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"Impact of Behavioural Finance on Stock Investment Decisions of Working Employees"

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Abstract

Behavioural financing is an evolving field that studies how psychological factors affect decisions taken under uncertain conditions of working employees. Behavioural finance speaks about the mindsets of the people about how they think, when they are investing in securities. This research analyses the mentality of the people while they invest in various investment avenues. i.e., what do they think while investing. Investors considers factors like goals in life, spending habits, expenses, income, perception towards investments, lifestyle changes, time period, demographic factors, nature towards investment, thought process, natural habits, individual financial risk bearing capacity, liquidity and expected yields. The paper has concentrated on effects of behavioural financing on investors and also impact and relevance of behavioural financing in investment decision of investors. This study has also underlined the factors influencing the investors while investing and the concepts of behavioural financing.

Finally, study accomplishes that behaviour matters a lot when it comes to making a wise investment decision in selecting a particular investment. most of the respondents are investing in order to meet some specific purpose for their like additional source of income, retirement plan etc., This study also concludes that investors' investment decision is based on risk-taking capacity, their level of income and the sources of income. Although every Individual is subject to some sort of prejudices, they tend to think more in coherent way.

Keywords: Behavioural Finance, Securities, Psychology

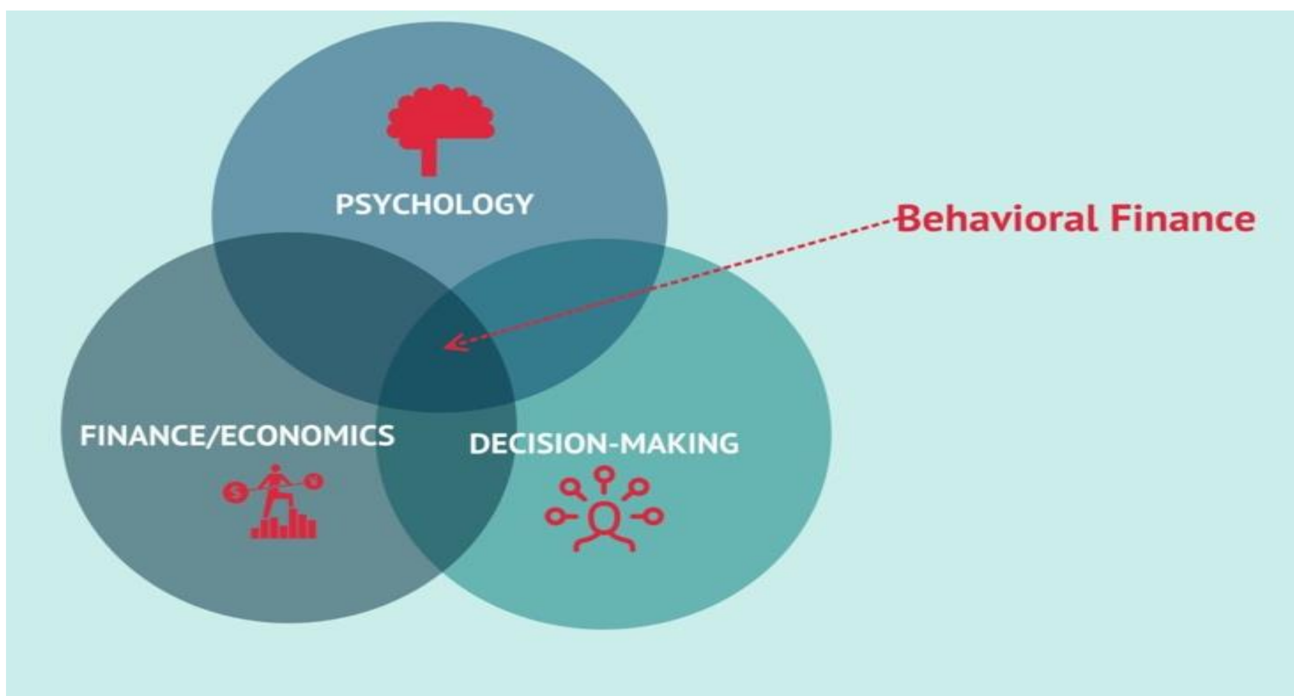
Introduction

Behavioral finance is the study of how psychology affects the conduct of financial professionals and how that affects markets **(Sewell, 2007).** Some financial occurrences, according to behavioral finance, can be explained

using models in which some investors are fully rational, meaning that their investment decisions are based on risk and return considerations. Harry established one of the most well-known hypotheses.

