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How Common Indian People Take Investment Decisions: Exploring Aspects of Behavioral Economics in India

Satyam Mehta
UniteSync
New Delhi, India

Nirbhik Deb Chowdhury
UniteSync
New Delhi, India

Ananay Rajput
UniteSync
New Delhi, India

Abstract:- Although investing and finances are known to be subjects where humans are supposed to exercise the highest rationality in making informed decisions, it must not be forgotten that human beings are incomplete without their emotions and that these affective processes of the human mind dictate and influence their cognitions and conations as well. Thus, leading to the influence of emotions in decision-making wherein rationality starts losing its grip as soon as the emotions overwhelm. With these theoretical underpinnings, the current study aimed to understand the public perception about investing in the market and the financial literacy of the common people of India. With online survey questionnaires that collected 127 responses, we report the different perspectives of investments and investing dynamics of five different age groups: 0-18 years, 18-30 years, 30-45 years, 45-60 years, and more than 60 years. We also found out that Indian investment professionals in the sector sometimes do let their behavioural instincts and emotions take over their investment decisions. We conclude by saying that irrationality in the market is essential for its survival.

Keywords:- *Finance, Behavior, Behavioral Finance, Mining, Mineral Sector.*

I. INTRODUCTION

Behavioral finance refers to the psychology and the mindset of investors in financial decision-making. Humans are incomplete without emotions and these emotions influence financial decisions. Every decision-making process of humans is clouded by an overwhelming number of emotions, which deeply influences our actions. Basic behavioral factors affecting investors, according to Fischer and Gerhardt (2007) are fear, love, greed, optimism, herd instinct, the tendency to focus on recent experience, and the tendency to overestimate oneself. There are various biases that affect and influence decision-making in humans, like anchoring, loss aversion, etc. which will be discussed later in this paper. Biases are a huge factor in these decisions, which can lead them into an emotional rollercoaster. Although, a common notion is that positivity and self-belief attract positive results, any kind of emotion, whether self-affirming or pessimistic can greatly affect an investor's purchasing tendencies, thereby largely affecting returns (Louro et. al, 2005). Several studies have comprehensively covered the entanglement of human behaviour and investment decisions and how these two aspects are inseparable (Baker & Ricciardi, 2015; Statman, 2015).

Overcoming emotions and thinking rationally would yield investors the best and safest results, however, the quest for becoming logical itself entails a plethora of behavioural aspects. Psychologists suggest investors keep their inner mindsets in control and think rationally and logically for their investments. Since psychology explores human judgment, behaviour, and welfare, it can also provide important facts about how human actions differ from traditional economic assumptions. Behavioral finance as science became seriously popular after 2002 when Daniel Kahneman was awarded The Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel for having done psychological research into economic science, human judgment, and decision-making under uncertainty. In this paper, we study behavioural finance and its factors and also examine different biases along with the importance of irrationality in the market.

Behavioral finance incorporates cognitive psychology into conventional finance, suggesting that people are prone to various heuristic-driven biases in the decision-making process (Hayes, 2021). The two important aspects of behavioural finance are Individual investors and the entire market. This is also known as micro and macro behavioural finance respectively. Micro behavioural finance deals with individual investor mentality while macro behavioural finance deals with the anomalies of the market and herd.

The definition of behavioural finance dates back to the early 18th century, Adam Smith *The Theory of Moral Sentiments* determined emotional human interactions. Some of the basic behavioural elements in this were pride, disgrace, insecurity, and egoism. It tried to explain the actions of a man and the pursuit for profit (Smith, 2010). In the 19th century, when the economy was mostly dominated

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by neoclassical theories, the concept of psychology in finance and economics started to displace which had an effect on the discourse of economy until the mid of 20th century. For decades, psychologists and sociologists have pushed back the theory of mainstream finance and economics, arguing that humans cannot always be fully rational and have their own capacity and ability and that markets are not efficient in the real world (Kapoor and Prosad, 2017). The field of behavioural finance arose in the late 1970s to address these issues, accumulating a wide number of cases and evidence where people systematically behave “irrationally” (McClure, 2021). Goldberg et al. (2001) defined behavioural finance as financial market theory; a subject that is applied to facts. People behave rationally only within specific limits. Thaler (1999) stated that behavioural finance is an integration of basic economics and financial theories including investigating psychology and decision making.

II. OBJECTIVE

The aim of the present study is to gain an overview of the public perception and behavior concerned with investing. The primary objective is to understand an Indian common man’s financial literacy, aspirations and goals.

III. METHODOLOGY

In order to elicit responses from a wide range of respondents so as to reach a richer and broader understanding of people’s views relating to investing and to understand their financial literacy, two survey questionnaires were designed using Google Forms. The two surveys extensively covered the financial knowledge, aspirations, and behavioural reactions of the respondents to specifically tailored cases mimicking real-life market volatility and inherent biases. The first survey’s scope was broader seeking to understand the financial goals, expectations, and expertise of the respondents. The majority of the survey questions fell under the categories of investor experience, investor expectations, and tendencies. The second survey however intended to attract a more concentrated audience, ones with real experience as an investor. The ultimate objective of the second survey was to comprehend the biases and reactions of investors which surface when the markets demonstrate unexpected or unprecedented volatility, contrary to the investor’s speculation. The survey, through a series of case scenarios that mirror critical emotion-inducing circumstances faced by every investor, seeks to gather data on how each individual reacts to the ever-evolving equity markets and how their inherent biases might affect their sale or purchase decisions. The survey questionnaires were then floated on various groups through social networking platforms in order to reach a bigger sample. The responses gathered through the survey were then analysed using Microsoft Excel.

