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"Behavioral factor affecting investment decision among the investor"

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Abstract

Investors have different mindset when they decide about investing in a particular avenue. Every individual wants his saving to be invested in most secure and liquid way. However, the decision varies for every individual depending upon their risk aptitude. Investment behavior is related to activities of individual investors regarding searching, evaluating, acquiring, reviewing the investment products and if necessary, disposing such investment products. Investment behaviour reveals how the individual investor allocates the surplus financial resources to various instruments available. This project analyzes the trading or investing behavior of professionals. These young investors generally take trading decisions based on their self-perceived competence but sometimes with the help of professional advisors too. Their investment objective also differs from financial stability to additional income and so on. This project attempts to find out the factors responsible for increased investing activities among young professionals. The present has examined the trading behaviour of young investors by using a structured questionnaire. A survey of 150 young investors among the people. Based on the findings of the survey, the study examines the factor affecting the investment behavior in the stock market, real assets, government bonds, etc. On the basis of age, income and gender it can be concluded that for young investors' investment is independent of age, income and gender.

Keywords:- Investment avenues, investors' behaviour, saving objectives

Introduction

An investment is an asset or item acquired with the goal of generating income or appreciation. Appreciation refers to an increase in the value of an asset over time. When an individual purchases a good as an investment, the intent is not to consume the good but rather to use it in the future to create wealth.

An investment always concerns the outlay of some capital today—time, effort, money, or an asset—in hopes of a greater payoff in the future than what was originally put in.

Questioning Rational Actor Theory

Standard economic theory is based on the belief that individuals behave in a rational manner and that all existing information is embedded in the investment process. This assumption, known as rational actor theory (RAT), is the crux of the efficient market hypothesis (EMH).[1] According to RAT, individuals rely completely on rational calculations to make rational choices that result in outcomes aligned with their own best interests, or utility-maximization. RAT supposes that rational actors make these rational choices based on error-free calculations given full and complete information that is always available to them. Rational actors thus try to actively maximize their advantage in any situation and consistently try to minimize their losses in a self-interested manner.

Researchers, however, have been questioning the RAT assumptions and have uncovered evidence that rational behavior is, in fact, not nearly as prevalent as we might be led to believe by mainstream economics. Behavioral finance attempts to understand and explain how human emotions influence financial and investment decision-making processes. You may be surprised by what they have found thus far

Fear of Regret theory:-

Fear of regret, or simply regret theory, deals with the emotional reaction people experience after realizing they've made an error in judgment. Faced with the prospect of selling a stock, investors become emotionally affected by the price at which they purchased the stock. So, they avoid selling it as a way to avoid the regret of having made a bad investment, as well as the embarrassment of reporting a loss. We all hate to be wrong, don't we?

What investors should really ask themselves when contemplating selling a stock is: "What are the consequences of repeating the same purchase if this security were already liquidated and would I invest in it again?" If the answer is "no," it's time to sell; otherwise, the result is regret in buying a losing stock *and* the regret of not selling when it became clear that a poor investment decision was made and a vicious cycle ensues where avoiding regret leads to more regret.

Regret theory can also hold true for investors when they discover that a stock they had only considered buying has increased in value. Some investors avoid the possibility of feeling this regret by following the conventional wisdom and buying only stocks that everyone else is buying, rationalizing their decision with "everyone else is doing it."Oddly enough, many people feel much less embarrassed about losing money on a popular stock that half the world owns than about losing money on an unknown or unpopular stock.

Mental Accounting Behaviors

Humans have a tendency to place particular events into mental compartments, and the difference between these compartments sometimes impacts our behavior more than the events themselves. Say, for example, you aim to catch a show at the local theater and tickets are $20 each. When you get there, you realize you've lost a $20 bill. Do you buy a $20 ticket for the show anyway? Behavior finance has found that roughly 88% of people in this situation would do so. Now, let's say you paid for the $20 ticket in advance. When you arrive at the door, you realize your ticket is at home. Would you pay $20 to purchase another? Only 40% of respondents would buy another. Notice, however, that in both scenarios, you're out $40: different scenarios, the same amount of money, different mental compartments. Pretty silly, huh?

