



Behavioural Finance: Understanding Investor behaviour and Decision Making

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ABSTRACT

This study examines how psychological and environmental factors influence investment decisions, revealing that investors often act irrationally due to biases such as overconfidence, herd behaviour, and loss aversion. By challenging the Efficient Market Hypothesis, which assumes all available information is processed by the market, the research highlights the limitations of predicting market patterns due to unknown variables. Using descriptive and explanatory research methods, the study analyses data from 151 Indian stock market investors, exploring the impact of demographic profiles, experience, and behavioural biases on investment decisions. Findings suggest that while age and experience do not significantly impact these biases, awareness of negative consequences plays a crucial role in decision-making. The research advocates for tailored financial education programs focusing on risk management and safe investment strategies, particularly for younger, well-educated investors. By understanding and mitigating the impact of behavioural biases, the study aims to improve investment strategies and market efficiency, providing valuable insights for financial practitioners and policymakers.

Keywords: Diversity, Equity, Inclusion, Organisation performance.

Introduction

Investments is one of the significant investment strategies for an individual. The behavioural patterns of investors are influenced by many factors. Many a times, the investors assume that their decisions are rational but understanding and predicting the investment patterns and behaviour of market is inevitable for profitable and visionary decisions. This study aims at developing strategies on predicting and designing effective strategies on behavioural patterns and understanding the behavioural factors. By studying and exploring these factors, the researcher can discover the most critical factors which would help the rational decisions of investors and financial practitioners. According to Barberis and Thaler (2003), "Behavioural finance is the study of how psychology affects financial decision-making and financial markets". Behavioural finance studies the psychological, cognitive and emotional bias on the investment decisions and also challenges the assumption that the investors are rationally deciding the financial decisions. This theory discovers the irrationality of individuals on financial decisions due to the psychological factors Behavioral finance, a study of how psychology affects financial decision-making and markets, challenges the assumption that investors are rational and reveals the irrationality of individuals' financial decisions due to psychological factors and environmental factors. This study aims to develop strategies for predicting and designing effective investment strategies based on behavioral patterns and understanding the psychological and environmental factors that influence investment decisions.

Statement of the problem

The Efficient Market Hypothesis (EMH) is a financial economics concept which emphasis that the financial market process all the available information for predicting market patterns but it is not possible to outperform the market performance since the unknown factors are too many as well as the time limitations for all the factors. It creates the chaos in the financial market decisions. The individuals are irrational on their investment decisions due to many psychological factors. These factors interact with investment strategies and decisions. Ultimately, predicting the behavioural factors become a challenge for financial practitioners and investors. Negative attitudes and behaviours in investors, such as overconfidence, herd behaviour, and loss aversion, further complicate investment decisions. These attitudes often lead to poor investment choices and market inefficiencies. Understanding these negative behaviours and their impact on investment decisions is crucial for developing strategies that can mitigate their adverse effects and improve overall market performance.

Objectives

- Identify and analyse the most prevalent behavioural biases among investors.

- Investigate the interplay between different biases and external factors in shaping investment decisions.
- Explore the influence of cultural, social, and economic variables on investor behaviour.

Scope

The scope of this study encompasses a comprehensive analysis of the psychological and environmental factors influencing investment decisions among individuals, with a particular focus on the behavioural biases that shape these decisions. By examining the interplay between these biases and external variables such as cultural, social, and economic influences, the research aims to provide a holistic understanding of investor behavior. The study's scope also includes an in-depth exploration of the demographic profiles of investors, their motivations for investing, and how these factors impact their decision-making processes. Through the application of statistical tools like ANOVA and regression analysis, the study seeks to identify the most critical behavioural factors that affect investment outcomes. This research will contribute valuable insights for financial practitioners, policymakers, and educators by informing the development of strategies and programs that promote more rational and effective investment decisions, ultimately enhancing market efficiency.

