International Journal of Trend in Scientific Research and Development (IJTSRD)
Volume 4 Issue 1, December 2019 Available Online: www.ijtsrd.com e-ISSN: 2456 – 6470

Influence of Psychological Factors on the Investor's Trading Decisions with Reference to Equity Market - an Insight

Dr. H. Prakash[1], Rekha D. M[2]

[1]Director and HOD, [2]Research Scholar,
[1]Department of Commerce, Maharani Cluster University, Bangalore, India
[2]Department of Commerce, Central College Of Commerce, Bangalore, India

ABSTRACT
The influence of psychological factors on the investors' trading and investment decisions and its subsequent impact on capital market is studied with the concept of behavioural finance. Behavioral finance, which is a recently popularized paradigm in the financial market analysis, analyses the influence of human psychological factors on the financial market's evolution. In other words, behavioral finance analyses the financial market inefficiency in the light of the psychological perspectives and theories. The psychological principles of behavioral finance include the analysis of various factors, such as overconfidence, heuristics and biases, emotion and social forces, etc. This analysis is helpful in understanding the ability of the investor to temper the irrational components of investment decisions while satisfying their individual requirements and preferences. However, the traditional models failed in explaining and solving the anomalies of the financial market and this failure cemented the application of the behavioral finance model, which clearly explains the motivation behind the individual in taking a specific decision regarding the investment. This paper is giving an insight into the investment decision making and trading behaviour of individuals is influenced by the psychological factor which also states that the performance of portfolio and its implications on equity market is also affected.

KEYWORDS: *Psychological factors, investment decisions, equity market and investor's trading*

How to cite this paper: Dr. H. Prakash | Rekha D. M "Influence of Psychological Factors on the Investor's Trading Decisions with Reference to Equity Market - an Insight" Published in International Journal of Trend in Scientific Research and Development (ijtsrd), ISSN: 2456-6470, Volume-4 | Issue-1, December 2019, pp.590-593, URL: www.ijtsrd.com/papers/ijtsrd29637.pdf

IJTSRD29637

INRODUCTION

The stock markets play an important role in the economic growth of India, as our country looking towards rapid industrialization and the growth is depending on the number of business organizations' which need huge capitals. The companies look forward equity markets as the primary source to obtain the required capitals. This dependency directly reflects in the growth parameters, such as GDP and per capita income and in turn which also reflects the performance of the economy. This development in turn requires the investor's interest to invest in the equity market, which itself depend on various factors which include social, economic, company oriented and investor's behavior in order to choose equity investment option as an investment avenue which also give good rate of return to them, again this depends on the business performance.

Behavioral finance, which is a recently popularized paradigm in the financial market analysis, analyses the influence of human psychological factors on the financial market's evolution. In other words, behavioral finance analyses the financial market inefficiency in the light of the psychological perspectives and theories. It is considered as an effective alternative to classical finance (Birau, 2012), which assumes investors are rational and the capital markets are efficient, and hence it's impossible to outperform the market over the long-term. However, the traditional models failed in explaining and solving the anomalies of the financial market and this failure cemented the application of the behavioral finance model, which clearly explains the motivation behind the individual in taking a specific decision regarding the investment.

The efficient markets Hypothesis assumes that the capital market is information ally efficient, on the other hand, behavioral finance considers that the financial markets are information ally inefficient in certain circumstances (Ritter, 2003). Behavioral finance provides very complex and unconventional perspective, it signposts the influence of psychological and emotional factors in the investment decision of an investor. The concept explains how the human emotional complexity, which includes anxiety, panic, fear, envy, greed, ambition, vanity, euphoria or satisfaction influences his investment mentality and examines to what extent these influences and play a role in the financial investment decision making (Birau, 2011). The psychological principles of behavioral finance include the analysis of various factors, such as overconfidence, heuristics and biases, emotion and social forces, etc. This analysis is helpful in understanding the ability of the investor to temper the irrational components of investment decisions while satisfying their individual requirements and preferences. Considering the above factors, this study, by analyzing the psychological factors of investors, attempts to provide an insight about the influence of psychological factors on the investors' trading and investment decisions and its subsequent impact on the equity market in India.

