Perception and Behaviour of Retail Investors in Decision Making

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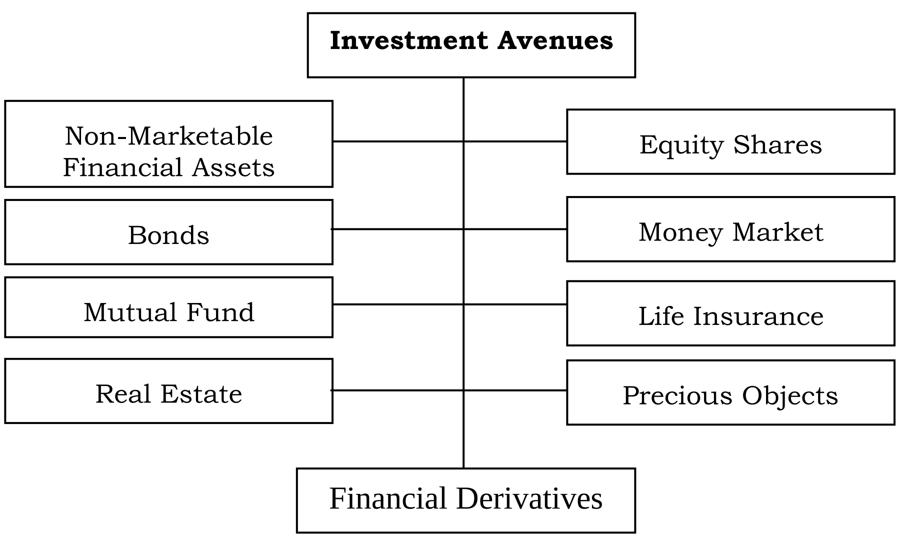
Abstract

Investment is an activity, which involves deployment of funds on some profitable channels for the purpose of acquiring profits. For this purpose investors invest their money on various portfolios such as equity shares, debentures, real estate, bank deposits, post office deposit schemes, NSC, PPF Gold ETF etc., every investor makes investment for the purpose of gaining returns out of their investment. This motive is for the purpose of having regular income, growth, preservation of capital etc., to meet the present and future contingencies. This activity of investment is affected from various factors such as risk factors, diversification factors and behavioral factors etc., Every individual investors behaves differently while investing depending on various factors such as demography, age, sex, emotions, social factors, market related factors etc. In this paper, main focus is levied on the main factors such as perception and behavior of investors which influences the investment behavior. It is because these factors mainly disturb the overall behavioral attitude, which makes a major difference in their behavioral portfolio.

Keywords: Investments, Financial assets, Risk aversion, diversified portfolio.

Introduction

An investment is a sacrifice of current money or other resources for future benefits. The U.S. Treasury defines an investment to be a market asset that has a holding period longer than 1 year. The tow key aspects of any investment are time and risk. Every investment involves uncertainties that make future investment returns risky. Therefore, investment planning begins with the establishment of objectives by the investor, based on personal financial needs, preferences and constraints. A strategy can then be formulated and a portfolio (or group) of assets can be selected. The step then the investor need to take is to examine some of the elements that determine investment objectives. An investor can have a wide array of investment avenues available such as;



Source: Prasanna Chandra, “Investment Analysis and Portfolio Management”, Tata McGraw-Hill Publishing Company Limited, New Delhi, Ninth reprint 2004, ISBN 0-07-048322-1, page 4

The length of the holding period, the time between signing a purchase order and selling the item, helps us determine whether something is an investment or something else masquerading as an investment asset. Whether an investment of money is short-term or long term and whether it is productive or unproductive, whether it is legal or illegal and whether it is a rational or irrational activity are all criteria useful in separating investing from other economic activities that are sometimes confused with investing.

Conceptual Framework

The traditional finance paradigm, which underlies many of the other articles, seeks to understand financial markets using models in which agents are "rational." Rationality means two things. First, when they receive new information, agents update their beliefs correctly, in the manner described by Baye's law. Second, given their beliefs, agents make choices that are normatively accepted, in the sense that they are consistent with Saage's notion of Subjective Expected Utility (SEU).