Research Methodology

In this study, "Descriptive and Explanatory research" methods were employed. Descriptive research was used to summarize the findings related to the research question and to capture the behaviors and characteristics of the respondents. Explanatory research was chosen to investigate and validate the hypotheses formulated by the researchers. This approach aims to systematically provide evidence supporting the initial hypotheses about the causes and relationships underlying the investors decision making. Quantitative study as a research approach that seeks to explain a situation by collecting and analysing numerical data using statistical methods. The primary advantage of this approach, which is its capacity to produce reliable and measurable data that can potentially be generalized to a larger population. In this research, a quantitative approach was selected to address the research question and achieve the study's objectives. This method enabled a thorough understanding and interpretation of the data, allowing the researchers to draw meaningful conclusions based on statistical analysis.

Sampling procedure

Sample size

151 respondents, who are participated as investor in stock market (NSE and BSE).

Sources Data collection

This survey-based research utilized a combination of primary and pre-existing data. Primary data consists of information directly collected from respondents. The primary data were structured collected from individual investors participated in Indian stock markets. To gain a more comprehensive understanding of the topic, the researcher utilized a variety of published sources, including books, journal articles, and online resources. The study reviewed findings from previous literature on investors behaviours and its impact on decision making. Structured questionnaire has been used for collect data. Questionnaire includes demographic information and measurement scale for the investors behaviour and decision making.

Tools for data analysis

In this study, for data analysis, four Analysis has been used such as Descriptive analysis, Mean and standard deviation, ANOVA and Regression.

Demographic statistics: A valuable statistical tool that helps in understanding the distribution and proportion of demographic profile within a Respondents. Here, for summarize the demographic variable, percentage analysis has been used. Percentage analysis is used in various fields for two main reasons: simplification and comparison, as percentages simplify data and make comparisons easier, and normalization, as they allow for comparison across different scales, such as exam scores between different classes.

Mean and Standard Deviation: The fundamental statistics which provides valuable insights into the central tendency or Individuality and variability of the data. The mean and standard deviation are used to describe normal distributions, assess performance in business analysis, calculate z-scores, and identify anomalies in data. They help understand data clustering around the mean, aid in outlier detection, and measure the number of standard deviations a data point has from the mean.

ANOVA: A powerful statistical tool used to compare the means of three or more groups. It helps to determine if there are statistically significant differences among group means. ANOVA is a statistical technique used to compare the means of three or more groups, allowing simultaneous comparisons of means across multiple groups. It tests hypotheses about differences between group means, determining if observed differences are statistically significant or if they might have occurred by chance. ANOVA also helps identify group effects, such as the impact of independent variables on dependent variables.

Regression Analysis: A statistical technique used to examine the relationship between one dependent variable and one or more independent variables. Regression analysis is a statistical method used to understand relationships between variables and make predictions. It helps predict outcomes by predicting the value of a dependent variable based on independent variables. It quantifies relationships, identifies predictors, controls for confounding variables, and informs decision-making. Regression is used in academic research and business to optimize resource allocation and performance. To find the impact of Behavioral Bias, Behavioral Scrutiny, Behavioral consequences, behavioral effect on Investment decisions, the regression analysis has been conducted.

Findings

The study reveals a slightly male-dominated workforce, with 56.9% males and 43.1% females. The majority of participants are between 21 and 40 years old, with a smaller percentage over 50. The majority are married, with a higher percentage holding a graduate degree. The majority of participants have less than 5 years of experience, with a small percentage having over 10 years. The majority of participants earn between 5000 and 10000, with a smaller percentage earning below 5000 and very few earning higher amounts. The demographics provide a clear picture of the workforce, highlighting a younger, relatively inexperienced workforce with a lower to middle income range and a well-educated profile.

The study reveals that safety and low risk are the primary reasons for investment, with low risk being a major concern for 22.5% of participants. Personal benefits and speculation are also significant factors, while capital gains are a minor concern. Future security is a major concern for 15.2%, with investment amount and past experience influencing decisions.

The study analyzed the perception of investment decisions and behavioral factors among 151 participants. Behavioral bias (BB) and Behavioral Effect (BE) were rated relatively high, with BE being the highest. Behavioral Scrutiny (BS) and Behavioral Effect (BC) were rated lower, with BC being the lowest. Investment Decisions (ID) was rated moderately positive, with a low level of variability. These statistics provide a snapshot of how participants perceive different constructs related to their investment decisions and behavioral factors, highlighting areas of higher and lower evaluation. The results suggest that participants generally perceive these constructs fairly consistently, with a small degree of variability around the mean.

