	95% CI Upper	0.796	—			
	95% CI Lower	0.423	—			
5Yr Rating	**Pearson's r**	0.550***	0.178	—		
	df	58	58	—		
	p-value	<.001	0.267	—		
	95% CI Upper	0.733	0.460	—		
	95% CI Lower	0.291	-0.138	—		
Log(fund)	**Pearson's r**	0.213	0.152	0.170	—	
	df	58	58	58	—	
	p-value	0.182	0.344	0.287	—	

	95% CI Upper	0.488	0.439	0.454	—	
	95% CI Lower	-0.101	-0.164	-0.145	—	
Expense Ratio	**Pearson's r**	-0.257	-0.163	-0.224	-0.240	—
	df	58	58	58	58	—
	p-value	0.105	0.309	0.159	0.131	—
	95% CI Upper	0.055	0.152	0.089	0.073	—
	95% CI Lower	-0.523	-0.448	-0.498	-0.510	—

***p<0.01, **p<0.05, *p<0.1

Multiple Regression Analysis

A multiple regression model was estimated to examine the determinants of Assets Under Management (AUM) growth among equity mutual funds. The dependent variable in the baseline specification is the logarithm of AUM growth, while the independent variables include fund ratings provided by CRISIL, five-year fund returns, fund size, and the expense ratio.

The regression results indicate that the overall model explains a substantial proportion of the variation in AUM growth, with an R^2 value of 0.619, suggesting that approximately 61.9% of the variation in AUM growth across the sampled funds is explained by the explanatory variables included in the model. Among the explanatory variables, five-year return shows a positive and statistically significant relationship with AUM growth ($\beta = 0.0358$, $p < .001$). This finding suggests that funds delivering stronger historical returns tend to attract greater investor inflows. Similarly, CRISIL ratings exhibit a positive and statistically significant effect on AUM growth ($\beta = 0.1782$, $p < .001$), indicating that higher-rated funds experience stronger asset expansion.

In contrast, fund size and expense ratio do not demonstrate statistically significant effects in the baseline regression. The expense ratio shows a negative but insignificant coefficient, suggesting that cost considerations may not strongly influence investor allocation decisions once performance and ratings are taken into account.

Table 3. Determinants of log(AUM Growth): Multiple Regression Results

Variables	Estimate	Std. Error	t-value	p-value
CRISIL Rating	0.178	0.034***	5.229	<0.001
5-Year Return	0.036	0.009***	4.014	<0.001
Log-Fund Size	0.024	0.063	0.382	0.705
Expense Ratio	-0.079	0.143	-0.554	0.583
Constant	-0.055	0.341	-0.160	0.874

Model statistics:

R = 0.7867, Adjusted $R^2 = 0.619$

F-statistic = 22.6***

Observations = 60

Notes:

Standard errors are reported in parentheses.

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.10$.

Rebustness Check

To assess the robustness of the findings, an alternative regression specification was estimated using AUM growth without logarithmic transformation as the dependent variable. The results

remain broadly consistent with the baseline model. Five-year return and CRISIL ratings continue to exhibit positive and significant relationships with AUM growth, while the expense ratio remains statistically insignificant. In this alternative specification, fund size becomes statistically significant, suggesting that larger funds may benefit from visibility and reputational advantages in attracting investor inflows. The consistency of results across alternative model specifications strengthens the robustness of the empirical findings.

Diagnostic Test

Table 4. Cook's Distance

			Range	
Mean	**Median**	**SD**	**Min**	**Max**
0.0292	0.00918	0.0583	1.82e-6	0.311

Table 5. Multicollinearity Test

	VIF	Tolerance
EPR	1.11	0.898
LFUND	1.09	0.919
5YRT	1.09	0.918
CRISIL	1.06	0.943

Diagnostic tests were conducted to assess the validity of the regression model. The Variance Inflation Factor (VIF) values range between 1.06 and 1.11, indicating that multicollinearity is not present among the explanatory variables. The Shapiro–Wilk test ($p = 0.099$) confirms that the residuals are approximately normally distributed. Cook's distance statistics were examined to identify potential influential observations in the regression model. The maximum Cook's distance value (0.311) is well below the commonly accepted threshold of 1, indicating that no individual observation exerts an undue influence on the regression estimates. Furthermore, the Q–Q plot of residuals indicates that the assumption of normality is reasonably satisfied, while residual diagnostics do not reveal evidence of heteroskedasticity. Diagnostics plots are added in Appendix A.

Discussion

This study examines the determinants of Assets Under Management (AUM) growth in Indian mutual funds by integrating insights from Signaling Theory, the fund flow–performance literature, and Behavioural Finance. The empirical findings indicate that investor capital allocation in the Indian mutual fund market is primarily influenced by informational signals and past performance rather than by cost considerations.

