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Research Article

Influence of Behavioral Finance in Making Investment Decisions

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ABSTRACT

Humans operate logically while making financial decisions, according to numerous conventional financial theories. Various studies have revealed, however, that there are instances in which human behavior is impacted by moods and emotions, causing individuals to react in an unexpected or unreasonable manner, impacting their decision making. Whether an individual's demographic and psychographic features impact behavioural investment decision making is an uncharted field. This study examines an important demographic variable, gender, and aims to determine how much the variable impacts investment decision making. The study's goal is to determine if gender differentiation influences investing decisions and to what degree men and women investors are impacted by behavioural factors. The study has significance for the financial sector since it aims to assess how behavioural and psychological aspects impact various investors based on their basic gender distinction, and it will also assist to design the portfolio depending on their investing preferences.

Keywords: Behavioral Finance, Investment Decision Making, Gender Differentiation, Risk Appetite, Anchoring Bias.

Introduction

Despite significant progress and advancement in Science and Technology, one issue remains unanswered: why do people behave the way they do? A variety of human behaviour research conducted by many schools of thought has failed to effectively anticipate and comprehend human behavior. Philosophers, Social Scientists, Psychologists, and Management Experts have developed a plethora of theories and methodologies, yet they have never been sufficient to open Pandora's Box

The Human Mind

Finance is primarily concerned with investment decisions, working capital decisions, dividend decisions, and money allocation decisions, whereas economics is concerned with production decisions such as what to create, how to produce, and for whom to produce. Similarly, the burgeoning area of behavioural finance is concerned with the complicated process of decision making. Though economics and finance have contributed numerous theories throughout the years, they have not been able to explain why individuals occasionally make illogical financial decisions. Humans' illogical behavior has given rise to a new research topic in finance called as "Behavioral Finance." This is a relatively new branch of financial study that attempts to explain why people make specific types of financial decisions by combining behavioural and cognitive psychology theories with traditional economics and finance. As a result, behavioural finance has arisen as a new area that investigates the impact of psychology and emotions on financial decision making.

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The study's primary objective is to critically investigate behavioural finance theories and numerous behavioural aspects, as well as to identify the many challenges involved in investing decision making with regard to male and female investors. There is ample data to show that when it comes to financial decision making, humans do not always act rationally, and individual personality and emotions have a significant part in the outcome. Because the emotional stability of male and female investors differs, this study seeks to investigate how it influences investing decisions. The study also looks at the psychological aspects that influence investing decisions in terms of gender differentiation. The following psychological elements are taken into account: financial goal clarity, risk appetite, and anchoring bias.

Literature Review

(Nichlas Barberis, 2002): In this research study, behavioural finance proposes that some financial occurrences may be explained by models in which some agents are not totally rational. Limits to arbitrage, which contends that it can be difficult for rational traders to reverse the dislocations generated by less rational traders, and psychology, which catalogues the types of departures from complete rationality we could anticipate to observe, are the two building blocks of the discipline.

Barberis, Huang, and Santos (2001) investigated asset prices in an economy in which investors derived direct utility not only from consumption but also from fluctuations in the value of their financial wealth, and they preferred to be loss averse over these fluctuations, the degree of which depended on their prior investment performance. This approach aided in understanding the high mean, excess volatility, and predictability of stock returns, as well as the link with consumption growth. Prospect theory impacted the model's construction, while studies conducted by Barberis, Huang, and Santos (2001) offered data on how prior results affect hazardous decisions.

In India, relatively few research on gender-specific investment behaviour have been undertaken. A study on Investment Decision Making by Pal and Gill (2007) was an intensive empirical analysis that discovered that female investors had lower levels of investment awareness, confidence, and risk tolerance capabilities and were more cautious about their investment, whereas males had the opposite attitude toward their investment.

The various concepts of behavioral finance proposed by various researchers which determine the judgment and decision making are as given below:

Representativeness: Kahneman and Tversky (1972) defined the representativeness heuristic as a notion utilized when making judgements about the likelihood of an event when one is unsure of something. Representativeness was defined by Kahneman and Tversky (1982) as the degree to which an event's features are comparable to those of its parent population. The concept of representativeness is evaluating an event and determining how closely it relates to other events observed in the general population.