REVIEW OF LITERATURE:

Daniel Et Al. (1993): He tries to explain by constructing a model of investors sentiments aimed at reconciling the empirical findings of over reactions and under reaction to the market information. Here he discusses about the psychology of investors which motivates them to identify the various portfolios on which various theories has been constructed where certain psychological factors will be playing a major role in decision making.

Shefrin, 2000; Shleifer, 2000; Warneryd, 2001: It is generally believed that investment decisions are a function of several factors such as market characteristics and individual risk profiles, in addition to accounting information. The disposition error shows that regardless of accounting information, investors are influenced by sunk cost considerations and asymmetrical risk preferences for gain/loss situations.

Nagy and Obenberger, (1994) which examined factors influencing investor behavior, suggested that classical wealth – maximization criteria are important to investors, even though investors employ diverse criteria while choosing stocks. Contemporary concerns such as local or international operations, environmental track record and the firm's ethical posture appear to be given only cursory consideration.

Hussein A. H, and Dimitrios I. M, (2007) found that expected corporate earnings, get rich quickly, stock marketability, past performance of the firm's stock, government holdings, and the creation of the organized financial markets are the investors considerations and also found that individual investors rely more on newspapers/media and noise in the market when making their investment decisions, while professional investors rely more on fundamental and technical analysis and less on portfolio analysis.

(Francis and Soffer, 1997): Market participants are exposed to a constant flow of information, ranging from quantitative financial data to financial news in the media, and socially exchanged opinions and recommendations. Processing all this information is a difficult task. Variables that are loaded heavily on this factor include coverage in the financial and general press, recent stock index returns, information obtained from internet, current economic indicators and recommendations by investment advisory services. Each of these variables represents an outside source of information that is perceived to be unbiased.

Baker, Haargrove and Haslem (1977) propose that investors behave rationally, taking into account the investment's risk/return trade off which also examines and states the factors that appear to exercise the greatest influence on the individual stock investor and included not only the factors investigated by previous studies by also some of the prevailing behavioral finance theories.

Keller and Seigrist (2006): They examined the investor's attitude towards saving, financial matters, gambling obsession with money, etc. and its influence on their decision making. It states that the attitude towards buying and selling securities, risk tolerance to maximize the capital and price fluctuations along with the inclination with socially and environmentally responsible investments have an impact on their investment behavior.

Tamil Selvi (2015) conducted a study to assess the influence of investor's attitude on their investment decisions. It also mentions that there are lot many analyses which state the specific factors and also the psychological factor exists behind in order to influence these factors in the decision making regarding the investment.

Donkor, Akohene and Acheampong (2016) examined whether the behavioural factors, including overconfidence and anchoring have an impact on the investment decisions of the investors in Ghana. The research study exhibited that the bankers' investment decisions were largely influenced by the heuristic factors, such as anchoring and overconfidence. The findings revealed that the bankers often tend to be overconfident during the making of investment decisions. Furthermore, the decisions were also influenced by the experience of their past performance also.

Pak and Mahmood (2015) examined the impact of personality traits on the individual's risk tolerance and hence on the investment decision making process of the individuals. Here it is explained that the risk tolerance, which had a direct relationship with the personality traits, influenced the investment decisions of the investors to a greater extent.

Objectives of the Study:

The main objectives of this study are:
1. To examine the psychological factors influencing the investment decision of investors.
2. To analyse the investors investment trading behaviour.
3. To know about the impact of trading behaviour of investors on equity market.

Statement of problem:

India is proven with a developmental trend nowadays especially with the growth of industries. These industries require sufficient funds flow from the capital market. A positive trend in the stock market will significantly affect the development of the economy and vice versa. This makes the decisions of investors a important factor, which plays a major role in setting the equity market trend. This context necessitates the exploration of the relationship between investor's trading behavior and their impact on investment avenues which also impacts equity market. This motivates the researchers to conduct analyse the impact of different behavioral factors of the investor on their investment nature. Therefore this study aims at finding the behavioral factors which influences the investment and its impact on their investment performance.