Behavioral finance is a combination of psychological and financial factors that investigates what happens in markets where some investors exhibit human limitations and complications. As a result, psychology investigates human judgement, behavior, and well-being in a systematic way, and it can teach us important facts about how humans differ **(Rabin, 1996).**

As a result, investor behaviour in the stock market is based on psychological decision-making concepts that explain why people purchase and sell equities. "A fast-emerging topic that deals with the effect of psychology on the conduct of financial practitioners," **Shefrin (1999)** described behavioural finance. Behavioral finance, according to **Ricciardi and Simon (2000),** aims to explain and improve comprehension of investors' thinking processes, including the behavioural aspects involved and the degree to which they impact the decision-making process.



Knowledge Workers

The phrase "knowledge worker" was originally used by Peter Drucker in his book, The Landmarks of Tomorrow, which was published in 1982. (1959). Information workers, according to Drucker, are high-level employees who use theoretical and analytical knowledge, which they have obtained via formal training, to the development of goods and services. Because of their high levels of productivity and creativity, he believes that knowledge employees will be the most important assets in a 21st-century firm.

Knowledge employees are becoming more significant assets for enterprises all over the world because of the advent of automation and the idea that the number of blue-collar workers will continue to decline in the future years. Organizations are now seeking for strategies to get the most out of their knowledge employees to address the growing skill and knowledge gaps that they are experiencing.

Review of literature

Raut, R. K., Das, N., & Mishra, R. (2020). Behaviour of individual investors in stock market trading: Evidence from India. Global Business Review,

This research uses structural equation modelling (SEM) to analyse data from a statewide survey of 396 individual investors in order to better understand the factors that influence individual investors' decisions in the Indian stock market. This research looked into the elements that influence individual investors' investment decisions to see if the Indian financial market is efficient and investors make reasonable selections. Herding, information cascades, anchoring, representativeness, and overconfidence all have a major impact on investors, whereas contagion has a minor impact. Moreover, the study has produced substantial evidence of investor irrationality as well as financial market inefficiencies. The findings may be utilised to further investigate individual investor trading behaviour and to stimulate new study in the field of behavioural finance.

Kartini, K., & Nahda, K. (2021). Behavioral Biases on Investment Decision: A Case Study in Indonesia. Journal of Asian Finance, Economics and Business.

A shift in perspective from standard finance to behavioral finance has taken place in the past two decades that explains how cognition and emotions are associated with financial decision making. This study aims to investigate the influence of various psychological factors on investment decision-making. The psychological factors that are investigated are differentiated into two aspects, cognitive and emotional aspects. From the cognitive aspect, we

examine the influence of anchoring, representativeness, loss aversion, overconfidence, and optimism biases on investor decisions. Meanwhile, from the emotional aspect, the influence of herding behavior on investment decisions is analyzed. A quantitative approach is used based on a survey method and a snowball sampling that result in 165 questionnaires from individual investors in Yogyakarta. Further, we use the One-Sample t-test in testing all hypotheses. The research findings show that all of the variables, anchoring bias, representativeness bias, loss aversion bias, overconfidence bias, optimism bias, and herding behavior have a significant effect on investment decisions. This result emphasizes the influence of behavioral factors on investor's decisions. It contributes to the existing literature in understanding the dynamics of investor's behaviors and enhance the ability of investors in making more informed decision by reducing all potential biases

Objectives of the Study

1. To understand the current stock investment patterns of Knowledge workers.
2. To study the factors influencing behavioral bias of Knowledge workers.
3. To analyze the impact of behavioral bias on the stock investment decision.

Stock investments in India

A Financial Instrument is a monetary contract between two parties that can be traded and settled in the financial markets. For one side (the buyer), this contract represents an asset, whereas for the other party, it represents a financial responsibility (the seller). It is important to remember, however, that not all financial products are available for trading on the stock exchange. To give an example, although cheques are considered a financial instrument, they are not permitted to be exchanged on the exchange.