This traditional framework is appealingly simple, and it would be very satisfying if its predictions were confirmed in the data. Unfortunately, after years of efforts, it has become clear that basic facts about the aggregate stock market, the cross-section of average returns and individual trading behavior are not easily understood in this framework.

Behavioral finance is a new approach to financial markets that has emerged at least in part in response to the difficulties faced by the traditional paradigm. In broad terms, it argues that some financial phenomena can be better-understood using models in which some agents are not fully rational. More specifically, it analyzes what happens when we relax one, or both of the two tenets that underlie individual rationality.

The premise of behavioral finance is that conventional financial theory ignores how real people make decisions and that people make a difference. A growing number of economists have come to interpret the anomalies literature as consistent with several "irrationalities" that seem to characterize individuals making complicated decisions. These irrationalities fall into two broad categories: first, those investors do not always return; and second, that even given a probability distribution of returns, they often make inconsistent or systematically suboptimal decisions.

Of course, the existence of irrational investors would not by itself be sufficient to render capital markets inefficient. If such irrationalities did affect prices, then sharp-eyed arbitrageurs taking advantage of profit opportunities might be expected to push prices back to their proper values. Thus, the second leg of the behavioral critique is that in practice the action of such arbitrageurs are limited and therefore insufficient to force prices to match intrinsic value.

Review of Literature

Abhijeet Chandra and Ravinder Kumar (2013) suggest that the psychological biases such as conservatism and under confidence are playing significant role in determining individual investment behavior. The author through the survey findings suggest to reduce the significance of behavioral biases such as anchoring, availability bias, representativeness bias, and attributes such as overconfidence, mental accounting and regret aversion in individual investment decision making processes. Also suggests that individual investors should not be left behind as an isolated batch in the financial markets, rather they should be made aware of heuristics-based decision-making processes and learn how to incorporate them, along with fundamentals, in their investment strategies.

Rakesh H,M (2014) Through his study it is concluded that results of the factor analysis and descriptive statistics have led that there are multiple factors that have greater influence on the behaviour of commodity market investors in India. The main factors that have such greater influence are information asymmetry, objective knowledge, high return and low risk. The influence of all these four factors on the commodity market investors' behaviour is found to be significant with 95 percent confidence level.

David Pascual-Exama, Barbara Scandroglio, Beatriz Gil-Gomez de Liano (2014) say that the intention towards investing in stock exchange is positively associated with the behavior towards investing. This result is in accordance to social psychology researchers, also considering intention as a very important variable in the study of behavior. And attitudes are positively associated with behavioral intentions towards investing in stocks exchange. In fact, it has been the variable with the strongest correlation both with intention and behavior. Also, control which has not been one of the most popular variables in the field of investment analysis. Finally, they say individual investors. Beliefs toward attitudes and perceived behavioral control are positively associated with attitudes and control, respectively and indirectly with behavioral intentions towards investing in stocks exchange. According to this, others have beliefs as important factors to understand the investor behavior. They conclude by saying that we need to leap in order to build a more consistent bridge between theoretical academic fields and daily companies' activities. Therefore, further research must be focused on improving existing models or proposing new ones, which allow us to apply the results found in basic research. They think that the study of psychological factors such as attitudes and control may be a good start to advance in the knowledge of individual investor's behavior in the stock market.

Mr. P. Arulmurugan, Dr. K.Balanagaguruthan and Ms.Mirudhubashini (2013) in their study made an intense effort to study the Investment behavior of the professors towards Gold Investment in Tamil Nadu State. In the ultimate analysis of the study, individual and family characteristics of professors such as age, gender, marital status, lifestyle, monthly family income, stage of family life cycle and various factors like safety, liquidity, traditional value, investment tool, risks and returns associated with Gold investment determines the investment behavior of professor's community in the study region. Their study also analyzes the preference towards various forms of gold investment and discloses that professors' first choice goes for Ornaments, Gold Coins, bars and last priority to ETF (Exchange Traded Funds). In Factor analysis, as well those similar variables are factorized under five categories as future prospects, risk management, Ideal time for investment, conventional value and as an alternative investment tool which are highly correlated to each other in right of way order. Their study also evidences that investment towards various forms of Gold is influenced by the occasion of Gold investment and by the Gender too with respect to Gold investment behavior of Professors in Tamil Nadu state.

