

# Investors pour Rs 47,000 crore in midcap & small cap mutual funds in H1 CY25. What are they really chasing?

By Surbhi Khanna, Published on: July 11, 2025.



With investors' showing clear preference for midcap and small cap mutual funds by pouring Rs 47,000 crore in the first half of the current calendar year and the categories offering good returns, market experts are of the view that these inflows have been driven by higher trailing returns in recent years, and the fear of missing out (FOMO) may also be pushing investors to chase past performance.

"These returns may not always be backed by sustainable earnings growth and other fundamentals of the underlying companies and thus investors may need to be cautious. Also, past returns can result in mis-selling and pushing such funds easily to retail investors," Vishal Dhawan, CEO, Plan Ahead Wealth Advisors, a wealth management firm in Mumbai told ETMutualFunds.

Considering this as a concern, Dhawan mentioned that the current valuations in mid and small caps are well above historical averages, leaving little margin for error if earnings disappoint and also, based on trailing returns investors may enter with high return expectations, only to be disappointed if the segment underperforms or corrects.

In the first half of the current calendar year, mid cap funds received a total inflow of Rs 21,870 crore whereas small cap funds received an inflow of Rs 24,774 crore in the same period. Another expert cautions investors that they should invest in mid and small caps only with a slightly longer-term horizon compared to large caps and also be ready with slightly higher volatility given that these segments are trading at a higher valuation.

"We are not negative on mid and small caps. So, we are just saying that if you are coming into mid and small cap strategies, please do come with a slightly longer-term horizon compared to large caps and also be ready with slightly higher volatility given that they are trading at a higher valuation and that is what our view has been," Harsha Upadhyaya, CIO-Equity, Kotak AMC told ETNow.

As the categories are currently trading at a higher valuation and are receiving heavy inflows, Dhawan mentioned that investors often fall prey to herd mentality, chasing recent winners like small and mid-cap funds assuming past returns will be replicated in the future, the current forward valuations in the small and mid-cap space are still significantly above their long-term averages, therefore this space lacks valuation comfort, and these segments are more volatile and sensitive to earnings disappointments or any weak fundamentals.

Depending on one's risk appetite and investment horizon, allocation to small and mid-cap funds can range between 10% to 30% of the portfolio and the large-cap segment offers more reasonable valuations currently and can be a major part of the portfolio providing stability and downside protection, is what Dhawan advised.

Though midcap and small cap funds have been on the lower side of the return chart in the current calendar year so far (till June 30) but since April's low, mid cap funds have gained 20% and small caps have gained nearly 21%.

On April 7 the benchmark index was at the level of 73,137, the lowest in the current financial year so far.

After looking at the recent inflow trend, returns offered, and recent valuations in the mid cap and small cap categories, Dhawan recommends investors that a staggered investment approach through SIP or STP is wiser than a lumpsum.

While selective exposure to mid and small cap funds can still be beneficial for long-term goals, it's crucial to limit allocation based on risk profile and focus on consistent, disciplined investing rather than timing the market and selective allocation, backed by earnings visibility and reasonable valuations, may be key to navigating this space wisely, Dhawan added.

Many investors tend to follow the inflow trend and invest where others are investing and putting their money and the categories which are delivering high returns, which deviates them from their asset allocation and risk profile. Many experts always advise choosing a fund based on their risk appetite, investment horizon and goals and follow the trend.

In addition to this, Dhawan recommends that chasing inflow trends is never a wise strategy, such moves are often driven by FOMO, leading investors to enter at peak valuations and see downsides during corrections and inflows are not a reliable indicator for making investment decisions.

He adds that focusing on the long-term asset allocation and risk profile ensures that the portfolio is aligned with the goals and capacity to handle volatility.

“Staying disciplined avoids emotional, peer driven decisions and encourages better rebalancing and long-term wealth creation. A diversified approach offers far more stability than trend-chasing, especially in uncertain market phases,” Dhawan shared.

Post analysing the recent flow of returns and categories receiving inflows, Dhawan is of the opinion that the outlook for mid and small-cap funds remains cautious, and the future performance will be driven by earnings growth of the underlying businesses, which will indicate whether the current high valuations are justified by actual earnings and business growth.

“While long-term structural tailwinds remain fine, near-term corrections cannot be ruled out due to elevated valuations and recent developments such as geopolitical tensions, trade tariffs, and Wars,” he adds.