The study analyzed the impact of age on behavioral constructs and investment decisions. The results showed no significant differences in Behavioral Bias, Behavioral Scrutiny, Behavioral Effect, Behavioral Consequence, or Investment Decisions among different age groups. Age did not significantly influence Behavioral Effect, indicating that different age groups may experience different levels of Behavioral Effect. However, age did not significantly affect Behavioral Bias, Behavioral Scrutiny, Behavioral Effect, or Investment Decisions. The results suggest that age does not significantly impact these constructs, suggesting that different age groups may experience different levels of Behavioral Effect.

The study conducted an Analysis of Variance (ANOVA) to examine the impact of experience on various behavioral constructs and investment decisions. The results showed no significant differences in Behavioral Bias, Behavioral Scrutiny, Behavioral Effect, Behavioral Consequence, and Investment Decisions between groups with different levels of experience. The p-values were greater than 0.05, indicating that experience does not significantly impact these constructs. The variance between groups in terms of experience was not significant for these constructs. The p-values for Behavioral Effect and Behavioral Consequence were also greater than 0.05, indicating that experience does not significantly influence these constructs. The study concludes that experience does not significantly impact these constructs.

The regression analysis reveals that Behavioral Consequence significantly impacts Investment Decisions. Behavioral Bias, Behavioral Scrutiny, and Behavioral Effect do not significantly impact Investment Decisions. Behavioral Consequence has a significant negative impact, with a -0.166-coefficient indicating that for each one-unit increase in Behavioral Bias, Investment Decisions are predicted to decrease by 0.166 units. Behavioral Effect has a -0.050 coefficient, and Behavioral Consequence has a -0.166 coefficient, indicating that Behavioral Consequence has a negative impact on Investment Decisions.

Suggestions

To enhance investment decision-making among employees, it is crucial to promote gender balance and focus on younger, well-educated employees. Tailored training programs should be developed to address their specific needs, emphasizing financial education and planning, particularly in risk management and safe investment strategies. Given that experience does not significantly impact behavioural constructs, onboarding and continuous learning programs should be comprehensive to compensate for this. Raising awareness of behavioural consequences is essential to mitigate the negative impact of psychological biases on investment decisions. Investment policies should be regularly reviewed and adjusted to reflect employees' preferences for safety and low risk. Implementing tools to support more objective decision-making and continuous monitoring of training initiatives and investment policies will help align with employees' needs, ultimately fostering better investment outcomes and overall market efficiency.

Recommendations

The study suggests promoting gender balance in the workforce, focusing on younger employees and enhancing financial education and planning. It recommends developing tailored training programs and career development opportunities for these employees. Financial education workshops should emphasize risk management and safe investment strategies. The limited impact of experience on behavioral constructs should be addressed by developing comprehensive onboarding and continuous learning programs. Awareness of behavioral consequences should be promoted, and investment strategies

should align with employees' preferences for safety and low risk. Investment policies should be reviewed and adjusted to reflect employees' concerns. Behavioral factors in decision-making should be addressed, and tools should be implemented to help employees make more objective decisions. Continuous monitoring and evaluation of training programs, financial education initiatives, and investment policies can help improve employee satisfaction and decision-making in relation to investments and other behavioral constructs.

Conclusion

This study emphasizes the critical role of psychological and environmental factors in shaping investment decisions, challenging the assumption of rational behavior among investors. It reveals a workforce that is predominantly young, well-educated, and relatively inexperienced, with a male majority. Key motivators for investment include safety and low risk, highlighting the importance of future security and personal benefits. Despite demographic variations, age and experience do not significantly impact behavioural constructs like Behavioral Bias, Behavioral Scrutiny, Behavioral Effect, or Investment Decisions. Notably, Behavioral Consequence significantly negatively influences Investment Decisions, indicating that awareness of potential negative outcomes can deter investment enthusiasm. The research underscores the need for financial education programs focused on risk management and safe investment strategies. Promoting gender balance, tailored training, and continuous monitoring of investment policies can enhance decision-making and align with employee preferences, ultimately fostering more informed and objective investment practices.

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