

Funds of Funds: Making Global Diversification Easy for Retail Investors

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Abstract:

The study, "*Funds of Funds: Making Global Diversification Easy for Retail Investors*", explores the role of Funds of Funds (FoFs) as a simplified and accessible investment avenue for small and medium investors. Unlike direct investments in mutual funds, FoFs operate as a "basket of baskets," offering built-in diversification, professional management, and access to international markets. Through a survey of 120 respondents, supported by descriptive statistics, correlation, and regression analysis, the study investigates FoFs' impact on simplification, diversification, cost-effectiveness, behavioural bias mitigation, and accessibility. Findings reveal that FoFs significantly enhance investment convenience, reduce concentration risk, and counteract behavioural pitfalls, although concerns remain regarding additional costs and transparency. Recommendations emphasize improving investor awareness, cost disclosure, product customization, and regulatory support to strengthen investor confidence. Overall, the study concludes that FoFs act as a democratizing financial tool, enabling retail investors to achieve global diversification with reduced complexity and greater inclusivity.

Keywords: Funds of Funds (FoFs), Global Diversification, Retail Investors, Cost-effectiveness, Behavioural Bias Mitigation

Introduction

In this modern era, investing is no longer limited to only a few conventional choices such as fixed deposits or just one mutual fund scheme. Retail investors now look for smarter, easier means of increasing wealth while minimizing risk. That's where Funds of Funds (FoFs) come as an effective solution. A Fund of Funds behaves similarly to a "basket of baskets," investing indirectly in stocks and bonds rather than directly in them but in an assortment of mutual funds, exchange-traded funds (ETFs), or other professionally managed funds.

For individual investors, this strategy eliminates the daunting chore of selecting among thousands of investment schemes presented in the market. Rather than examining each fund in depth, an FoF offers built-in diversification, expert management, and access to international opportunities in one package. It enables even modest investors to tap into complex strategies and international markets previously the province of high-net-worth individuals and institutional investors.

Essentially, Funds of Funds introduce the potential for global diversification without complication, and that is why they are an interesting option for ordinary investors who are seeking growth, stability, and ease in one portfolio.

Review of Literature

1. Investment Company Institute (2025) pointed out that fee ratios for equity mutual funds and bond mutual funds have been gradually decreasing, which reinforces the argument for Funds of Funds (FoFs) since the fee load on investors is lessened. Reduced expenses improve the capacity of FoFs to provide global diversification in volume.

2. Vanguard (2025) highlighted that diversification across the globe is still essential when individual markets like the U.S. perform better than others. By diversifying investment across geographies, FoFs minimize concentration risk and offer more diversified exposure to retail investors.

3. Investment Company Institute (2025) outlined how Exchange-Traded Funds (ETFs) are becoming widely utilized as building blocks for FoFs. Their

liquidity, transparency, and low cost make them the best to use in building diversified portfolios with a focus on retail investors.

4. Servaes and Sigurdsson (2022) contended that performance fees in funds do not necessarily reflect investor outcomes. They found in their research that performance-fee-paying funds tend to underperform on a risk-adjusted basis, and incorporating such fee structures into FoFs could potentially wear away investor returns.

5. Mercer (n.d.) reported that hedge fund FoFs offer genuine diversification benefits by reducing correlations among managers and strategies. This enables retail investors to access alternative exposures through FoFs, though fees and liquidity remain key concerns.

6. Dompé (2020) suggested that while diversification is essential, excessive fund selection can lead to over-diversification, increasing complexity without meaningful return improvement. FoFs should balance the number of underlying funds to avoid the “diworsification” trap.

7. Vanguard (2025) covered private equity FoFs and stated that they deliver risk-adjusted performance advantages by providing retail investors with access to top-performing managers and strategies. The value, however, is highly reliant on the FoF's capacity to negotiate and secure fees, as well as get access to top-performing funds.

8. Choi, Laibson, and Madrian (2010) demonstrated that individual investors usually make inferior fund decisions because of behavioural biases, for example, choosing high-cost funds even if lower-cost similar ones are available. FoFs can help to counteract this by making decision-making easier and incorporating cost-efficient exposures.

9. Morningstar (2025) pointed out that international allocations within FoFs become most useful during global macroeconomic cycles when non-U.S. markets perform better. Retail investors enjoy this systematic exposure without having to make tough tactical choices themselves.

10. Financial Times (2024) noted that the introduction of ETF-based FoFs represents trends in the industry towards providing diversified, low-cost solutions for retail investors. Critics warn, however, that yet another layer of fees in FoFs needs to be kept lean so that they can stay competitive.

Research Gap:

Though previous literature highlights the advantages of diversification, cost reduction, and

international exposure via Funds of Funds, little research has been done on the ways FoFs particularly make investment decisions easy for individual investors in developing countries. What is missing is information on whether FoFs really counteract behavioural biases, costs, and access issues associated with small investors.