Dr. Taqadus Bashir, Hassan Raza Ahmed, Sheraz Jahangir, Samina Zaigham, Hifza Saeed and Sameera Shafi (2013) says that the main purpose of their research was to analyze the behavior of salaried individuals of Gujarat and Sialkot about risk level, stock investment and gambling decisions. The situation of these cities is quite different from previous research. All previous literature investigates that higher income or wealthier persons are most willing to invest but in Gujarat and Sialkot salaried individuals do not invest. However, they have only learning of these things they practically has not been invested. The researchers find out that education is necessary but regular financial advices are also necessary for investors because they don't construct their portfolio. For diversified portfolio, financial advisor is necessary. With lack of investment opportunities and absences of investment trends in Gujarat and Sialkot there is no concept of financial advisors in these cities. At the end of the research it is concluded that demographic factors have significant relationship with risk level, stock investment and gambling. But another thing is that people have knowledge and income but still that are not willing to invest. They have fear of losses, reluctance and religious factor. There are brokerage houses nor adviser available to advise or construct the portfolio according to the risk tolerance of salaried individuals.

Arvid O.I. Hoffmann and Thomas Post (2013) say that prior research shows that individual investor behavior influences asset prices, market volatility and even the macro economy. Important drivers of individual investor behavior are investor optimism, as expressed by return expectations and investor fear as expressed by risk tolerance and risk perceptions. They contribute to the field evidence of the directional impact of both return and risk experiences on investor optimism and fear using a panel study of active individual investors. Their results show that individual investor's return expectations indeed exhibit adaptive behavior with respect to return experiences and thus they provide empirical support for Barberis's theoretical perspective regarding the psychological factors that contribute to the creation of asset-price bubbles.

Objectives of the Study

1. To analyze the technical and fundamental factors affecting the investor's behavior
2. To analyze the various emotional factors that affects the investor's behavior
3. To analyze the middlemen related factors that affects the investor's behavior

Sources of Data

Primary and Secondary data is being used. The secondary data is collected through published and unpublished sources. The primary data will be collected through the structured questionnaire administered on the retail investors.

Limitations of the Study

The expected limitations of the study are:

1. Available published data is used.

2. The study is subject to in-built limitations of published data.

3. The investors buying pattern keeps changing with the introduction of innovation in terms of product, price, place and promotion. If there is introduction of new financial product, investors buying behavioral pattern may change.

4. The sample investors belong to a selected group of sample investors. Hence the inference drawn is based on the feedback given by only those sample investors.

Statement of the Problem

Today the investment is a dynamic and growing field. But the investors even today shows irrational behavior and behave sentimentally towards the selection of portfolios. The investors tend to become blind investors and would like to diversify their investment on the traditional portfolios such as LIC, Bank Deposits, Public Provident Fund scheme etc. The rationality and the traditional behavior of the investors seem to differ from region to region and also based on their income. To find the reason for such state of affairs, the present study has been undertaken.

Hypotheses

The present study is going to test the following hypotheses;

Ho: The pre-purchase and post-purchase factors do not affect the investor's perception and behavior.

H1: Technical and fundamental factors affect the investor's perception and behavior

H2: Emotional factors affect the investor's perception and behavior.

H3: Middlemen related factors affect the investor's perception and behavior.

Scope of the Study

The main scope of the study is to covers various factors that influence the investment decisions of retail investors.

