THE INFLUENCE OF BEHAVIOURAL FACTORS ON FINANCIAL DECISIONS

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Abstract*: Although finance has been studied for thousands years, behavioral finance which considers the human behaviors in finance is relatively a new area for study. Finance is considered as the life blood of every industrial concern. Every concern invests to meet their financial needs for better growth in future. But financial investment decisions are directly influenced in a large proportion by psychological and emotional factors. These behavioural factors may be enthusiasm, greed, fear, ambition, satisfaction, etc. Classical finance believes that investors are rational and they are focused to select an efficient portfolio, which means including a combination of asset classes chosen in such a manner as to achieve the greatest possible returns over the long term, under the terms of a tolerable level of risk. Financial investors are people with a very varied number of deviations from rational behaviour, which is the reason why there is a variety of effects. So, Behavioural finance utilises knowledge of human psychology to explain irrational investor behaviour that is not being captured by the traditional rational based models. The objective of the research article is to identify the behavioural factors and also find out the relationship between the factors and the financial decisions of the investors. To attain this objective various respondents from investment banks in Karnal have been studied through sequential structured questionnaire. Drop and pick later method was used to distribute the questionnaire and a pilot study was used to verify reliability and validity of the questionnaire. Descriptive statistics, chi-square test and correlation analysis were used to summarize the research findings. The outcome of these decisions gives the results in the form of investment performance and satisfaction to the different investors.

***Keywords*: behavioral finance, classical finance, financial investor, investment decision, market efficiency, psychological factors, rational behavior.**

1. PROLOGUE

Behavioral finance is the study of the influence of the psychological factors on financial markets evolution. In other words, financial markets inefficiency is analysed in the light of the psychological theories and perspectives. Behavioural finance is defined as a theory that associates the psychological variables and their emotional responses with the personal and general economic conditions (Swell, 2008). It combines both psychology and economics to explain how and why investors act the way they do, and to analyze how that behaviour has an effect on the market (Vias, 2006).

In today's financial era, behavioural finance is relatively a new field and has become a subject-matter of keen interest to financial analysts and decision-makers. Due to globalization and advanced information technology, the financial environment has become dynamic and competitive. To stay competitive in today's financial market, to take advantage of the opportunities, and to maximize returns on the investments, a constant acquisition of skills, knowledge and equipments is needed by financial investors. Therefore, the behavioural trend of the investors is constantly moving and changing, from time to time, within various markets. There are many factors that play a major role in influencing the investor's decision, whether to buy, sell, participate, merge, or buy-out. These factors can either be financial, or psychological.

Effective decision-making is a complex process of choosing a particular alternative from a number of alternatives after proper evaluation. In stock market, it requires better insight, and understanding of human nature in a global perspective, apart from sharp financial skills and ability to gain best out of investments (Del, Ferrante and Costantini, 2007). It is believed that decision-making is primarily based on two things: personal factors, and technical factors. Therefore, investors have to rely on these two factors for making decisions in stock market. Positive vision, foresight, perseverance and drive are must for an investor to be successful in his investment decisions. Investors differ in characteristics due to demographic factors such as socio-economic background, educational level, age, gender, etc. and Personal factors such as age, education, profession, income, psychological and emotional traits, etc. So, it is difficult for an investor to make an appropriate investment decision on the basis of the decisions made by someone else. It is very likely that all these emotions interfere in certain proportions in a financial investment decision making. Moreover, their investment decisions are also influenced from complex models of finance. Daniel Kahneman, a psychologist, won the 'Nobel' Prize in Economics for having integrated insights from psychological research into economic science, especially concerning human judgment and decision-making under uncertainty (Shapira and Venezia, 2001). Behavioural Finance is, in general, the application of psychology to the field of finance.

It is observed that various studies have not yet described the factors that put forth a significant influence on financing decisions. This study therefore, will add to the existing literature in these areas by analysing factors influencing financing decisions. This study will seek to answer the following research question: What behavioural factors influence financing decisions?

2. RESEARCH METHODOLOGY

2.1 Research Objective:

1. To identify behavioural factors that has influence on financial decisions.
2. To establish the effect of behavioural factors on financial decisions.

2.2 Research Design:

This research problem was studied through the use of a descriptive research design. According to Cooper and Schindler (2003), a descriptive study is concerned with finding out the what, where and how of a phenomenon. This study therefore was able to generalize the findings to investment banks in Karnal City.