An investing example of mental accounting is best illustrated by the hesitation to sell an investment that once had monstrous gains and now has a modest gain. During an economic boom and bull market, people get accustomed to healthy, albeit paper, gains. When the market correction deflates investor's net worth, they're more hesitant to sell at the smaller profit margin. They create mental compartments for the gains they once had, causing them to wait for the return of that profitable period.

Prospect Theory and Loss-Aversion

It doesn't take a neurosurgeon to know that people prefer a sure investment return to an uncertain one—we want to get paid for taking on any extra risk. That's pretty reasonable. Here's the strange part. Prospect theory suggests people express a different degree of emotion towards gains than towards losses. Individuals are more stressed by prospective losses than they are happy from equal gains.[5]

An investment advisor won't necessarily get flooded with calls from her client when she's reported, say, a $500,000 gain in the client's portfolio. But, you can bet that phone will ring when it posts a $500,000 loss! A loss always appears larger than a gain of equal size—when it goes deep into our pockets, the value of money changes.

Prospect theory also explains why investors hold onto losing stocks: people often take more risks to avoid losses than to realize gains. For this reason, investors willingly remain in a risky stock position, hoping the price will bounce back. Gamblers on a losing streak will behave in a similar fashion, doubling up bets in a bid to recoup what's already been lost. So, despite our rational desire to get a return for the risks we take, we tend to value something we own higher than the price we'd normally be prepared to pay for it.The loss-aversion theory points to another reason why investors might choose to hold their losers and sell their winners: they may believe that today's losers may soon outperform today's winners. Investors often make the mistake of chasing market action by investing in stocks or funds which garner the most attention. Research shows that money flows into high-performance mutual funds more rapidly than money flows out from funds that are underperforming.

Anchoring Behaviors

In the absence of better or new information, investors often assume that the market price is the correct price. People tend to place too much credence in recent market views, opinions and events, and mistakenly extrapolate recent trends that differ from historical, long-term averages and probabilities. In bull markets, investment decisions are often influenced by price anchors, which are prices deemed significant because of their closeness to recent prices. This anchoring heuristic makes the more distant returns of the past irrelevant in investors' decisions.

Over- and Under-Reacting

Investors get optimistic when the market goes up, assuming it will continue to do so. Conversely, investors become extremely pessimistic during downturns. A consequence of anchoring, or placing too much importance on recent events while ignoring historical data, is an over- or under-reaction to market events, which results in prices falling too much on bad news and rising too much on good news. At the peak of optimism, investor greed moves stocks beyond their intrinsic values. When did it become a rational decision to invest in stock with zero earnings and thus an infinite price-to-earnings (P/E) ratio (think dotcom era, circa the year 2000)? Extreme cases of over- or under-reaction to market events may lead to market panics and crashes.

Investor Overconfidence

People generally rate themselves as being above average in their abilities. They also overestimate the precision and veracity of their knowledge -- as well as the perceived superiority of their own knowledge relative to others. Many investors believe they can consistently time the market, but in reality, there's an overwhelming amount of evidence that proves otherwise. Overconfidence results in excess trades, with trading costs denting profits.

Social Factors

While much of behavioral economics to date has been driven by cognitive psychology, recent research from economic sociology indicates that there are also supra-individual forces at work that drive investor behavior. A recent study, for instance, found that individuals become far more conservative when making investment decisions on behalf of close others - with people taking around one-third less risk in a portfolio intended for a child than one allocated for one's own behalf. Moreover, investors became even more conservative with investments made in accounts that had culturally-salient labels such as "retirement" or "college savings."Other research is now looking at how social relations and also larger structures like culture play on financial decisions. This shows that investor behavior is driven not only by psychology but also by social factors.

LITERATURE REVIEW

S. Uma maheshwari , M. Ashok Kumar (2014):-Awareness, environment level of exposure intensions, beliefs, responsibilities are the factors responsible for deciding investment policies . Behavioral pattern helps in preparing various schemes for investments. Investment temperament of salaried strata based on investment awareness and expected rate of investment return.