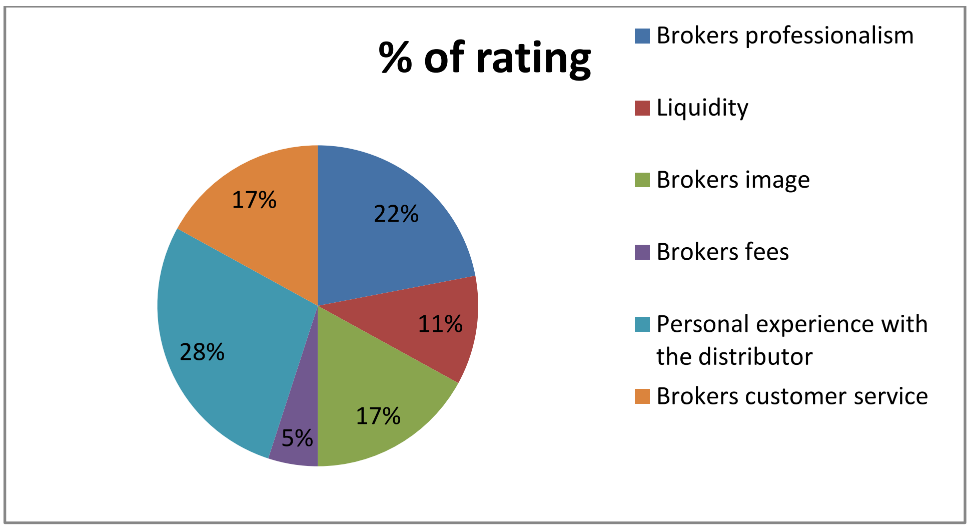
Analysis and Interpretation

Table 1 Showing Investment decision towards choice of distributor (broker)

Investment decision towards choice of distributor (broker)	% of Rating
Brokers professionalism	22%
Liquidity	11%
Brokers image	17%
Brokers fees	5%
Personal experience with the distributor	28%
Brokers customer service	17%

Analysis:- The above table shows that the investors mainly depend on their personal experience with the broker and the professionalism of the broker for the purpose of decision making.

Graph 1 Showing Investment Decision towards Choice of Distributor (Broker)



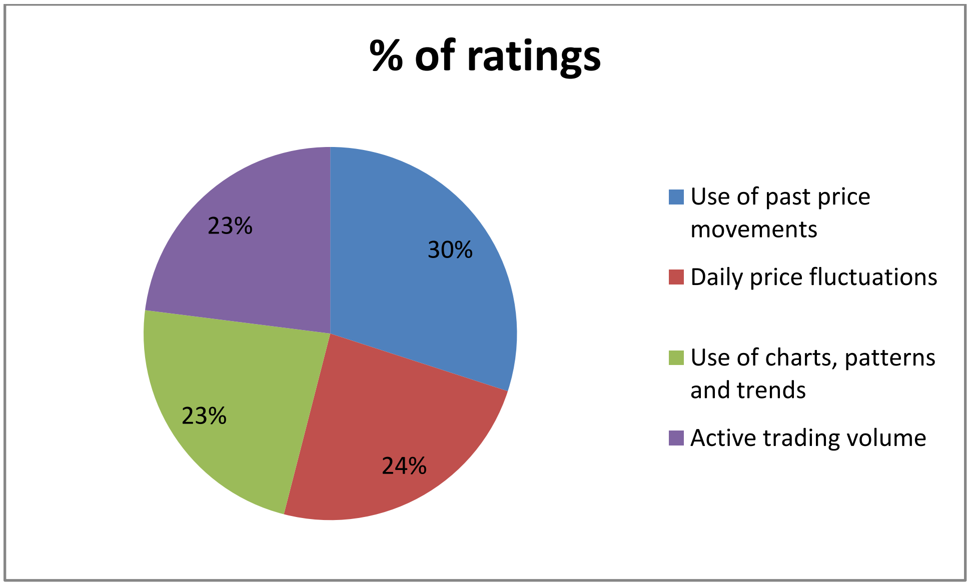
Interpretation:- Investors mainly depend on the previous personal experience which they have had with the broker while picking the broker. Alternatively, sometimes they also depend on the experience faced by their friends or relatives along with the broker's professionalism because they also do the survey before selecting the broker so that they do not burn their hands out the investment.

Table 2 showing technical analysis used by the investors while making decisions

Technical analysis	% of ratings
Use of past price movements	30%
Daily price fluctuations	24%
Use of charts, patterns and trends	23%
Active trading volume	23%

Analysis:- The above table shows that past price movements help the investors a lot while making investment.