Stock investments in India

BEHAVIORAL BIASES

According to Agrawal (2012), biases in human behaviour have always had and will continue to have an influence on the decisions made by investors. It becomes critical for investors to avoid particular behavioural biases in specific scenarios even if it is not feasible for them to be totally eliminated from their decision-making process. Reiterating the notion that psychological elements have an influence on stock price anomalies and financial decision making, (Rayenda Khresna Brahmana, 2012) explains how psychological factors might contribute to irregularities in financial decision making. The study of human behaviour and decision-making has resulted in the discovery of several cognitive biases by psychologists throughout the course of their research.

Number of biases that lead to this type of behaviour.

Framing

Framing is a term used in behavioural finance to refer to a collection of phrases that are used to frame a certain problem or solution at hand. When presented with a variety of options for investing their money, investors would choose those that speak of possible returns rather than those that speak of probable losses as the basis for their decision. Individuals are more troubled by the prospect of potential losses than they are by the prospect of possible benefits. This means that for an individual investor, a Rs.500 loss will be twice as unpleasant as a Rs.500 gain in the same period.

Loss Aversion

Individuals prefer to avoid loss rather than get equal profits; losses appear to be twice as potent as the same amount of gains.... If, for example, an individual is presented with the 50-50 chance of winning Rs 500 or losing Rs450 in a gamble, he or she will not accept the bet because the impact of the loss is perceived to be significantly greater than the impact of the gain, even if the associated gains are greater than the associated loss. This indicates that if an investor is fearful of losing money, he or she may resort to the rule of averages and acquire additional underperforming stocks in order to recover previous losses. When it comes to motivating individuals, utilise loss aversion to explain why, at times, penalties are more effective than positive rewards.

Regret Aversion

The tendency for individuals to be disappointed in their decisions when the outcome is not good. If an investor loses money in the stock market, he or she will likely experience more remorse as a result of having made a poor judgement than the actual loss incurred. Investors may come to believe that they are to blame for making the decision to invest in a bad stock that eventually resulted in losses. In some cases, this can lead to poor financial decisions, such as investing in stocks that have recently performed well, avoiding stocks that have not performed well recently, or simply investing in stocks that everyone else invests in so as to feel like they are part of the "herd" and not feel left out if they lose their money. Individuals with this mindset are unable to make financial judgments because they believe that whichever option they make, they will come to regret it in the future. Individuals usually make risk-minimizing decisions, according to the findings of (Zeelenberga, Beattieb, Pligta, and Vriesa, 1996), who go on to elucidate on the significance of regret in choice behaviour.

Mental Accounting

Based on particular criteria such as the source of income and the purpose of the money, people who practise mental accounting tend to segregate their money and investments into several categories (or multiple mental accounts). Individuals or investors may find it useful to utilise mental accounting as a form of self-control in certain situations. Due to the fact that investors have little understanding of the market, they may choose to divide their funds into investment and expenditure pools in order to avoid overspending. This allows them to treat the two mental accounts as if they were wholly separate entities, and they forego the benefits of portfolio diversification. According to Thaler (2008), investors should approach money gained from different sources differently — for example, money earned as part of a wage and money received as capital gains. Investors tend to view capital gains as more favourable than salaried income, and they are more ready to take risks with capital gains than they are with salaried income.

Disposition Effect

Individuals, according to the disposition effect, aim to achieve paper profits while avoiding experiencing paper losses, and vice versa. This means that if an investor purchases a stock at, say, Rs100 and the stock later falls to Rs85 before rising to Rs95, the vast majority of investors will not want to sell the shares until the stock rises over Rs100 once again. In order to avoid this, investors have a propensity to sell stocks whose value has climbed while retaining assets whose value has decreased – holding losers for an extended period of time while selling winners too fast! It has been suggested that investors in emerging markets such as China suffer from the disposition effect by selling companies that have grown in value rather than those that have depreciated in value (Chen, Kim, Nofsinger, and Rui, 2007).

Behavioral finance and stock investment decision

The goal of behavioural finance is to figure out how an investor's emotions and psychology influence his or her financial decisions. It is the study of how individuals in general, and investors, make typical financial decisions that are influenced by their emotions.

It's nothing more than an investigation into why otherwise reasonable people make irrational investing judgments. Planning is the process of selecting the best option from a set of options. This choice was reached after a thorough examination of all options. The most difficult and complex task for investors is making decisions. Due to many criteria such as demographics, socioeconomic background, educational level, sex, age, and ethnicity, each investor is unique in every way.