The positive and statistically significant effect of fund ratings provided by CRISIL highlights the importance of signaling mechanisms in environments characterised by information asymmetry. In a retail-dominated investment environment such as India, third-party ratings appear to function as credible and easily interpretable indicators of fund quality. These ratings condense complex information regarding performance consistency, risk exposure, and managerial competence into simplified signals that investors can readily interpret. As a result, higher-rated funds tend to attract stronger capital inflows and experience faster growth in assets under management. This finding is consistent with signaling theory and supports prior evidence that external certifications and ratings influence mutual fund flows beyond raw performance

indicators. The results also reveal a strong and positive relationship between historical performance and AUM growth. The statistical significance of five-year returns suggests that investors allocate capital toward funds that demonstrate sustained performance over longer periods. This finding supports the fund flow–performance hypothesis, which posits that investors often extrapolate historical returns when making allocation decisions. Such behaviour reflects performance-chasing tendencies that have been widely documented in the mutual fund literature. While this behaviour may reward skilled fund managers in the short run, it may also expose investors to the risk of return mean reversion if past performance is interpreted as a reliable predictor of future outcomes.

The role of fund size in influencing AUM growth appears to be more nuanced. In the baseline model using logarithmic AUM growth, fund size does not exhibit a statistically significant effect. However, in the robustness specification using non-logarithmic AUM growth, fund size becomes positive and statistically significant. This suggests that larger funds may benefit from visibility and reputational advantages that enhance investor confidence. From a behavioural perspective, investors may display familiarity bias and limited attention, favouring well-known funds that appear more established and stable. These dynamics imply that scale and visibility can contribute to cumulative advantage effects, whereby larger funds continue to attract inflows due to their stronger market presence.

In contrast, the expense ratio does not exhibit a statistically significant relationship with AUM growth across model specifications. This finding indicates that investors may underweight cost considerations when allocating capital among mutual funds. Although higher fees are theoretically expected to discourage inflows, the empirical evidence suggests that investors place greater emphasis on salient signals such as ratings and past performance. This pattern is consistent with behavioural finance explanations of bounded rationality and limited attention, according to which investors rely on simplified cues when evaluating complex financial products.

Overall, the findings suggest that the growth dynamics of mutual funds in India are driven primarily by perceived quality, reputation, and sustained performance rather than strict cost efficiency. Informational signals provided by rating agencies and observable performance indicators appear to play a central role in shaping investor behaviour in an emerging market environment characterised by information asymmetry and heterogeneous financial literacy.

Conclusion

This study investigates the determinants of Assets Under Management (AUM) growth in Indian mutual funds by integrating insights from Signaling Theory, the fund flow–performance literature, and Behavioural Finance. Using a sample of open-ended equity mutual funds and applying multiple regression analysis, the study examines how fund ratings, historical performance, fund size, and expense ratios influence investor capital allocation in an emerging market context.

The empirical results provide strong evidence that information signals and past performance are the primary drivers of AUM growth in the Indian mutual fund industry. Specifically, fund ratings provided by CRISIL show a positive and statistically significant impact on AUM growth, suggesting that third-party ratings serve as credible signals that help investors evaluate fund quality under conditions of information asymmetry. Similarly, long-term historical performance, measured by five-year returns, exhibits a strong positive relationship with AUM growth, indicating that investors tend to allocate capital toward funds with sustained performance records.

The results further suggest that fund size may contribute to asset growth through visibility and reputation effects, particularly in the robustness specification. Larger funds may benefit from brand recognition, broader distribution networks, and stronger investor familiarity, which can

enhance investor confidence and attract additional inflows. In contrast, the expense ratio does not show a statistically significant effect on AUM growth, indicating that cost considerations play a relatively limited role in investor decision-making once performance and ratings are taken into account.

Overall, the findings highlight that mutual fund growth in India is shaped more by perceived quality, reputation, and performance signals than by strict cost efficiency. These results contribute to the literature on mutual fund flows by providing evidence from an emerging market where retail investors dominate and informational frictions remain significant

Policy Implications

The findings of this study carry several important implications for regulators, fund managers, and investors in emerging financial markets.

First, the strong influence of fund ratings on AUM growth highlights the critical role of credible information intermediaries in reducing information asymmetry in capital markets. Regulators should therefore ensure transparency, accountability, and methodological consistency among rating agencies such as CRISIL. Strengthening oversight mechanisms and disclosure standards can help maintain investor confidence in rating systems and improve the quality of information available to retail investors.

Second, the evidence that investors rely heavily on historical performance suggests the need for enhanced investor education initiatives. While past performance may provide useful information about fund management quality, it does not necessarily guarantee future returns. Regulatory bodies such as Securities and Exchange Board of India may therefore consider expanding investor awareness programs that emphasise the importance of diversification, risk assessment, and long-term investment strategies.