Graph 2 showing technical analysis used by the investors while making decisions



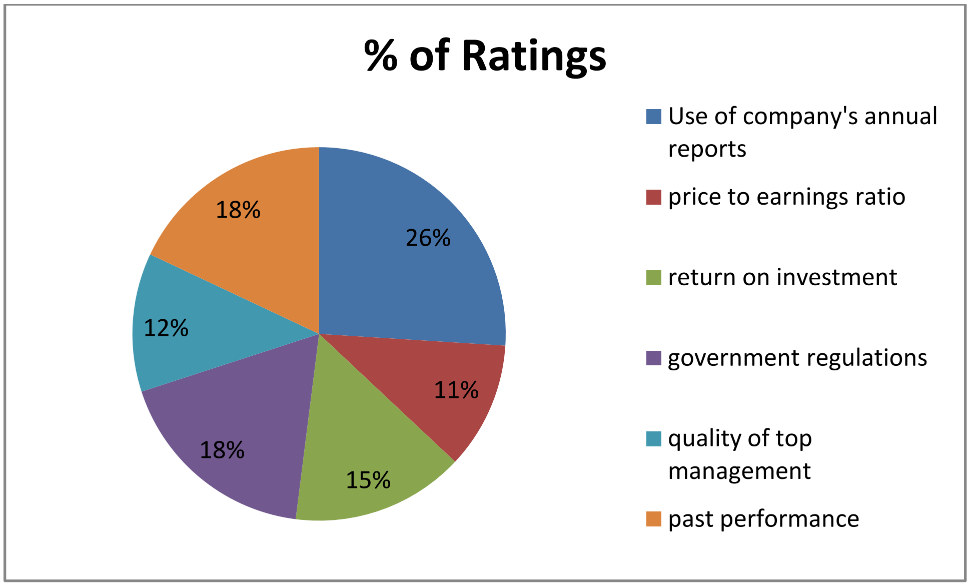
Interpretation:- Past data will help the investors in analyzing the movements of stock which will help them to analyze the present and future prospects of their investment and thus help them in decision making.

Table 3 Showing the fundamental analysis used by the investors while making decisions

Fundamental analysis	% of Ratings
Use of Company's Annual Reports	26%
Price to Earnings Ratio	11%
Return on Investment	15%
Government Regulations	18%
Quality of Top Management	12%
Past Performance	18%

Analysis:- From the above table it is understood that the investors mainly depend upon the company's annual reports for the purpose of decision making.

Graph 3 Showing the fundamental analysis used by the investors while making decisions



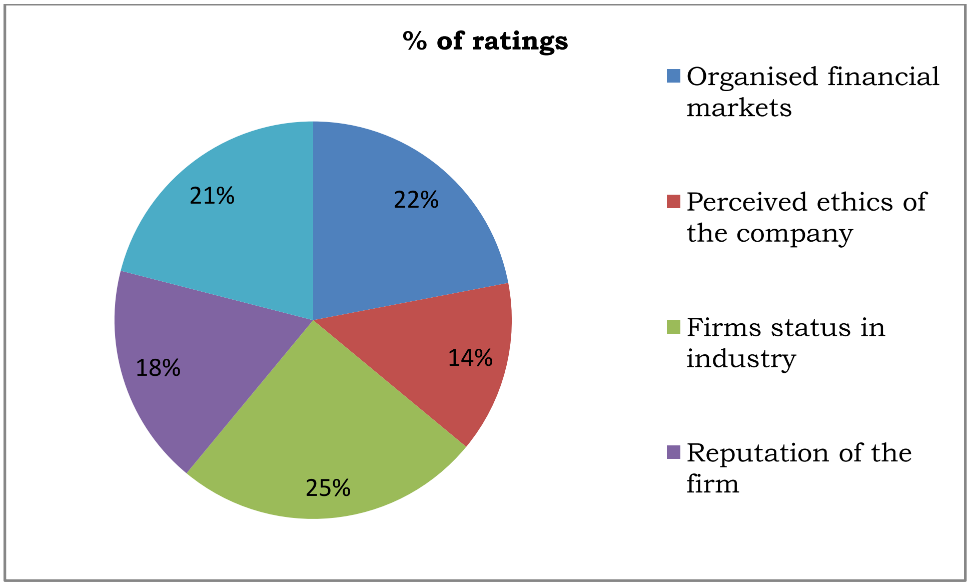
Interpretation:- Company's annual reports shows the exact picture of the company, their financial position, their stake holding capacity and overall performance of the company which will help the investors in deciding their investment attributes.