IV. RESULTS

We collected a total of 127 responses through our survey to get an insight into the mindset of Indians belonging to various age categories about investments. For better clarity and understanding, we have grouped the responses into 5 different age groups that include the age groups of 0-18 years, 18-30 years, 30-45 years, 45-60 years, and more than 60 years. The results received from each of the age groups have been mentioned below.

1.0-18 years: We found out that even though this age group was not able to invest due to legal obligations, they did possess some passable knowledge about investments. However, this knowledge is only limited as they only look at gaining high returns and do not know about the risks involved.

2.18-30 years: This is the group that reported to have just started earning through jobs or internships. As a result of that, they were found to have some basic knowledge about the shortcomings of investing. They mentioned being usually investing in either the stock market or cryptocurrency.

3.30-45 years: This group was found to be usually knowledgeable about savings, investments, etc., and reported to be often investing 15-50% of their savings depending on their knowledge and experience.

4.45-60 years: This group was found to have a low-risk appetite and reported to be usually investing 0-30% of their savings, as they did not want to risk a majority of their savings as most people in this age group start planning their retirement. Hence, this group was found to be mostly risk-averse. Though this group was found to be investing less amount of their savings, they did acknowledge their tendency of looking at various significant factors other than high returns for their investments.

5.More than 60 years: In this age group, people were found to be investing less and safe, however, an important difference was noticed in this age group that reflected their knowledge and experience. It was found that, unlike youngsters who invested a majority of their money into one or two assets, this older group divides its savings among multiple assets, hence diversifying their investment. As compared to the other groups, this group was reported to be having the lowest risk appetite as most of the population belonging to this age group start to retire during this time.

In general, we observed that people belonging to different age groups had contrasting responses whereas people belonging to the same age groups more or less had a similar mindset to the idea of investing. We also found that a majority of people invest in SIPs, mutual funds, and Life insurance. We found out that the most prominent factor taken into consideration before investing are high returns followed by risk appetite and dividends. Most people who chose high returns comprised of youngsters of age 0-30 years. Furthermore, the people who chose either risk

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appetite or dividends were somewhat skillful in the field and knew about the repercussion of going only after high returns. We also had the chance of observing that a majority of people are influenced by the media's perspective and also by the advice of their friends or relatives. Compared to this, a very small percentage of people take recommendations from their broker or financial advisor. Otherwise, it is evident that a majority of people invest according to their self-awareness and research undertaken by themselves.

V. DISCUSSION

Theoretically, the benefits of being rational for investing and economics have been put forward strongly. However, the current study makes evident the fact that putting this rationality to use in the practical world is nearly unachievable by common Indian people. The investigators hereby conclude that irrationality in humans cannot be done away with and it shall always influence the economy and markets in some way or the other.

Investors are constantly encouraged to always think rationally and logically for their investments, but that is, of course, not always possible as noticed in the present study. Mistakes are bound to happen and almost every investor has made some mistake or the other. The basic definition of economics has humans in it, and irrationality and humans will always coexist, affecting our decisions. Humans cannot be rational in every situation and only programmed bots can perform in such a manner.

This irrationality can be caused due to things like first impressions, loss aversions, familiarity, and prediction of an asset's future. In addition, it is noted that accumulated investment experience of the investor has no significant effect on the number of errors. Some theorists contend that if investors are rational, then the market price for all securities will reflect fundamental values; that is, future cash flows discounted by a rate of return that accounts for risk. Ramiah et al., (2014) opined that "Overconfidence on the part of these investors leads them to trade anyway. This overconfidence provides market liquidity, but more importantly, provides the market with the private information that individual investors possess (but should, rationally, withhold)." A balance between rational and irrational investor behaviour is required to maintain market liquidity.

If everyone thinks logically in the market, then every person would be able to invest their money in the best asset for the future, leading to a lot of investments being made in the same asset. This will lead to the degrowth or reduction of the value of that asset. A real-world example of this is that a particular thing is worth something because of its rarity. If that thing starts to be produced or found in bulk, then it will cause a reduction in its worth. Hence, reforms designed to save investors from the costs of their cognitive errors would reduce market liquidity and deprive the market of valuable information. In short, markets need irrationality (Blanc & Rachlinski, 2005).

VI. CONCLUSION

To conclude, we acknowledge and affirm that the study of behavioural sciences is important to know and understand the psychological factors that influence the decision-making of investors. These studies give us an insight into the emotional quotient of various investors. This field contests the standard finance theories and presents us that investors in real life work according to their investment biases. As our study noted, we also see that investors of varied age groups in India think similarly and react to investing factors in a similar fashion and that professional and experienced Indian investors have somewhat same reactions to the market however their actions are different.

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