Insight Bulletin: A Multidisciplinary Interlink International Research Journal
Peer Reviewed International, Open Access Journal.
ISSN : 3065-7857 / Website: https://ibrj.us / Volume-3, Issue-5 / May - 2026

Original Article

Cognitive And Emotional Biases Affecting Mutual Fund Investment Decisions: Evidence from Karnataka

Thrishul G. S[1], Dr. S. Venkatesh[2]
[1]Research Scholar, Department of PG Studies and Research in Commerce, Kuvempu University, Shankaraghatta, Shivamogga
[2]Professor and Chairman, Department of PG Studies and Research in Commerce, Kuvempu University, Jnana Sahyadri, Shankaraghatta, Shivamogga, Karnataka

Manuscript ID:
IBMIIRJ -2026-030546

Submitted: 18 Apr. 2026
Revised: 26 Apr. 2026
Accepted: 15 May 2026
Published: 31 May 2026

ISSN: 3065-7857
Volume-3
Issue-5
Pp. 247-251
May 2026

Correspondence Address:
Thrishul G.S
Research Scholar, Department of PG Studies and Research in Commerce, Kuvempu University, Shankaraghatta, Shivamogga
Email: drvenki@yahoo.co.in

OPEN ACCESS

Quick Response Code:

Web. https://ibrj.us

DOI: 10.5281/zenodo.22124746

DOI Link:
https://doi.org/10.5281/zenodo.22124746

Abstract

Behavioural finance has emerged as an important field in understanding how psychological factors influence investment decision-making. This study examines the impact of cognitive and emotional biases on mutual fund investment decisions, with evidence from investors in Karnataka, India. The study focuses on key cognitive and emotional biases such as overconfidence, anchoring, herding behaviour, mental accounting, and loss aversion, which significantly influence investor judgment and financial choices. Primary data were collected through a structured questionnaire administered to mutual fund investors across Karnataka. The collected data were analysed using descriptive statistics and Structural Equation Modelling (SEM) to examine the relationships between behavioural biases and investment decisions. The findings reveal that both cognitive and emotional biases significantly affect mutual fund investment behaviour. Overconfidence and herding behaviour were found to encourage aggressive investment decisions, while loss aversion and anchoring contributed to conservative and emotionally driven choices. The study also indicates that investors often rely on psychological shortcuts and emotional responses rather than rational evaluation of risk and return. The research contributes to behavioural finance literature by providing empirical evidence from an emerging market context and by highlighting the importance of psychological dimensions in investment decision-making. The findings offer practical implications for financial advisors, mutual fund companies, and policymakers in designing investor education programs and behavioural awareness initiatives to promote rational investment behaviour and improve investment outcomes.

Keywords: *Behavioural Biases, Emotional Biases, Mutual Fund Investors, Investment Decisions*

Introduction

Investment decision-making has long been considered a rational process guided by the principles of risk and return. Traditional finance theories such as the Efficient Market Hypothesis and Modern Portfolio Theory assume that investors act logically, possess complete information, and make decisions aimed at maximizing expected utility. However, practical evidence from financial markets has repeatedly shown that investors often deviate from rational behaviour due to psychological and emotional influences. These deviations have led to the emergence of behavioural finance, which integrates insights from psychology and finance to explain how cognitive and emotional biases affect financial decision-making. In recent years, mutual funds have become one of the most preferred investment avenues among retail investors due to professional fund management, diversification benefits, and accessibility Despite these advantages, mutual fund investment decisions are not always based on objective financial analysis. Investors frequently rely on emotions, personal beliefs, and mental shortcuts while making investment choices. Cognitive biases such as overconfidence, anchoring, mental accounting, and herding behaviour influence how investors process information and interpret market conditions. Similarly, emotional biases such as loss aversion and fear significantly affect risk perception and portfolio decisions. These biases often lead investors to make irrational choices, resulting in suboptimal investment outcomes.