Table 4 showing the Firm image coincidence factors that are considered by the investors while making decisions

Firm image coincidence factors	% of ratings
Organised financial markets	22%
Perceived ethics of the company	14%
Firms status in industry	25%
Reputation of the firm	18%
Increase of firms involvement in solving community problems	21%

Analysis:- From the above table it is understood that status of the firm, organized financial market and firms involvement in solving community problems constitute the major role.

Graph 4 showing the Firm image coincidence factors that are considered by the investors while making decisions



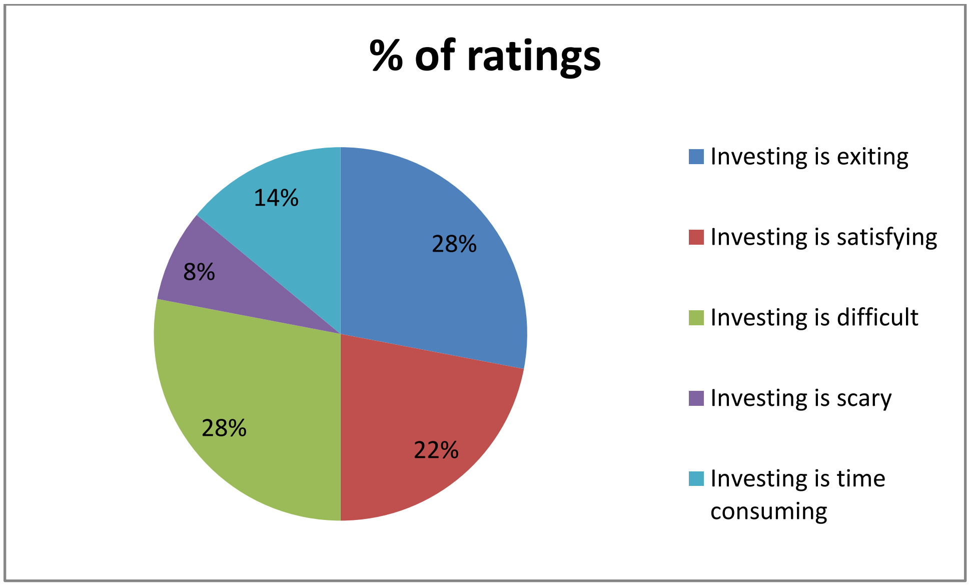
Interpretation:- Status of the firm and their involvement in solving community problems plays a major role because it is these factors which shows the capacity of the firm, their reputation, their stake in the society and their earning capacity which is very important for an investor to know before making investing. Because it is these factors which will decide the returns for the investors.

Table 5 showing variety of emotions that are considered by the investors for decision-making

Variety of emotion	% of ratings
Investing is exiting	28%
Investing is satisfying	22%
Investing is difficult	28%
Investing is scary	8%
Investing is time consuming	14%

Analysis:- From the above table it is understood that most of the investors feel that making investment is exiting and also it is difficult. However, they are also of the opinion that it is difficult.

Graph 5 showing variety of emotions that are considered by the investors for decision-making