N. Dharani , et. al. (2014):-Investment attracts all people irrespective of their occupation education and social status. Women also involve in investment activities. Women's below age of30 are involve in investment activities. Women's with graduation are involve in more investment activities. women's with income of 50001 to 100000 are involve in investment activities.

S. Uma maheshwari, M. Ashok Kumar (2014):- This study is to find the relationship between Demographic and social factors that affects the invest decision of respondent like investment attitude, investment awareness and return on investment. This study analyses the priorities of salary classed people regarding investments. Different factors that affect the decision of respondents such as age, gender, Income scale, marital status etc.

Edward Egilinsky (2016):-Has addressed the top investment myths about alternative investment. The researcher has mentioned and identified some misconceptions.

These are: 1. Alternative strategies are too volatile and only suited for aggressive investors. 2. All alternative investment strategies are created equal. 3. Alternative investments are only geared towards high-net-worth and institutional investors and are off-limits to retail clients. 4. Alternative investments should be viewed as standalone investments. 5. Absolute returns/hedge funds have to show positive returns in every calendar year. 6. Incorporating a small percentage of alternatives investments within a portfolio constitutes an adequate level of diversification. In order to understand and get enough investment knowledge, one has to understand alternative strategies of investment together; it has proved by the researcher (Egilinsky, 2016).

Adams Otundoh Stephen, Enock Martha Otundo (2015):- This study is titled 'Investment Decision Making: A Study of Individual Investors Perception'. In this research survey, the researchers studied the individual investor's behaviour while taking an investment decision. Following are some important observations. It is observed that investors are more aware of various investment avenues & the risk associated with that. Investors are more conservative in nature and they prefer to invest in those avenues where risk is less like bank deposits, small savings, post office savings etc. This study shows that Life insurance is most preferred investment avenue among different variables. It gives the benefit of life protection, tax advantage & making provision for future (Adams Otundoh Stephen, 2015).

R. Sreepriya, P. Gurusamy (2013):- Additional income or growth in value can be achieved by investment. Waiting for rewards is the main characteristic of investment. Investment is allocation monetary resources to get returns over given period. Surplus funds are invested with different channels by salaried class people. This research analyses the different investment avenues. 81 percent respondents faced problem at the time of investment.

RESEARCH METHODOLOGY

Research methodology is the outline of the plan and method that how the study is conducted. So, mention below detail about it.

Research design:- A research design is a frame work or blue print for conducting the research projects. It details the procedures necessary for obtaining the information needed to structure or solve research problem.

In order to make the problem statement more clear and to have better understanding of the same, the study is descriptive in nature and based on secondary data and primary data. The endeavor is descriptive in nature

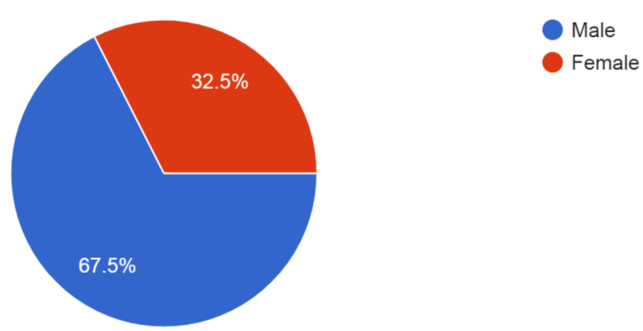
Research method

Quantitative:- Descriptive research

- Descriptive research refers to a research that provides an accurate portrayal of characteristics of a particular individual , situation , group or process. It is also known as statistical research.

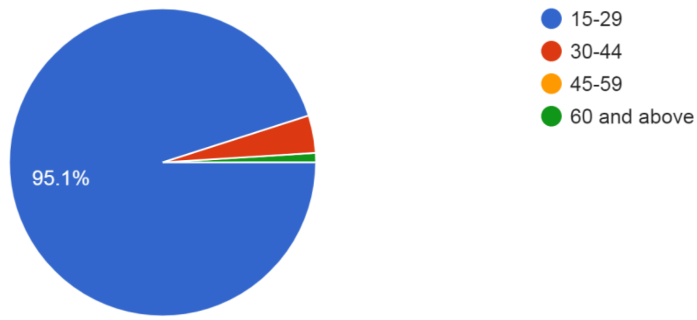
Data analysis interpretation

Gender



Interpretation:-

From the above graph it can be seen that more respondents were male than of female. In which 67.5 respondents were male and 32.5 were female.