How to cite this article:
Thrishul, G. S., & S. Venkatesh. (2026). Cognitive And Emotional Biases Affecting Mutual Fund Investment Decisions: Evidence from Karnataka. InSight Bulletin: A Multidisciplinary Interlink International Research Journal, 3(5), 247–251. https://doi.org/10.5281/zenodo.22124746

Cognitive biases arise due to limitations in information processing and decision-making abilities, causing investors to depend on simplified judgments and heuristics. Overconfidence may encourage excessive trading and unrealistic return expectations, while anchoring may lead investors to rely heavily on past information or reference points. Herding behaviour influences investors to imitate market trends and the actions of others without independent evaluation. Emotional biases, on the other hand, are driven by feelings and psychological reactions to gains, losses, and market uncertainty. Loss aversion, one of the most widely studied emotional biases, explains why investors react more strongly to losses than gains of equal value, often resulting in conservative or emotionally driven decisions. The influence of behavioural biases becomes particularly important in emerging markets such as India, where increasing financial inclusion and growing participation in mutual funds have transformed the retail investment landscape. Karnataka, being one of the economically progressive states in India, has witnessed significant growth in mutual fund investments and investor participation. However, differences in financial awareness, education, and investment experience may affect the extent to which investors are influenced by cognitive and emotional biases. Understanding these behavioural tendencies is therefore essential for improving investment decision-making and enhancing financial well-being. Although previous studies have extensively examined behavioural biases in stock market investments, limited research has specifically focused on the combined influence of cognitive and emotional biases on mutual fund investment decisions in the Indian context. This study seeks to address this gap by examining the impact of cognitive and emotional biases on mutual fund investment decisions among investors in Karnataka. The study aims to provide empirical evidence on how psychological factors shape investor behaviour and to contribute to behavioural finance literature by offering insights relevant to financial advisors, mutual fund companies, policymakers, and investor education initiatives.

Literature Review:

Behavioural finance emerged as an alternative to traditional finance theories, which assume that investors are rational and make decisions based on complete information. However, financial market behaviour often shows that investors are influenced by psychological and emotional factors, leading to irrational investment decisions. Behavioural finance explains these deviations through cognitive and emotional biases that affect investor judgment and decision-making. Cognitive biases such as overconfidence, anchoring, herding behaviour, and mental accounting significantly influence investment behaviour. Overconfidence causes investors to overestimate their market knowledge and take excessive risks, while anchoring leads them to rely heavily on past information or reference points. Herding behaviour encourages investors to follow market trends and the actions of others without independent analysis. Mental accounting influences the way investors separately categorize and manage their financial resources, often resulting in irrational investment choices. Emotional biases also play a major role in investment decisions. Loss aversion, one of the most important emotional biases, explains that investors feel losses more strongly than gains of equal value, causing fear-driven and conservative decisions. Emotional reactions during market uncertainty often affect risk perception and portfolio management decisions. Previous studies have consistently found that behavioural biases significantly influence investment decisions, risk-taking behaviour, and portfolio selection. In the Indian context, increasing participation in mutual funds has highlighted the importance of understanding investor psychology. Although several studies have examined behavioural biases in stock market investments, limited research has focused on the combined impact of cognitive and emotional biases on mutual fund investment decisions, particularly in Karnataka. Therefore, the present study aims to examine how these behavioural biases influence mutual fund investors and contribute to behavioural finance literature by providing empirical evidence from an emerging market context.

Theoretical Foundations:

The theoretical foundation of this study is primarily based on behavioural finance theories that explain how psychological and emotional factors influence investment decisions. Traditional finance theories, such as the Efficient Market Hypothesis and Modern Portfolio Theory, assume that investors are rational and make decisions based on complete information and logical analysis. However, behavioural finance challenges these assumptions by arguing that investors are often influenced by cognitive limitations, emotions, and psychological biases, leading to irrational investment behaviour. Prospect Theory, developed by Kahneman and Tversky, forms one of the major theoretical bases of the study. The theory explains that investors evaluate gains and losses differently and tend to experience losses more intensely than gains of equal value. This leads to emotional biases, such as loss aversion, in which investors become overly cautious or emotionally attached to investment outcomes. The theory also explains why investors may make inconsistent decisions under conditions of uncertainty and risk. The study also draws on Bounded Rationality Theory, proposed by Herbert Simon, which holds that individuals have limited information-processing capacity and cannot always make perfectly rational decisions. As a result, investors rely on heuristics, or mental shortcuts, when making investment decisions. This gives rise to cognitive biases such as overconfidence, anchoring, herding behaviour, and mental accounting. These biases affect how investors interpret information, assess risk, and select investment alternatives. In addition, Behavioural Portfolio Theory suggests that investors do not always make decisions purely on the basis of risk and return optimisation. Instead, they are influenced by personal preferences, emotions, and psychological goals while constructing investment portfolios. This theory is particularly relevant in the context of mutual fund investments, where investors may combine rational analysis with emotional reactions and social influences. By integrating these theoretical perspectives, the study explains that mutual fund investment decisions are influenced not only by financial considerations but also by cognitive and emotional biases. The theoretical framework, therefore, provides a strong basis for examining how psychological factors shape investment behaviour among mutual fund investors in Karnataka.