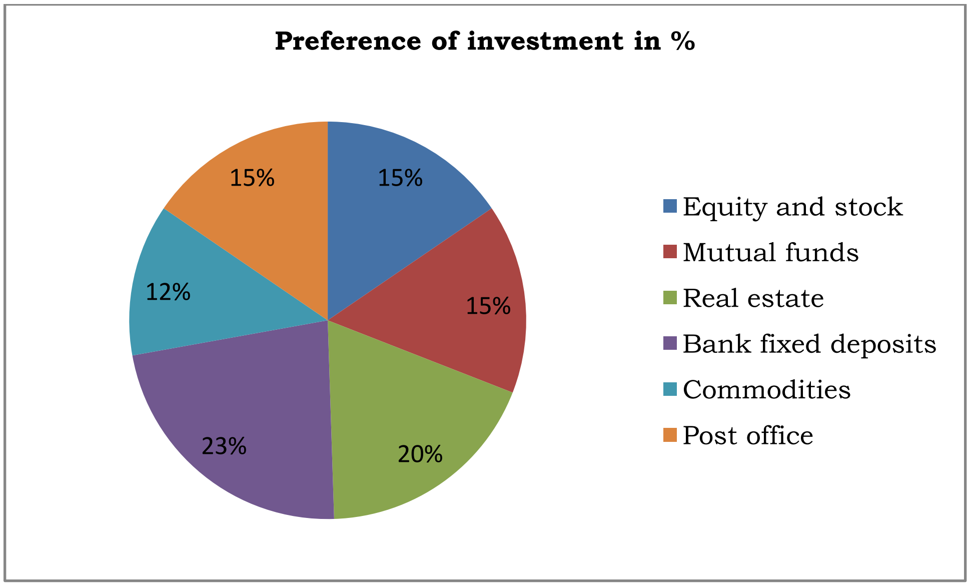
Interpretation:- Investors who are new to the field of investment feel that it is difficult because it takes time for them to analyze the financial market. Once they are known to the market they start feeling that it is exiting and feels satisfied once they start getting returns.

Table 6 showing preference of investment across different financial instruments

Investment Avenues	Preference of investment in %
Equity and stock	15%
Mutual funds	15%
Real estate	20%
Bank fixed deposits	23%
Commodities	12%
Post office	15%

Analysis:- From the above table it is clear that majority of investors prefer traditional portfolios such as real estate, bank deposits etc. In addition, less preference is given to commodities market.

Graph 6 showing preference of investment across different financial instruments



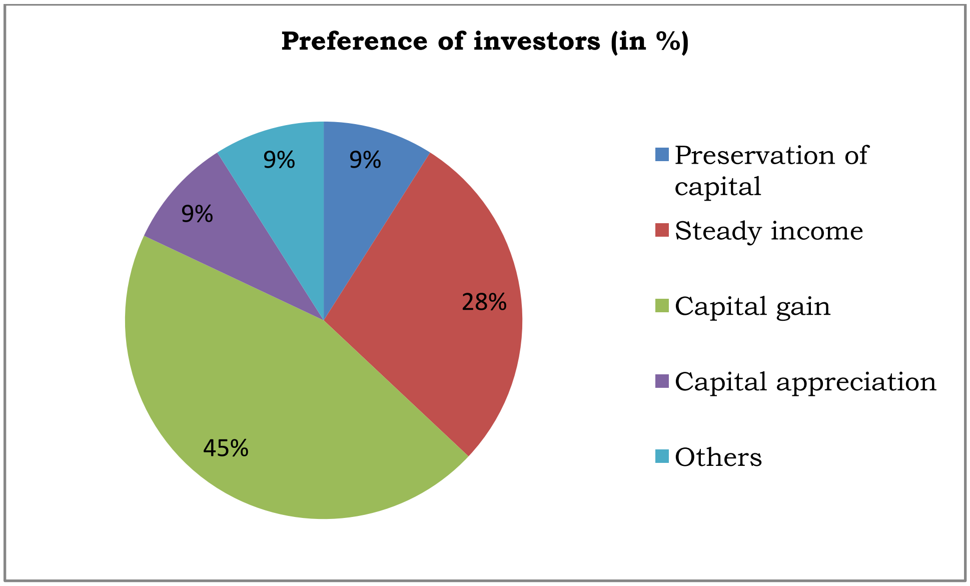
Interpretation:- The above graph says that since the middle class income grouped investors do not want to take risk they would like to invest mainly on real estate, bank deposits etc., It is also clear from the above graph that investors are not much exposed to modern portfolio due to lack of knowledge or what so ever.

Table 7 Showing the investment objectives of investors

Investment Objective	Preference of Investors (in %)
Preservation of capital	9%
Steady income	28%
Capital gain	45%
Capital appreciation	9%
Others	9%

Analysis:- From the above table it is clear that investors mainly invest in order to have capital gain and regular income.