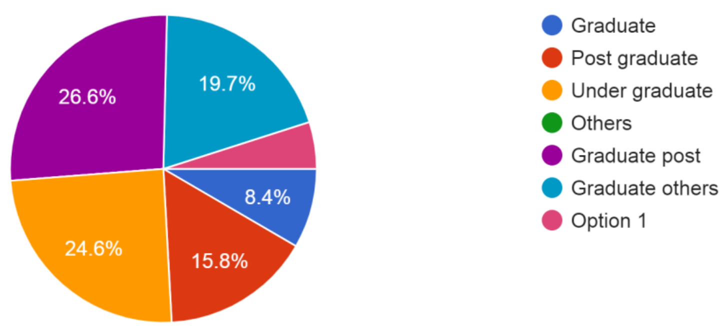


Age

Interpretation

This question represents the age group of the respondents. In which it was seen that 95.1% belongs to 15-29 years and the least percentage belongs to age group above 60.

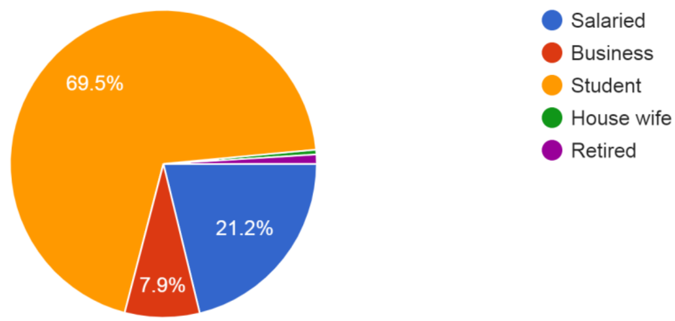
Qualification



Interpretation

This question represents the qualification of the respondents. In which it was seen that 26.6% belongs to post graduate and least percentage belongs to graduate that is 8.4%

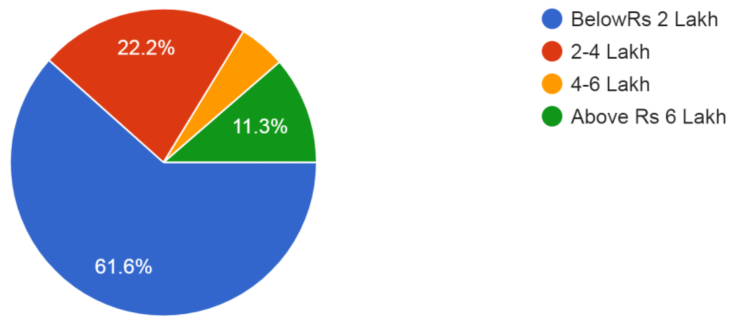
Occupation



Interpretation

This question represents the occupation of the respondents. In which 69.5% belongs to a student and the least percentage to occupation group is house wife