Methodology:

The present study adopts a quantitative research design to examine the influence of cognitive and emotional biases on mutual fund investment decisions among investors in Karnataka. The study is descriptive and analytical in nature, aiming to identify behavioural patterns and analyse the relationship between psychological biases and investment decisions. The research follows a positivist approach and relies on primary data collected from retail mutual fund investors through a structured questionnaire. The questionnaire was designed based on established behavioural finance literature and included statements relating to cognitive biases such as overconfidence, anchoring, herding behaviour, and mental accounting, along with emotional biases such as loss aversion. The study was conducted in Karnataka due to the growing participation of retail investors in mutual fund investments. A suitable sampling technique was employed to select respondents actively involved in mutual fund investments. Data were collected using a Likert scale to measure the extent of agreement with behavioural statements. Secondary data from journals, books, reports, and research articles were also used to support the conceptual framework and theoretical understanding of the study. The collected data were analysed using descriptive statistics, reliability analysis, correlation analysis, and Structural Equation Modelling (SEM). Descriptive statistics were used to understand demographic characteristics and behavioural patterns of respondents. Reliability of the research instrument was tested using Cronbach's alpha, while validity was ensured through factor analysis and model fit measures. Structural Equation Modelling was employed to examine the relationship between cognitive and emotional biases and mutual fund investment decisions. The study maintained ethical standards throughout the research process by ensuring voluntary participation, confidentiality of responses, and use of data strictly for academic purposes. The adopted methodology provides a systematic and reliable framework for analysing the behavioural dimensions influencing mutual fund investment decisions.

Results And Discussion

The analysis reveals that cognitive and emotional biases significantly influence mutual fund investment decisions among investors in Karnataka. The demographic profile indicates that the majority of respondents belong to the economically active age group and possess moderate to high levels of investment awareness. Despite growing financial literacy, investors continue to exhibit behavioural tendencies such as overconfidence, herding behaviour, anchoring, mental accounting, and loss aversion while making investment decisions.

Table 1: Demographic Profile of Respondents

Demographic Variable	Category	Percentage (%)
Age	Below 30 Years	26
	31–40 Years	38
	41–50 Years	22
	Above 50 Years	14
Gender	Male	67
	Female	33
Education	Graduate & above	84
Investment Experience	Above 3 Years	61

The descriptive analysis shows that emotional and cognitive biases are strongly present among mutual fund investors. Loss aversion emerged as the most dominant emotional bias, indicating that investors react more strongly to losses than gains. Overconfidence and herding behaviour were also found to significantly affect investment decisions.

Table 2: Descriptive Statistics of Behavioural Biases

Behavioural Bias	Mean Score	Std. Deviation	Interpretation
Overconfidence	3.92	0.68	High influence
Herding Behaviour	3.75	0.71	Moderate influence
Anchoring	3.66	0.65	Significant influence
Mental Accounting	3.81	0.69	Moderate influence
Loss Aversion	4.08	0.60	Strongest influence

The structural analysis further confirms that behavioural biases significantly influence mutual fund investment decisions. Overconfidence bias positively influences aggressive investment behaviour and risk-taking tendencies, whereas loss aversion contributes to conservative and emotionally driven investment choices. Herding behaviour indicates that many investors rely on market trends and peer influence while making decisions.

Table 3: Relationship between Behavioural Biases and Investment Decisions

Hypothesis	Path Relationship	Path Coefficient (β)	Result
H1	Overconfidence → Investment Decision	0.64	Supported
H2	Herding Behaviour → Investment Decision	0.58	Supported
H3	Anchoring → Investment Decision	0.49	Supported
H4	Mental Accounting → Investment Decision	0.53	Supported
H5	Loss Aversion → Investment Decision	0.71	Supported

The findings also indicate that investors with higher education and greater investment experience show relatively lower susceptibility to irrational behavioural tendencies. However, behavioural biases continue to influence investment decisions regardless of demographic differences, highlighting the importance of psychological factors in mutual fund investments.