Graph 7 showing the investment objectives of investors



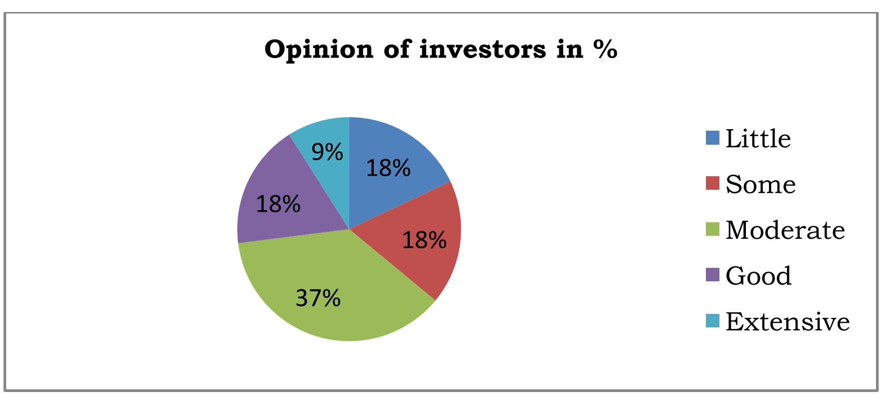
Interpretation:- Every investors mainly invest in order to get regular and steady income and also to have gain on their capital. This mentality of investor is mainly due to forecast the unforeseen event, which may happen in future.

Table 8 Showing the level of knowledge of investors about investment

Level of knowledge about investment	Opinion of investors in %
Little	18%
Some	18%
Moderate	37%
Good	18%
Extensive	9%

Analysis:- From the above table it is clear that investors have moderate or some knowledge about investment. In addition, they do not have extensive knowledge, which is required for successful investment activity.

Graph 8 showing the level of knowledge of investors about investment



Interpretation:- The above graph shows that the investors have moderate knowledge about investment which may or may not be sufficient for successful investment strategy. They take investment related decision out of some knowledge they have. This may be because of lack of knowledge of investors towards the SEBI regulations or they may not be aware of various recent amendments or recent activities, which are taking place in the investment world from time to time.

Findings:

1) Personal experience with the broker and the professionalism of the broker plays the important role in decision making.
2) Past price movements, fluctuation in the financial market along with the trading volume help the investors a lot while making investment.
3) Investors mainly depend upon the company's annual reports for the purpose of decision making along with past reports and government regulations.
4) Status of the firm, organized financial market and firm's involvement in solving community problems constitute the major role in decision making.
5) Investor's feel that making investment is exiting and also it is difficult. But they are also of the opinion that it is difficult.
6) Investor's mainly depend upon the traditional portfolios such as bank deposits, real estate and less preference is given to modern portfolios such as commodities market etc.
7) Investor's invest mainly to have capital gain and capital appreciation.
8) Investor's have moderate knowledge about investment.

Suggestions

1) Proper investment education programs should be organized by SEBI.
2) Proper education programs should also be enforced to the brokers.
3) Financial market should be organized and well regulated so that investors should feel comfortable while investing.
4) Proper actions should also be taken in controlling and monitoring the activities of the firm.
5) Investor's educational programs should be organized and it should be made reachable to the common investors so that they acquire more knowledge towards investment activity.
6) Overall investor's protection measures should be strictly regulated so that the confidence of the investors and gained by the financial market and thus the flow of capital in the economy is also necessitated.

Conclusion

The material wealth of a society is ultimately determined by the productive capacity of its economy, that is, the goods and services its members can create. This capacity is a function of the real assets of the economy: the land, building, machines and knowledge that can be used to produce goods and services.

The overriding consideration in individual investor goal setting is one's stage in the life-cycle. Most young people start their adult lives with only one asset – their earning power. In this early stage of the life cycle, an individual may not have much interest in investing in stocks and bonds. The needs for liquidity and reserving safety of principal dictate a conservative policy of putting savings in a bank or a money market fund.

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