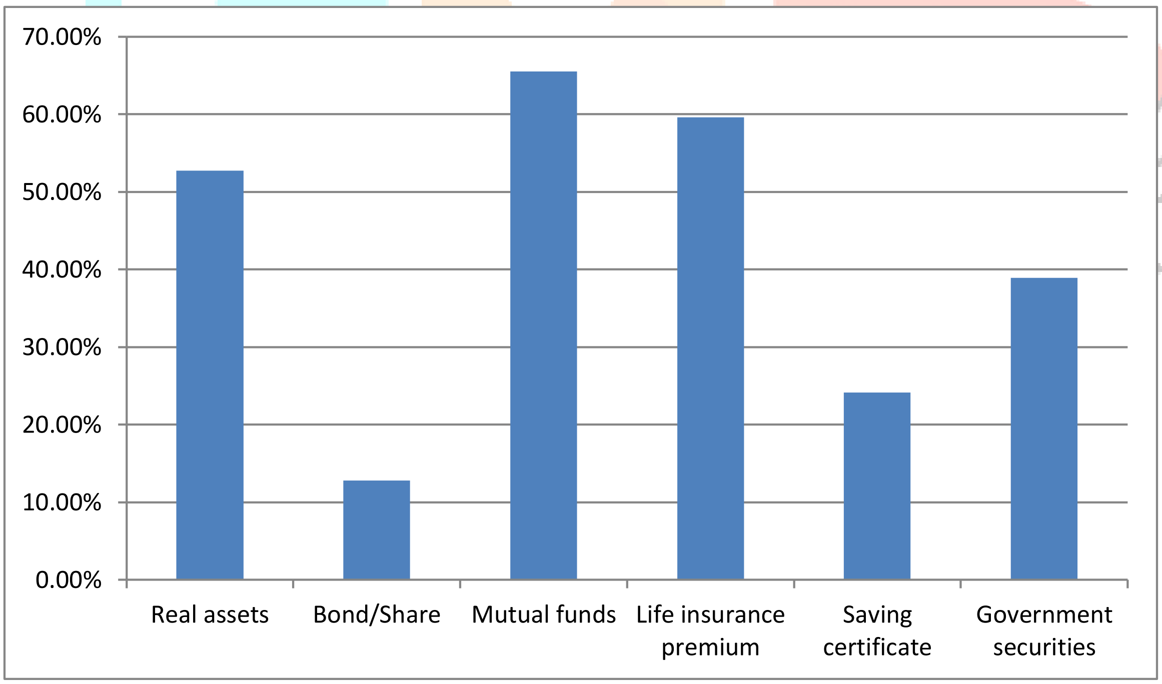
Annual Income



Interpretation

It represents about the annual income which shows that maximum number of people have their income below Rs 2 lakh and the others have under 4 to 6 lakh.

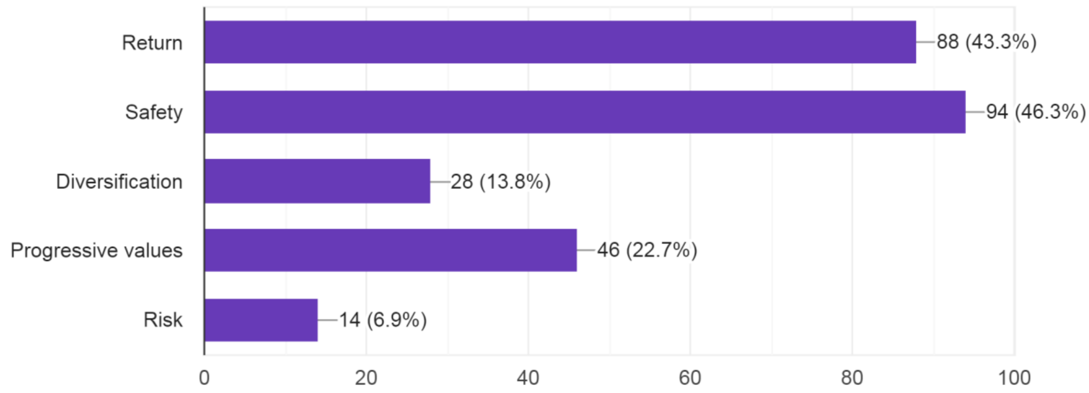
Investment avenue



Interpretation

This graph shows that the highest investment avenue is the mutual fund that is 133 and the least investment avenue is the bond/share that is 26.