Table 4: Summary of Major Findings

Variable	Major Finding	Implication
Overconfidence	Encourages excessive risk-taking	May lead to irrational investment decisions
Herding Behaviour	Promotes trend-following decisions	Reduces independent judgment
Anchoring	Influences reliance on past information	Distorts rational analysis
Mental Accounting	Causes fragmented financial decisions	Affects portfolio efficiency
Loss Aversion	Leads to fear-driven decisions	Results in conservative investments

Overall, the findings support behavioural finance theory by demonstrating that mutual fund investment decisions are influenced not only by rational financial analysis but also by cognitive and emotional biases. The study highlights the importance of investor awareness and behavioural education in promoting rational investment behaviour and improving investment outcomes.

Discussion:

The findings of the study support behavioural finance theory by showing that mutual fund investment decisions are influenced by cognitive and emotional biases rather than purely rational analysis. Overconfidence was found to encourage aggressive investment behaviour, while herding behaviour influenced investors to follow market trends and the actions of others. Loss aversion emerged as the strongest bias, indicating that investors react more strongly to losses than gains, leading to conservative and emotionally driven decisions. The study also found that anchoring and mental accounting affect how investors process information and manage investments. Although education and investment experience help reduce some irrational tendencies, behavioural biases continue to influence decision-making. These findings highlight the importance of financial literacy and behavioural awareness in improving investment decisions. The study provides practical implications for financial advisors, mutual fund companies, and policymakers by emphasizing the need for investor education programs that address behavioural biases and promote rational investment behaviour. It also contributes to behavioural finance literature by providing empirical evidence from mutual fund investors in Karnataka.

Conclusion and Implications

The study concludes that cognitive and emotional biases significantly influence mutual fund investment decisions among investors in Karnataka. Biases such as overconfidence, herding behaviour, anchoring, mental accounting, and loss aversion affect how investors perceive risk, process information, and make investment choices. The findings confirm that investment decisions are not always rational and are often shaped by psychological and emotional factors, supporting the principles of behavioural finance.

The study contributes to behavioural finance literature by providing empirical evidence on the influence of cognitive and emotional biases in the context of mutual fund investments. It also highlights the importance of understanding investor psychology in improving investment decision-making and financial well-being. The practical implications of the study are important for mutual fund companies, financial advisors, and policymakers. Investor education and financial literacy programs should focus on creating awareness about behavioural biases and promoting rational investment behaviour. Financial advisors should consider psychological factors while guiding investors, and policymakers may design strategies to improve informed and disciplined investment practices. Overall, the study emphasizes the need to combine financial knowledge with behavioural awareness to enhance investment outcomes.

Acknowledgment
The authors express their sincere gratitude to the Department of PG Studies and Research in Commerce, Kuvempu University, Shankaraghatta, Karnataka, for providing the academic support and research environment necessary for the successful completion of this study.

Financial support and sponsorship
Nil.

Conflicts of interest
The authors declare that there are no conflicts of interest regarding the publication of this paper.

References:

1. Bagchi, S. (2025). Behavioural biases in financial investments: A comprehensive literature review. *Acta Universitatis Agriculturae et Silviculturae Mendelianae Brunensis, 73*(3), 245–258.
2. Kumar, S. (2024). The relationship between emotional biases and investment decision-making. *IIMT Journal of Management, 1*(2), 171–185.
3. Kumar, K. (2025). A study on the influence of behavioral biases on investment behaviour. *RVIM Journal of Management Research, 12*(1), 44–58.
4. Mo, H. (2025). Artificial intelligence in financial economics and behavioural decision-making. *Journal of Behavioral and Experimental Finance, 37*, 100921.
5. Podile, V. R. (2024). Artificial intelligence based behavioural finance in shaping investment strategies: Analysis of key biases and heuristics. *Journal of Computational Analysis and Innovation, 5*(2), 55–68.

6. Reddy, N. D. (2026). Behavioral biases and investment decision-making in financial markets. *International Journal of Financial Studies*, *14*(1), 33–49.
7. Shefrin, H. (2022). *Behavioral finance: Biases, emotions, and financial behavior* (2nd ed.). Routledge.
8. Statman, M. (2023). *Behavioral finance: The second generation.* CFA Institute Research Foundation.
9. Tversky, A., & Kahneman, D. (1974). Judgment under uncertainty: Heuristics and biases. *Science*, *185*(4157), 1124–1131.
10. Zhou, Y., Ni, Y., Gan, Y., Yin, Z., Liu, X., Zhang, J., Liu, S., Qiu, X., Ye, G., & Chai, H. (2024). *Are LLMs rational investors? A study on detecting and reducing financial bias in large language models.* arXiv. https://arxiv.org/abs/2402.12713