METHODOLOGY:

Data for this study is purely based on secondary sources such as books, journals, articles and also internet.

Analysis:

The economic prosperity of any nation relies on its financial system. The effective functioning of financial market directly depends on the nature of investments by the investors which necessitates the exploration of the relationship between investor's behavior and their investment nature. Thus, the development of healthy equity markets is a vital factor for the rapid economic growth of the nation. This in turn requires the investor's interest to invest in the equity market, which itself depend on various factors such as, social, economic, company oriented and investor's behavior. Among these factors, the behaviour of the investors plays a major role in determining the investor's decisions. In this context, the present study examined the influence of various behaviour factors in the decision making of investors. The study attempted to provide an insight about the influence of various psychological factors on the investors' trading and investment decisions and its subsequent impact on the equity market in India. Further the investment decision of the investor impacts their investment pattern which possibly involves the choice of different avenues made available for them in financial market. Since the investment pattern involves investing the hard earned money into different long-term and short-term monetary plans, the investors plan their avenues based on certain factors which influence them in making decisions which states that investment performance of portfolios depends on the respondent's choice of investment pattern. By considering certain psychological factors the analysis was done to find out whether the psychological factors will influence the investor's decision making and their trading behaviour and the research says that the investor focuses on present requirement with an assumption that the savings is given much priority than expenditure for today and also the future income, i.e. the average income receivable now and in the future in order to maintain more or less the same level of consumption throughout the entire life with this regard more and more investment avenues are identified and selected.

Fama (1991) analysed in his research and stated that the market is efficient and market participants hold all necessary information required for decision making in order to make an investment in financial market as more uncertainties are attached with the equity or investment market. Investigators of individual behavioural finances Le Bon (1896), Raiffa, Raiffa (1968), Kahneman and Tversky (1979) noticed that behaviour finance theory, the behaviour of an individual differs from that in practice and also states that the conventional theory of investments could not explain and predict all financial decisions. Criticism was mainly concentrated on the fact, that profit maximization criteria could be less significant for an investors as they wants to gain sufficient profit to satisfy personal demands in present as well as in future where return and risk as to be considered equally to balance their portfolio(Вамeнкo 2007). The research revealed that the investors behavioral factors such as heuristic, prospect, market factors and herding behavior positively influences their investment decision. Further the investment decision of the investor impacts their investment pattern which possibly involves the choice of different avenues such as stocks, bonds, mutual funds, etc. Since the investment pattern involves investing the hard earned money into different long-term and short-term monetary plans.

Behavioural factor analysis:

A. Heuristic factors

According to (Ritter, 2003) the heuristics are defined as "the thumb rules, which creates decision making much easier, by the reduction of the complexity of probability evaluation and prediction of the values to make judgements easier in uncertain and complex environments wherein the investors based on certain information available to them and their own analysis and thoughts their investment pattern is framed.

B. Prospect factors

Basically the prospect theory highlights the influence of the investors' psychological value system on subjective decision-making. The theory explains that certain mind set of investors towards their investment patterns, selection of securities, selection of portfolios etc. are based on their future growth aspects wherein the growth of investment is expected and which also affect the investor's decision-making processes.

C. Market factors

As per the research made under this factor for which the investors will get influenced the market factors are particularly related to market, including market information, Price changes, customer preference, past trends of stocks and fundamentals of underlying stocks, which could have a certain impact on investors' decision making. Generally, changes in the stock price, market information and fundamentals of the underlying stock can become a source of over/under-reaction of investors to the price change and these changes can effectively influence the decision-making behavior of investors.

D. Herding

Herding where "the investor's tendency to follow to others' investment and trading actions" has resulted in some of the investors who don't have knowledge about fundamental and technical analysis of investing into the stock market will definitely go by other's perspective and decision in order invest in securities.

These are the major factors considered for the research study to know about the psychology of the investors which influence their decision making and trading.

Findings and Conclusion:

1. The analytical review of various theories and models of behavioural finances have a large practical value as they allow explaining the events in the market and predicting the behaviour of investors in different situations as well as in comparison with the developing efficient market strategies.