Third, the limited impact of expense ratios on investor allocation decisions raises concerns about cost awareness among retail investors**.** Investors may overlook fee structures when selecting mutual funds, potentially leading to sub-optimal investment outcomes over the long term. Policymakers and regulators may address this issue by improving the visibility and comparability of fee disclosures, ensuring that expense ratios are clearly communicated in investor-facing documents.

Finally, the potential influence of fund size on asset growth suggests that market concentration effects may emerge as larger funds continue to attract disproportionate inflows due to visibility and reputational advantages. Regulators should therefore monitor industry concentration and ensure that competitive conditions are maintained within the asset management sector.

Limitations and Future Research

Although this study provides important insights into the determinants of AUM growth in Indian mutual funds, several limitations should be acknowledged. The analysis is based on a relatively modest sample of equity mutual funds and focuses on a specific set of explanatory variables. Future research may extend the analysis by incorporating larger panel datasets, examining additional behavioural factors influencing investor decisions, and exploring the dynamic relationship between performance signals and fund flows across different market conditions.

Overall, this study advances emerging market finance research by demonstrating how information signals and behavioural biases jointly shape mutual fund capital allocation in a retail-dominated market.

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Appendix A: Diagnostics Plot

Figure A1: Residuals vs Fitted

Figure A1 presents the residuals versus fitted values plot for the regression model. The residuals appear randomly scattered around zero with no clear systematic pattern, indicating that the assumption of homoscedasticity is reasonably satisfied.

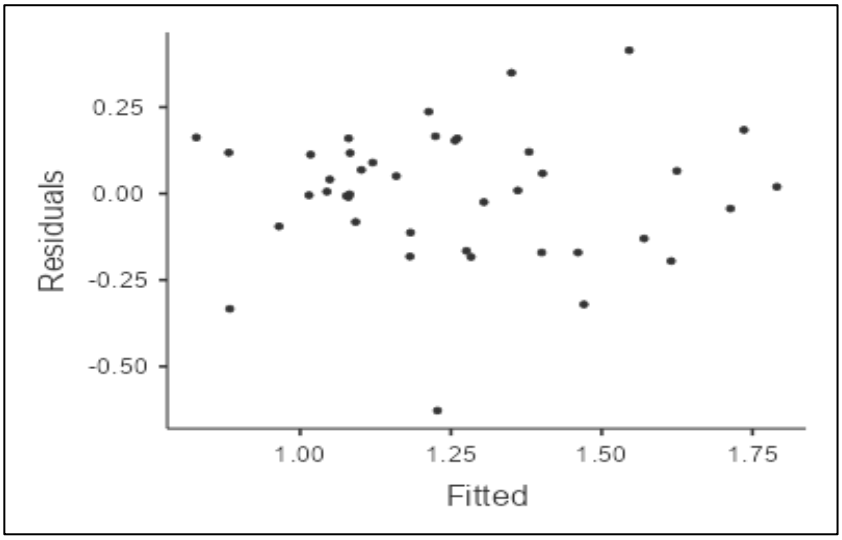
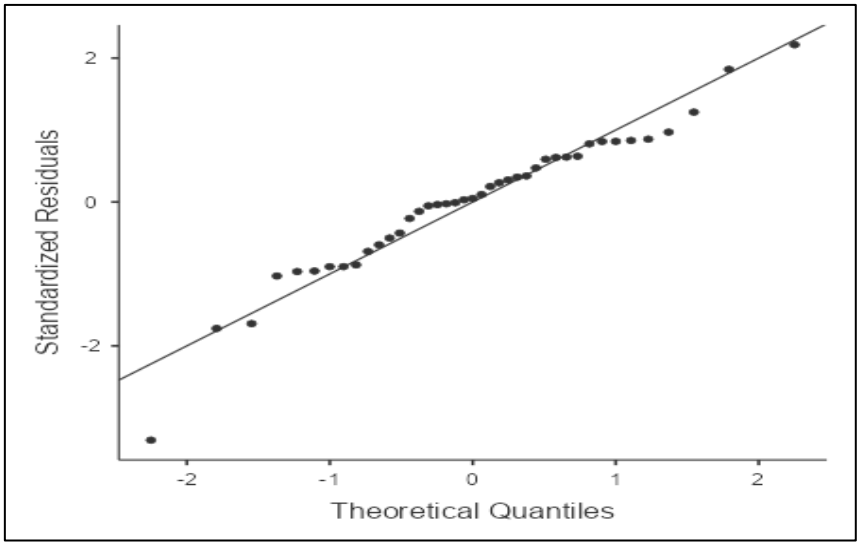


Figure A2: Normal Q-Q Plots of Residuals

Figure A2 shows the normal Q–Q plot of standardized residuals. The observations lie approximately along the 45-degree reference line, suggesting that the residuals are normally distributed.

Q-Q Plot