Representativeness

Investors have a tendency to think in terms of stereotypes. The success of financial judgments in the past has an impact on investors' future decisions as well, and they are more likely to discern a pattern when none truly exists. This means that investors do not take into account the law of averages and do not put any wagers on long-term trends. A greater emphasis is placed on short-term trends, such as the rise in the price of a current stock or the performance of an industry that has outperformed others in the market in the recent past. If markets were totally rational, any previous changes in stock prices should have had no effect on the future values of that particular

stock, according to conventional wisdom. That, however, is not the case in this instance. The same has been supported by Bondt (1998), who emphasises that investor evaluations are often focused on recent triumphs and failures, and as a result, investors' judgements about future investments are skewed in the same direction.

Anchoring

When making financial decisions, investors have a tendency to become fixated on a particular statistic or data. There might be a variety of reasons for this, including a large amount of data to digest, a lack of time, or just a lack of comprehension. Putting too much emphasis on a particular characteristic or 'anchoring' might result in substantial under-earning or loss of earning potential. In the long run, investors who ignore critical pieces of information and change their decisions based on a single fact are more likely to make poor decisions and lose money in the short run. Hoguet (2005) found that when asked to define a quantum, such as future expectations for the price of a stock, investors tend to "anchor" their decisions on specific pieces of information (such as the stock's price history). As a result, investors have a tendency to under react to new information.

Overconfidence

While having confidence in one's capacity to foresee and achieve above-average returns is important, having too much confidence can be damaging to one's financial selections. When investors overestimate their abilities to analyse a certain stock, company, or industry as a possible investment, they are said to be exhibiting overconfidence bias. As a result, individuals may choose to disregard any warning indications and may engage in excessive trading in a specific stock as a result of their actions. The results of these investments may be distorted since these investors do not research prior patterns or future expectations from a certain business and instead depend disproportionately on their own personal judgement when making decisions.

Gamblers Fallacy

The gamblers fallacy refers to an investor's decision-making process that leads them to assume that a trend will reverse. This is quite similar to the situation that a gambler may find themselves in in a casino. For example, if the dice has been landing on black numbers for the previous few turns, the gambler will make his or her wagers on a red number in the hope that the trend would reverse. Additionally, when it comes to investing in mutual funds, people have a tendency to assume that a company that has been underperforming for a long time would have a trend reversal, resulting in it being a smart investment.