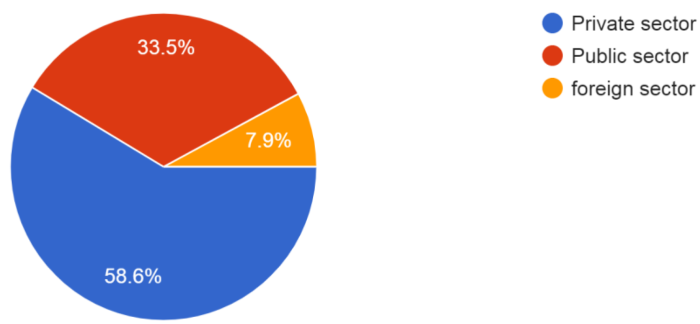
Investment decision



Interpretation

It represents that the safety factor having the highest investment decisions that is 46.3% and the least factor is risk that is 6.9%

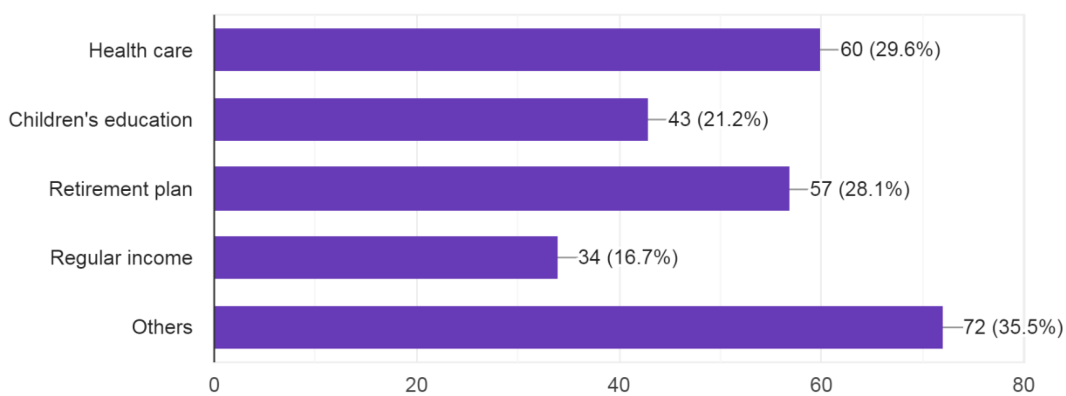
Investment of money



Interpretation

This question represents the sector to invest the money of the respondents in which it was seen that more respondents of private sector than of other sector. In which 58.6% was private sector and 7.9% was foreign sector.

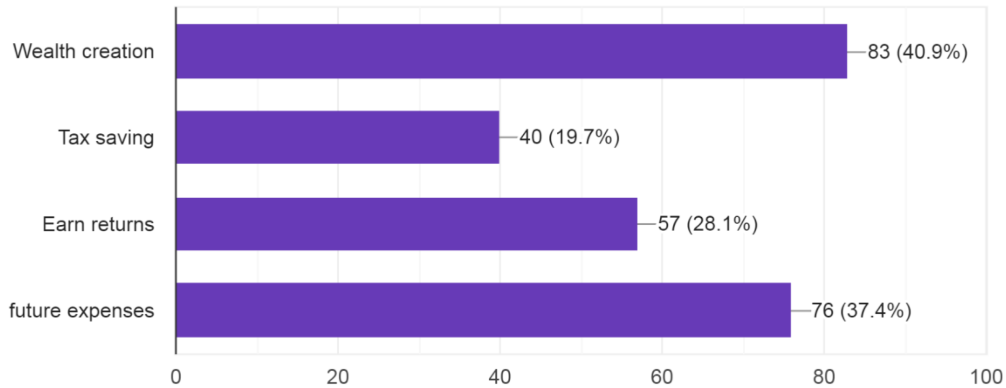
Saving objectives



Interpretation

This question represents saving objectives of the respondents. In which it was seen that 72 (35.5%) belongs to other reasons and the least percentage belongs to saving objective to regular income that is 34 (16.7%).