2. Financially investors are attempting to be successful in the financial market. They could be non-conscious of their financial decisions, as they can't always justify the financial motives, and, with a degree of uncertainty, their behaviour is irrational in terms of a certain risk level.

3. The identified behaviour factors of investor's confirm the necessity to consider behavioural factors in managing financial decisions of an individual. And also indicates that the behavioural factors will also have an influence and related to the investment decisions made by them on various investments in equity market.

4. The investors behavioral factors, including heuristic, prospect, market factors and herding behavior positively influences their investment decision. Further

the investment decision of the investor impacts their investment pattern which possibly involves the choice of different avenues such as stocks, bonds, mutual funds, etc.

5. The investors are very much skeptical in their investment based on the stock price predictions as the majority suffered huge losses by going after the predictions. Hence, the majority prefers to invest in the stocks with good past earnings and showed skepticism in investing in the stock which had made a loss in recent trading where it identifies heuristic nature and behaviour of investors.

References:

[1] Agrawal, D., Singhal, T., & Swarup, K. S. (2016). Role of Herding Behavior in Influencing Investor Decision Making in India. Indian Journal of Research in Capital Markets, 3(4), 43-48.

[2] Anum, B. A. (2017). Behavioral Factors and their Impact on Individual Investors Decision Making and Investment Performance: Empirical Investigation from Pakistani Stock Market. Global Journal of Management and Business Research.

[3] Bakar, S., & Yi, A. N. C. (2016). The impact of psychological factors on investors' decision making in malaysian stock market: a case of Klang Valley and Pahang. Procedia Economics and Finance, 35, 319-328.

[4] Birău, F. R. (2011) Behavioral Finance Paradigm And Its Implications On Investment Decisions, International Scientific Conference „ECO-TREND 2011 - Exit From The Crisis And Revival Of Sustainable Growth", 8th edition, November 25-26, Tg – Jiu, Romania.

[5] Birău, F. R. (2012). The impact of Behavioral finance on stock markets. Annals of the Constantin Brâncuşi" University of Târgu Jiu, Economy Series, 3, 45-50.

[6] Donkor, J., Akohene, V., Acheampong S (2016) Behavioural Factors and Investment Decisions of Bankers in Ghana, British Journal of Education, Society & Behavioural Science 18(3), 1-8.

[7] Geetha, N., & Ramesh, M. (2012). A study on relevance of demographic factors in investment decisions. Perspectives of Innovations, Economics and Business, 10(1), 14-28.

[8] Gumus, F. B., & Dayioglu, Y. (2014). An Analysis on The Socio-Economic and Demographic Factors That Have an Effect on The Risk Taking Preferences of Personal Investors. International Journal of Economics and Financial Issues, 5(1), 136-147.

[9] Keller, C., & Siegrist, M. (2006). Money attitude typology and stock investment. The Journal of Behavioral Finance, 7(2), 88-96.

[10] Lam, J. (2014). Enterprise risk management: from incentives to controls. Hoboken, NJ: John Wiley & Sons.

[11] Mahalakshmi, T. N., & Anuradha, N. (2018). Factors affecting Investment Decision making & Investment Performance among Individual Investors in India. International Journal of Pure and Applied Mathematics, 118(18), 1667-1675.

[12] Obamuyi, T. M. (2013). Factors influencing investment decisions in capital market: A study of individual investors in Nigeria. Organizations and markets in emerging economies, 4 (1), 141-161.

[13] Pak, Olga & Mahmood, Monowar. (2015). Impact of personality on risk tolerance and investment decisions. International Journal of Commerce and Management. 25. 370-384. 10.1108/IJCoMA-01-2013-0002.

[14] Parkash, R., Awais, M., & Warraich, U. A. (2014). Do Socio-Economic factors really Influence risk taking Behavior of individual Investors?. Research Journal of Management Sciences, ISSN, 2319, 1171.

[15] Selvi, T. (2015). Investors Attitude towards Investment Avenues. International Journal of Management and Commerce Innovations, 3(1), 717-722.