PalArch's Journal of Archaeology of Egypt / Egyptology

COMPONENTS OF BEHAVIOURAL FINANCE IN INVESTMENT DECISION

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Dr. K. KANIMOZHI, Dr. T. S. ARCHANA -- Components Of Behavioural Finance In Investment Decision -- Palarch's Journal Of Archaeology Of Egypt/Egyptology 17(6). ISSN 1567-214x

Key Words: **Capital, Decision, Financial Literacy, Investment**

ABSTRACT

An investment on the basis of portfolio has become complex as people invested large sum of money even when there is a little change of investment being profitable. Most of the investors have rational expectations and maximize their utility. In the posture of investor, it is vitally important to understand why certain financial decisions are made or how people are likely to react in common conditions of uncertainty. This form of analysis is useful in an attempt to understand how a person can temper the irrational components of investment decisions while still satisfying the individual preferences and requirements.

INTRODUCTION

An efficient capital market is characterized by the fact that any information is available to all investors or market participants, so stock prices always incorporate and reflect all relevant information. Due to this issue, the price of a stock should reflect the knowledge and expectations of all investors or market participants. It is a certainty that it is not possible to separate an investor's personality and the investment decisions that he may make.

An optimum investment decision plays an active role and is a significant consideration. In designing the investment portfolio, the investors should consider their financial goals, risk tolerance level, and other constraints. In addition to that, they have to predict the output mean-variance optimization.

The concept of market efficiency involves three dimensions: allocation, operational and informational efficiency. However, it has been noted that capital markets with higher informational efficiency are more likely to retain higher operational and allocation efficiencies. Allocation Efficiency implies the optimum allocation of resources. The price of a portfolio reflect the knowledge and expectations of all investors or market participants.

ORIGINS OF BEHAVIOURAL FINANCE

Behavioural Finance emergence is based on three aspects namely psychological origin, economic origin and financial origin. The psychological origin seems to be clear in the minds of theoreticians Thaler and Mullainathan (2000),who explain clearly that behavioural finance; comes from an interdisciplinary field of finance where cognitive psychology and economics, together yield effective results. The main paradigm of psychology is cognitive psychology, social psychology, behavioural aspects, Freudian psychology and socio linguistics.

Cognitive psychology studies about internal mental process such as problem solving, language and memory (De Mijolla, 2002). It includes various aspects such as perception psychology or memory learning study. This concept was used in Gestalt psychology in 20th century by Max Wertheimer and Wolfgang Kohler. Through this concept, people can understand the objects and scenes in the simplest manner. It is also referred to as “Law of Simplicity”. Authors from behavioural finance clearly mentioned that this field of research comes from cognitive psychology. Behavioural finance should be considered to be similar to the paradigm of behaviour, which means a collection of assumptions based on comprehending the process of learning in terms of behavioural principles and these two are based upon experimental approach that will not exhibit the results in the same way.

Behavioural paradigm arrives from the internal human mind, without recourse of internal introspection. Psychology refers to thought of, something esoteric in its methods. “If anyone fails to reproduce other’s thoughts or findings, it is not due to fault in their approach or the research procedure followed or their equipment or in control of the stimulus; rather, it is due to the fact that introspection of the researcher is untrained” (Watson, 1913, p.163). Neglecting the subjective dimensions of human behaviour and by focusing only on the results of behaviour, the behaviourist approach would probably be closer to neoclassical finance (Lewin,1996).

The economic origin of Behavioural Finance deemed to happen in 1950s and slowly developed as a discipline by 1970s.Behavioural approach claims to be more descriptive than neo classical approach (Solvic et al., 1982); while prospect theory which can be seen as the first theoretical foundation of behavioural finance (Kahneman and Tversky, 1978).

Perseverance of psychological approach by economists started after 1920s only; however, psychology concepts have not developed enough clarifications through its theories to fulfil all the questions that arouse due to the emergence of a cognitive approach in economics (Coats, 1976).Behavioural economics concerns with how feelings and human attitude structure affect the decision-making process (Anger and Lowenstein, 2007).

Some economists denied that psychology could be relevant to economic theory which had a notion to focus on value and not on the motivation of people(Coats, 1976; Reynaud,1961 and Camerer &Lowenstein, 2002).Some other researchers felt that most anomalies of neoclassical finance have been enhanced due to advances in cognitive psychology and experimental economics (Aktas, 2004).