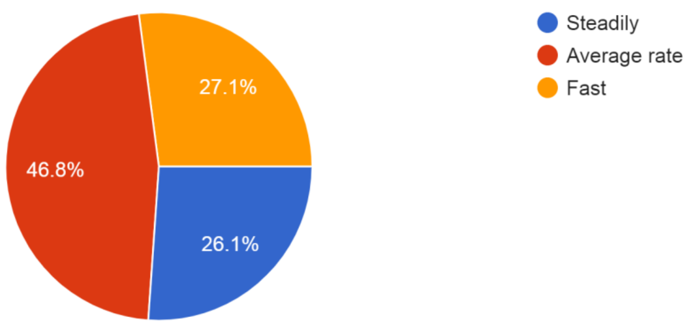
Investment purpose



Interpretation

It represents the purpose behind investment of the respondents. In which the wealth creation having 40.9% than the other purposes and the least percentage belongs purpose behind investment is tax saving i.e. 19.7%.

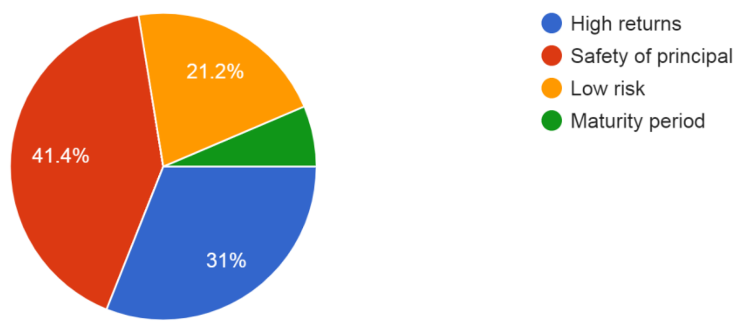
Investment rate to grow



Interpretation

This question represents the rate of investment grow of the respondents. In which it was seen that more respondents belongs to average rate that is 46.8% than the other rates. The least percentage belongs to investment to grow is steadily i.e. 26.1%

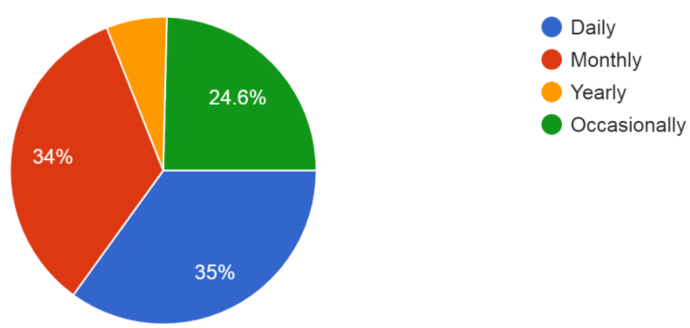
Consideration before investing



Interpretation

It represents about the factor consider before investing of the respondents having highest percentage factor is high returns that is 31% and the least percentage belongs to low risk that is 21.2% and maturity period.

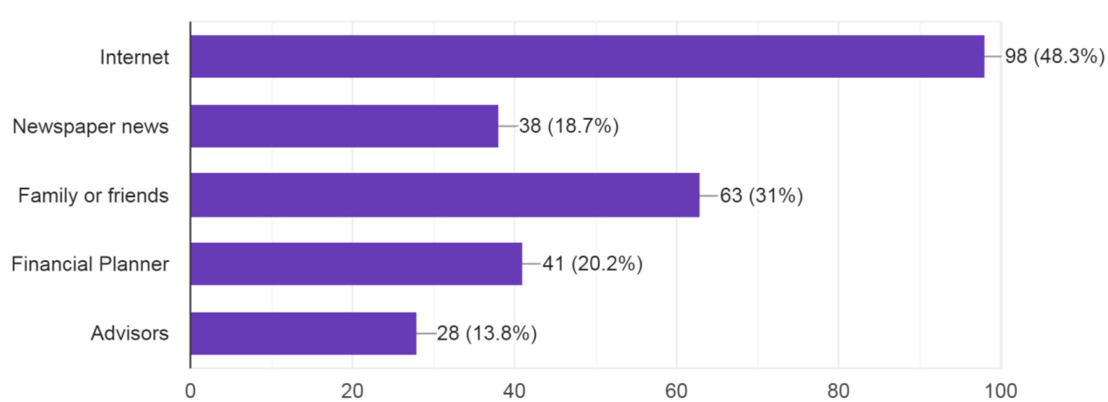
Monitoring the investment



Interpretation

It represents about the monitor of the investment that is daily monitoring is 35% and the least percentage belongs to yearly than the other investment monitor.