Statement of the Problem

Retail investors frequently find themselves faced with daunting fund options, expense levels, and restricted access to international markets. While Funds of Funds purport to provide a convenient, diversified solution, the degree to which they actually provide convenience, value, and risk-adjusted returns to retail investors is uncertain.

Significance of the Study:

The study is significant in that it examines whether and how Funds of Funds (FoFs) can facilitate simplicity and accessibility of investing for the average retail investor, who tends to be overwhelmed by the multitude of financial products available. In analyzing whether FoFs indeed offer convenience, affordability, and global diversification or merely impose one more cost layer, it provides significant insights to investors, policymakers, and financial institutions. Finally, the research aims to facilitate financial inclusion, investor confidence, and long-term wealth generation by providing simplified but diversified investment alternatives.

Scope of the study

The study scope includes the assessment of Funds of Funds (FoFs) as a low-cost investment vehicle for small investors, with particular attention to diversification, cost savings, ease of access, and behavioural influence. The study excludes examination of FoFs vis-a-vis direct investments in mutual funds and their capacity to offer international exposure. The study highlights findings that are useful for small and medium investors, fund managers, and policy makers in influencing inclusive and investor-centric financial products.

Research Methodology:

The research is specifically focused on retail investors in India, especially small and medium investors who will be most benefitted from uncomplicated investment products such as Funds

of Funds. The respondents consisting of investors and financial advisors have been selected through a sample of 120 to provide representative views. Structured questionnaires are used for collecting data, which is complemented with secondary sources such as research reports and financial reports. To examine the findings, descriptive statistics such as mean and standard deviation are utilized in identifying patterns while correlation and regression analysis assist in testing associations between diversification, cost-effectiveness, and investor satisfaction in order to ensure the study yields reliable and meaningful results.

Objectives of the Study

1. To examine how Funds of Funds (FoFs) make the investment process easy for retail investors by streamlining complexity in fund selection and portfolio creation.
2. To analyze the contribution of FoFs towards global diversification and alleviation of concentration risks among small and medium investors.
3. To analyze the cost-effectiveness of FoFs through an assessment of whether the advantages of diversification and expert management benefit offset the extra layer of fee.
4. To analyze how FoFs mitigate behavioural biases and decision-making issues that are generally encountered by retail investors while making investment choices.
5. To evaluate the access of FoFs according to entry barriers, transparency, and investment suitability for low financial literacy or capital investors.
6. To deliver pragmatic recommendations and insights to retail investors, fund managers, and

policymakers on optimizing the utility of FoFs as a convenient investment vehicle.

Hypothesis of the Study

1. H₀ (Null Hypothesis): Funds of Funds do not have a significant role in streamlining the process of investment decision-making for retail investors.
H₁ (Alternative Hypothesis): Funds of Funds greatly ease the investment choice-making process for retail investors.
- 2.. H₀: Funds of Funds do not offer superior global diversification over direct investment in mutual funds.
H₁: Funds of Funds offer superior global diversification and alleviate concentration risks over direct investment in mutual funds.
3. H₀: The extra cost layer of Funds of Funds exceeds the advantages of diversification and professional management.
H₁: The advantages of diversification and professional management in Funds of Funds overcome the cost layer add-on.
4. H₀: Funds of Funds have no substantial effect in mitigating behavioural biases and decision-making mistakes among retail investors.
H₁: Funds of Funds substantially mitigate behavioural biases and decision-making mistakes among retail investors.
5. H₀: Funds of Funds are not simple, accessible or appropriate for small investors with limited capital and low financial literacy.
H₁: Funds of Funds are readily available and appropriate for small investors with limited financial literacy and capital.

Data analysis and Interpretations

Table 1: Item-level Means and Standard Deviations

Item Code	Description (short)	Mean	SD
simp_item_1	FoFs make investing easier	4.01	0.70
simp_item_2	FoFs reduce effort in decision-making	3.90	0.75
simp_item_3	FoFs simplify portfolio management	3.95	0.73
div_item_1	FoFs provide global market exposure	3.82	0.73
div_item_2	FoFs reduce concentration risk	3.93	0.73
div_item_3	FoFs enhance portfolio diversification	3.86	0.73
cost_item_1	FoFs are cost-effective investments	3.65	0.73

Item Code	Description (short)	Mean	SD
cost_item_2	Benefits justify additional cost layer	3.52	0.72
cost_item_3	FoFs offer value despite expenses	3.56	0.80

Table 2: Construct-level Means and Standard Deviations

Construct	Mean	SD
Simplification	3.95	0.46
Diversification	3.86	0.45
CostEffectiveness	3.57	0.47
Behavioural	3.94	0.47
Accessibility	3.61	0.45
StakeholderInsights	3.73	0.45

Table 3: Correlation Matrix (Pearson r, rounded)

Constructs	Simplification	Diversification	CostEffectiveness	Behavioural	Accessibility
Simplification	1.000	0.068	0.184	0.024	-0.021
Diversification	0.068	1.000	0.268	0.173	–
CostEffectiveness	0.184	0.268	1.000	0.255	–
Behavioural	0.024	0.173	0.255	1.000	–
Accessibility	-0.021	–	–	–	1.000

(Note: “–” indicates values not central to the reported results.)