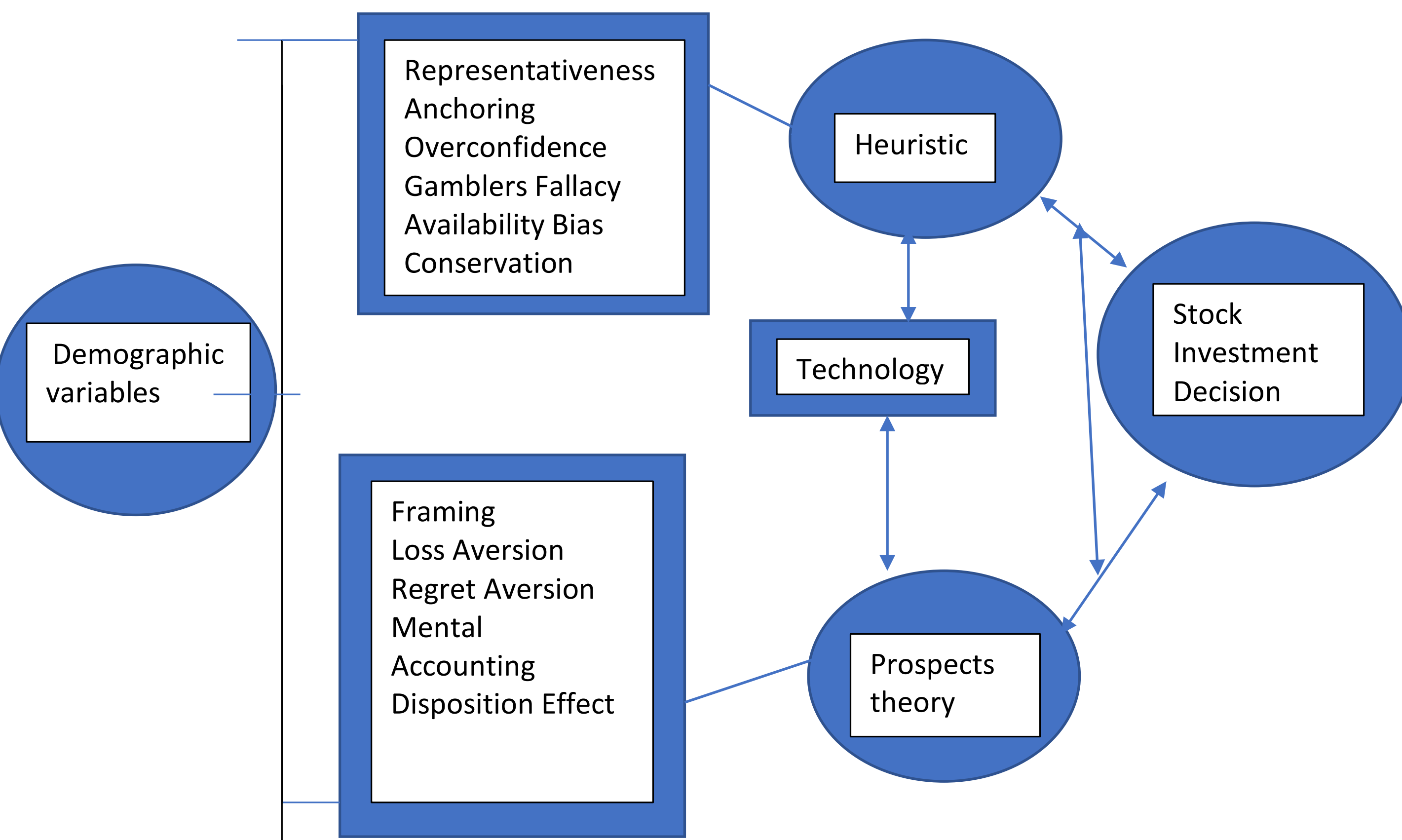
Availability Bias

People have a tendency to make judgments based on the information that is most readily available to them. The same has been witnessed in the world of investing. When making investing decisions, investors prefer to depend on specific heuristic techniques and to rely on information that has recently been in the press or that has been heard from his or her colleagues. In the case of investment decisions, information that is readily recalled at the moment of decision-making may not be the proper information, and it is more likely to result in an inaccurate conclusion. According to (Qawi, 2010), the more recent and significant an incident is, the more likely it is that it will have an impact on the decision-making process.

Conservatism

Known as conservative bias, it is the tendency to make insufficient revisions to your beliefs when confronted with fresh knowledge. Simply put, as trends shift, people may under react to the shift and may be hesitant to adapt to the new environment in which they find themselves. When they encounter new situations, they 'anchor' themselves to them and react to them in the same way they did previously. It has been stated by Singh (2012) that the conservative bias is at odds with the representativeness bias. The conservative bias may cause investors to be delayed in reacting to changes in the market as things change. If, on the other hand, there is a long-term pattern, investors will adjust to that trend and may even overreact, resulting in an inaccurate assessment of the long-term mean.

Conceptual Framework



Data collection tools and Techniques

Secondary data: Inputs for secondary research will be gathered from a variety of sources, including academic journals, trade journals, news articles, publications, RBI reports and institutional surveys, as well as discussions with market professionals. Secondary data will include information on a variety of investment alternatives, return and risk concepts as well as statistical information and other research-related inputs.

Conclusion

Behavioral finance provides explanations for why investors make irrational financial decisions on investments. It demonstrated how emotions and cognitive errors influence investors in the investment decision making process. The various causes that led to behavioral finance are anchoring, overconfidence, herd behavior, over and under reaction and loss aversions. In essence, behavioral finance approach investigates the behavioral patterns of investors and tries to understand how these patterns guide investment decision. Behavioral finance offers many useful insights for investment professionals and thus, provides a framework for evaluating active investment strategies for the investor. From this study it is clearly found out that demographics like age, gender, income, experience working pattern and education plays a major role in the risk appetite of individual investors and in their confidence level also. This study identified the major factors responsible for determining the attitudes and trading behavior of stock market investors. The most important factors that affects the attitude and trading behavior of stock market investors as obtained from factor analysis is as below: confidence level that an investors has in himself/herself as compared to formal sources, risk taking ability, more expectation and return oriented and conservative mentality.

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