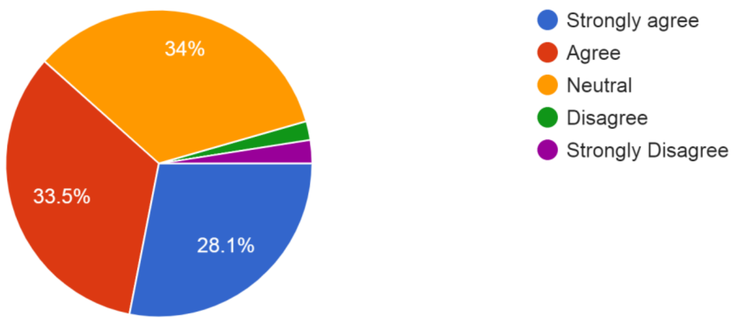
Sources of investment



Interpretation

This question represents about the source of investment advice of the respondents. In which it was seen that the highest percentage belongs to an internet advice i.e. 48.3% and the least percentage belongs to advisors i.e. 13.8%.

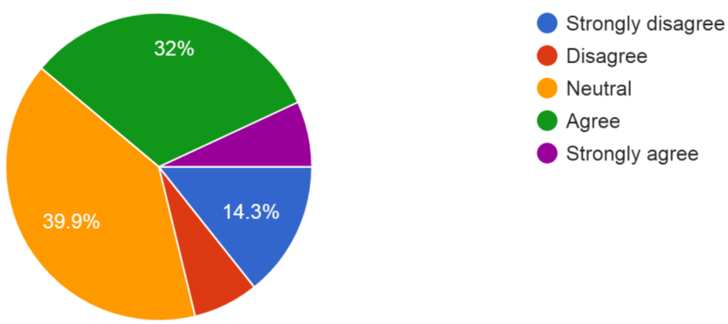
Herding factor on investment



Interpretation

This question represents about the herding factor on investment decisions of the respondents. In which it was seen that the neutral respondents having the highest investment i.e. 34% and the least percentage belongs to strongly agree i.e. 28.1%.

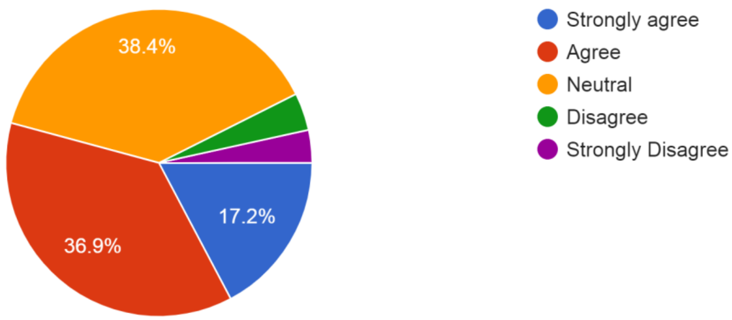
Mental accounting on investment



Interpretation

It represents about the impact of mental accounting on investment decision of the respondents is having the highest investment of neutral people i.e. 39.9% and the least percentage belongs to strongly disagree i.e. 14.3%.

Prospect Factors on investment



Interpretation

This question represents about the impact of prospect factors on investment decision of the respondents having the highest factor is neutral respondent that is 38.4% and the least percentage factor is strongly agree 17.2%

Conclusion –

The nature of investment differs from individual to individual and is unique to each one because its depends on various parameters like future financial goals , the present and the future income model, capacity to bear the risk, the present requirement and lot more. As an investor progresses on his/her life stage and as his/her financial goals change ,so thus the unique investor profile. Maximum investors are aware of all the investment options. Investors do not invest in a single avenue. They prefer different avenue and maximum investors prefer to invest in shares, mutual funds and debentures. The investment decision of investors is influence by their own decision and through friends and relatives. Majority of investors invest up to 10% of their annual income. The most important factor is returns which returns which influenced the decision regarding investment.

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