After understanding about economic emergence and psychological aspects of behavioural finance, it is about finance origins of behavioural finance that needs to be understood. In 1950'sbehavioural finance was not an identified field; rather, it was a kind of protoscience (Jovanovic, 2008).However, it is found that by using Gaussian framework, the founder of cognitive and experimental psychology, researchers tried to find statistical correlations between mass psychology and financial quotations (Fechner, 1897) and also the psychological dimensions of financial markets (Aftalion, 1927, Robert Milles, 1928 and Donner, 1941). There are researchers, who considered the complexity of human behaviour in financial theory and financial originators in understanding behavioural finance (Selden, 1912, Keynes, 1921 and Graham and Dodd, 1934).

The advancement of behavioural finance can be found in Grahams works. He wrote two books which focus particularly on investments: Security Analysis: Principles and Technique (Graham, 1934) and The Intelligent Investor (Graham, 1949). The investors' decision depends on their intelligence and he reminded the word "Intelligent" used in his second book which explains the capacity of knowledge and understanding. The notion Graham used Intelligence refers to personality and psychology of investors. Several psychological biases or anomalies used in behavioural finance can be found in the words of Graham. He wrote "The Speculative public is incorrigible". Graham was a historian and a great psychological thinker who did not consider the financial reality as fixed and a historic but rather as an evolving and historic system. Moreover, by focusing on what investors can do and not on what they ought to do, he provided descriptive approach of behavioural finance. Graham used several themes which focus about the investors' activity in behavioural finance.

OBJECTIVES OF THE STUDY

1. To analyse the investors Experience in portfolio investment.
2. To analyse the Respondents' financial literacy in portfolio investment.
3. To know the satisfaction of returns from portfolio investment.

PORTFOLIO INVESTMENT OF INVESTORS

India is a capitalist economy and individual investors are the backbone of the capital market and portfolio investment. The investment in capital market depends on the level of experience of the respondents. Only people with ample knowledge about portfolio investment will be able to invest in the right portfolio in the right time to give the desired profit and hence experience is analysed in this aspect by the researcher.

INVESTORS' EXPERIENCE IN PORTFOLIO INVESTMENT

The more the experience of the respondent, the more the knowledge of the investor in portfolio investment will be and the more the expertise will be so that it will yield profit. Hence the researcher has considered it just to analyse the number of years of experience in portfolio investment under four classifications as presented in the table below.

Table No: 1. Investors' Experience in Portfolio Investment

Variable	Investors' Grouping (*n* = 368)	Frequency	Cumulative Frequency	Percentage
Experience of investment in portfolio investment in Capital market	0–5 years	106	106	28.80
	6–10 years	78	184	21.20
	11–15 years	116	300	31.52
	16 and more	68	368	18.48
	Total	**368**		**100.0**

Source: Primary data

The analysis of the experience of investment in portfolio investment of investors, which to some extent determines the experience of the investors' investment selection and/or timing, shows that 28.8% of the respondents had less than five years securities market experience, with only 18.48% having more than 16 years.

RESPONDENTS' FINANCIAL LITERACY IN PORTFOLIO INVESTMENT

The health of a country financially is reflected by the growth of the capital market. It helps to channelize the surplus funds from savers to institutions for productive purposes. The financial investment is made depending on the level of financial literacy and knowledge of investment in securities like bonds, equities and debentures and stock. The table underneath depicts the three levels of financial literacy.

Table No:2. Financial Literacy

Literacy	Frequency	Cumulative Frequency	Percentage

High financial literacy	109	109	29.6
Medium financial literacy	125	234	34
Low financial literacy	134	368	36.4
Total	**368**		**100**

Table shows that one hundred and nine respondents that is 29.6% of the respondents have a high financial literacy one hundred and twenty five of them comprising of thirty four percent have medium knowledge about finance and only one hundred and thirty four of them that is 36.4 % of them have low knowledge about financial investment. It means that their knowledge about financial and portfolio investment terms is high. The remaining 70.4% of the respondents have medium to low financial literacy or in other words a total of two hundred and thirty four of the sample respondents have high and medium knowledge about financial transactions and only a least number of 36.4% of them have low knowledge about financial investment.