Overconfidence: In an experiment, Dittrich, Guth, and Maciejovsky (2001) discovered that two-thirds of the participants are overconfident. They also investigated whether or whether investors became more confident after losing money. Confidence provides individuals greater boldness, which is essential for success. Self-confidence is always seen as a desirable attribute, but occasionally investors overestimate their expertise and knowledge, which leads to excessive trading.

Anchoring is a cognitive notion established by Tversky and Kahneman (1974) regarding the human mind's inclination to tie or anchor their ideas to a reference point, even when there is no logical significance or justification for their judgments. Human people assess the end result by beginning with values regarding various conditions. That primary value might represent a partial calculation or the start of a problem. In both circumstances, modifications are insufficient (Slovic & Lichtenstein, 1971). Different introduction points provide various approximations, which lead to primary values.

Objectives of the Study

The study's main goal is to determine whether gender differentiation influences investing decisions and to what degree men and women investors are impacted by behavioural bias.

Methodology of the study

The study focused on the clarity of financial objectives, risk appetite, and the impact of anchoring bias on male and female investors. The study made use of both primary and secondary data. Secondary data was gathered from many publications and books. A systematic questionnaire was used to obtain primary data. Individual households were chosen for study because it was anticipated that they are less likely to have information about the use of behavioral theories in decision making and, as a result, would submit responses to the questionnaire without bias.

The study used a descriptive research methodology and relied heavily on primary data for analysis. The study employed a non-probability sampling strategy that was a hybrid of convenience and purposive sampling. Individuals who earn a living and are active or interested in investing were used as a sample. The final size of the sample was 60 respondents. The chi-square test was used for inferring the collected data. The study is limited to the Krishna region only.

Hypothesis

The following null hypotheses were formulated to study whether gender difference has any significant impact on investment behavior and vulnerability to concepts of behavioral finance.

H1.1: There is no significant difference between male and female investors with regard to risk appetite.

H1.2: There is no significant difference between male and female investors with regard to exposure of anchoring bias.

Data Analysis and interpretation

Risk appetite

Risk appetite refers to whether investors are prepared to face risks in exchange for a high return. The degree of variation in return on investment that an investor can tolerate is determined by the investor's risk tolerance. Investors that are willing to take a high risk for a high return are known as aggressive investors, while those who are unwilling to take any risk for their investment and are content with the lowest potential profits are known as cautious investors. The replies of male and female respondents on their risk appetite are presented in the table below.

Table 1.Risk Appetite and Gender

Risk Appetite	Gender		
	Male	Female	Total
High Risk Seeker	6	1	7
Moderate Risk Seeker	4	1	5
Risk Neutral	10	16	26
Risk averse	14	8	22
Total	34	26	60

Since the calculated Chi-Square value =11.163 is less than the critical value, the null hypothesis is rejected. Also, by comparing the P- Value = 0.011 with the significance level of 0.05, the null hypothesis is rejected. This means there is a significant difference between male and female investors with regard to risk appetite.

Anchoring Affect

Anchoring is a cognitive heuristic in which decision are made based on an initial anchor. That initial anchor could be any information received from friends or some other source. Table 4 and Figure 4 show that there is no gender differentiation in terms of anchoring bias and both genders get less influenced.

Since the calculated Chi-Square value =1.777 is less than the critical value, the null hypothesis is not rejected. Also, on comparing the P- Value = 0.411 with the significance level of 0.05, the null hypothesis is not rejected. It means there is no significant difference between male and female investors when it comes to anchoring bias in their investment decision.

Table 2.Anchoring Affect and Gender

Anchoring Effect	Gender		
	Male	Female	Total
Get influenced by Information	10	6	16
Not always get influenced by Information	10	8	18
Do not get influenced by Information	14	12	26
Total	34	26	60

Findings and Conclusion

The study's empirical findings reveal that both male and female investors are highly clear and focused on their financial goals when investing, and that both genders are impacted by anchoring bias while investing. However, there is a considerable disparity in risk appetite across the sexes. According to the empirical findings, males are more likely to engage in risk-taking and risk-averse behaviour than females, whereas females are more likely to engage in risk-neutral conduct. As a result, we may conclude that male investors invest and respond based on their return and safety expectations. The prospect of higher profits pushes individuals to take on greater risk, and when they seek safety in their investments, they become risk averse

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