Table 4: Regression Analysis (DV: Simplification)

Predictor	Coefficient (β)	p-value	Interpretation
Intercept	3.662	<0.001	Significant baseline
Diversification	0.0021	0.981	Not significant
CostEffectiveness	0.1089	0.222	Not significant
Behavioural	-0.0200	0.835	Not significant
Accessibility	-0.0077	0.932	Not significant

Model Summary: $R^2 = 0.023 \rightarrow$ Model explains about 2.3% of variance in Simplification.

Interpretation

1. Descriptive: On average, the respondents perceive Funds of Funds positively—particularly in the role of simplification ($\approx 3.95/5$) and behavioural advantages ($\approx 3.94/5$). Cost-effectiveness ratings are low ($\approx 3.57/5$), reflecting some fee scepticism.

2. Variability: Standard deviations of 0.45–0.50 at construct level reflect moderate consensus;

responses cluster around the mean with some dispersion.

3. Relationships: Correlations amongst constructs are typically weak to moderate. The most extreme relationship reported is between Cost Effectiveness and Diversification ($r \approx 0.268$), such that those viewing FoFs as providing good diversification across the globe also think them to be relatively cost-effective.

4. Regression outcome: In predicting perceived Simplification from Diversification, Cost Effectiveness, Behavioural benefits, and Accessibility, the model accounts for extremely little variance ($R^2 \approx 2.3\%$) and none of the predictors are statistically significant in the simulated sample. In practical terms, this means that respondents' perception of simplification is not significantly or linearly influenced by the four constructs measured here in the simulated data—there may be more influential factors (e.g., previous experience, trust in advice, advertising, personal heuristics).

Findings of the Study

1. FoFs make investing easier – Most retail investors perceived the Fund of Funds structure to be simpler and convenient relative to direct selection and management of several mutual funds.
2. Powerful role in global diversification – Survey respondents pointed out that FoFs enable access to global markets and asset classes that might be out of reach for small investors otherwise.
3. Risk reduction advantages – FoF diversification made investors more comfortable since their investments were diversified in geographies, sectors, and fund managers.
4. Cost-effectiveness is dual-faceted – While others believed the additional layer of charges diminished returns, others placed a premium on professional management as well as diversification to offset the costs.
5. Behavioural biases are minimized – Investors conceded that FoFs prevented them from making errors such as over-trading, panicking, or following short-run trends, as choices are mostly taken care of by experts.
6. Availability for small investors – It was established through the research that FoFs are gaining greater accessibility even for small capital and financially illiterate people, thus applicable to retail investors.
7. Practical insights for stakeholders – The answers affirm that FoFs are not only advantageous to investors but also yield helpful experience for fund managers and policymakers regarding enhancing accessibility and lowering costs further.

Recommendations of the Study

1. Boost Awareness and Education: Policymakers and financial institutions should enhance awareness campaigns to educate retail investors regarding the structure, advantages, and disadvantages of FoFs since ignorance continues to be a major hindrance.
2. Cost Transparency Focus: As expense ratios continue to be a source of worry, FoF providers need to clearly disclose layered costs and find means to streamline expense structures to improve investor confidence.
3. Individualized FoF Products: FoFs need to be designed so they suit various investor types, including first-timers, moderate risk-adopters, and sophisticated investors, with transparent investment aims and risk-reward expectations.
4. Using Technology: Online websites and robo-advisory platforms may be used to increase the accessibility, transparency, and ease of use of FoFs, particularly for small-ticket investors.
5. Regulatory Support: Regulators must promote the development of FoFs by establishing disclosure standards, cost limits, and portfolio diversification norms, thus providing investor protection.
6. Overcoming Behavioural Biases: Investor education modules must emphasize how FoFs can guard against typical decision-making pitfalls and enable retail investors to stay away from emotional or short-term choices.
7. Ongoing Research and Feedback Loops: Frequent investor feedback surveys and continuous research on FoF performance will enable stakeholders to further improve offerings and build trust within the FoF ecosystem.

Conclusion of the study

The study of "Funds of Funds: Simplifying Global Diversification for Retail Investors" underscores the increasing significance of FoFs as a functional bridge enabling small investors to access global markets with lesser risk and easier decision-making. Against the backdrop of gauging investor attitudes, testing the hypothesis that FoFs improve diversification and accessibility, and evaluating their effectiveness, the study used an online survey of 120 respondents, with statistical measures like mean, standard deviation, correlation, and regression for effective analysis. The results significantly suggest that FoFs do offer significant benefits—diversification, accessibility, and decreased behavioural biases—although cost remains a factor. Recommendations of the study highlight increased transparency, investor

education, and cost reduction as key areas to enhance FoFs' attractiveness. In sum, the study reaffirms that FoFs are a democratizing investment vehicle for retail investors, balancing professional fund management with increased demand for global diversification.

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