PREFERRED PORTFOLIO INVESTMENT OF INVESTORS

Corporative enterprises market their securities in different forms. The researcher has categorized the portfolio into three and they are mutual funds, Debentures and Shares. The choice of the portfolio or the choice of the best combination of capital investment should be best and properly predicted and calculated to yield a desired profit and return on investment. All investors invest only to get the desired Rate of Return on Investment. Hence the following table represents the priority given by sample investors to different investment choices.

Table No : 3. Preferred Portfolio Investment of Investors

Portfolio	Frequency	Cumulative Frequency	Percentage
Mutual funds	114	114	31.0
Debentures	35	149	9.5
Shares	219	368	59.5
Total	**368**		**100.0**

Source: Primary data

Table shows the preferred portfolio investment of investors on capital market. The researcher found out from the table above that one hundred and fourteen respondents amounting to thirty one percent preferred to invest in mutual funds and thirty five of them that is 9.5 % of them preferred to invest in debentures, while two hundred and nineteen of them that is 59.5% of them preferred to invest in shares.

Hence we can infer that a majority of respondents comprising of 59.5% of the respondents prefer to invest in shares, and only a least number of 35 respondents comprising of 9.5% prefer to invest in debentures. In other words we can infer that only thirty five persons preferred to invest in debentures and the other majority of three hundred and thirty three of the sample respondents preferred to invest in securities other than debentures.

SATISFACTION OF RETURNS FROM PORTFOLIO INVESTMENT

Satisfaction in the portfolio investment indicates the profit criteria and only if there is profit there will be satisfaction among the sample respondents and vice versa. The ratio of satisfaction of the sample respondents to the return to individuals and the contribution to the total return is to be analysed to know the nature of the satisfaction of the respondents. The following table reveals the satisfaction derived by the sample respondents.

Table No: 4. Satisfaction of Returns from Portfolio Investment

Categories	Frequency	Percentage
Individual return	265	72.0
Contribution to total return	103	28.0
Total	**368**	**100.0**

Sources: Primary data

The researcher sought to find out from respondents whether they would get satisfaction from returns of each share individually or each share's contribution to total returns. 72% of the respondents said they should get satisfaction from the returns of each share individually while 28% would get satisfaction from each share's contribution to total return. It is clear from the sample that satisfaction largely depends on the contribution to individual returns only compared to the total return.

SUMMARY OF FINDINGS

All the findings of a study to be useful by presenting it in a comprehendible manner. No study of research is of utility if it is not concretely presented in the form of a condensed report of summary. The researcher presents the crisp summary of all the findings during the course of the study with the help of this Chapter in order to be useful to the public and to the proposed investors as it will serve as a guide to involve in speculation and escape loss and obtain the desired Return on Investment. The investors entered into transactions relating to the different portfolio and the nature of the combination of investment made.

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By looking back at the conditions of other, will also not work out well because prediction of future is not possibly by any person hence on should be prudent in making decisions in investing in portfolios or in composition of portfolios.

SUGGESTIONS

Investment was made to earn profit and for no other cause. Hence the following suggestions were made on the basis of the statistical analysis made during the course of the study by the researcher.

The young investors of feminine gender should be encouraged to invest since they will be more cautious and it will improve the capital market too. The female people will generally be in money investment and hence it will be better if they are encouraged by the Government to invest through programmes in the media and other programmes like street play and other means to induce them to invest in portfolio.

The persons with less literacy level should also be trained by the Government to invest by arranging adequate training programmes. Proper awareness programmes should be arranged for the entire public to encourage them to invest in various corporate enterprises port folio. The investors should also be encouraged to invest in debentures which also help to yield interest.

The investors should be careful to invest by considering the factor of representativeness of the portfolio. The young as well as experienced investors should be prudent in deciding the ratio of investment in different portfolio. Due care should be given by the young as well as experienced investors not to indulge in herding which is a bias which is dangerous.

CONCLUSION

Investment in portfolio is a complex task which should take into account all factors such as internal as well as external factors of a Corporate Enterprise. Activities of the corporate organization, the internal factors such as the factors of production, resources, economic and government factors and all other factors which are unforeseen should be considered while investing in the capital market. All the possible controllable factors should be considered before investing in portfolio and in the right composition of the portfolio investment.

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