***2.3 Sample Design*:**

The study targeted 50 respondents comprising of five respondents operations manager, business development manager, and three investors from ten investment banks. These offices were chosen upon because of their key role in the purchase and sale of securities. As the target population of the study was small, the study conducted a census where all target respondents were included in the study.

2.4 Research Hypothesis:

The hypothesis that will guide through this research is-

H_0: Behavioural factors have significant relationship with financial decisions.

H_1: Behavioural factors do not have significant relationship with financial decisions.

2.5 Data Collection:

The study employed questionnaire to collect primary data with 100% response rate. The questionnaire comprised of both open and close-ended questions. Questionnaires were administered through drop and pick later method. The pilot testing was also conducted to establish the validity and reliability of the questionnaire.

2.6 Data Analysis:

A. Age brackets of the respondents

Age Brackets (in Years)	Frequency	Percentage
18-35	32	64
36-55	18	36
55 & Above	0	0

Source: Research Findings

B. Level of Education

Education	Frequency	Percentage
Certificate/Diploma	4	8
Graduation	38	76
Post Graduation	8	16

Source: Research Findings

C. Experience of Investors in trading

Experience (in Years)	Frequency	Percentage
0-1	28	56
1-3	8	16
3-5	14	28

Source: Research Findings

D. Amount of investment

Amount of investment (in Lakhs)	Frequency	Percentage
0-1	24	48
1-2	16	32
2 & Above	10	20

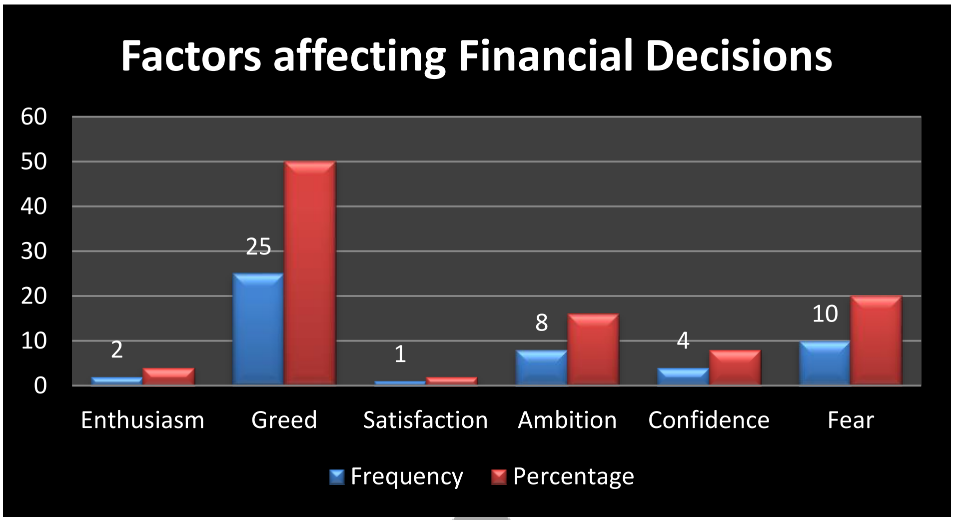
Source: Research Findings

E. Level of Significant Profits

Remarks	Frequency	Percentage
Yes	28	56
No	22	44

Source: Research Findings

F. Behavioural factors that affect Financial Decisions



Source: Research Findings

Correlation Analysis:

Factors affecting	No. of Respondents	
	Actual Value	Perceived Value
Enthusiasm	2	5
Greed	25	10
Satisfaction	1	0
Ambition	8	25
Confidence	4	5
Fear	10	5
	Correlation= 0.291869688	

Testing of Hypothesis: Chi-square Test

Factors affecting	Observed Value (O)	Expected Value (E)	$(O-E)^2$	$(O-E)^2/E$
Enthusiasm	2	5	9	1.8
Greed	25	10	225	22.5
Satisfaction	1	5	4	0.8
Ambition	8	20	144	7.2
Confidence	4	5	1	0.2
Fear	10	5	25	5
			$\chi^2=$	37.5

3. FINDINGS

In the census, 90% of respondents are graduated. 80% of the respondents are having up to one year investment experience have invested up to one lakh rupees in stock trading. From the analysis of the collected data, it is found that 90% of the respondents get influenced by their psychological/emotional factors. A direct, strong and positive relationship is observed between behavioural factors and their financial decisions and hence trading pattern also get affected by their financial decisions. 55% of the respondents consider 'Greed' as the significant factor, while 05% of the respondents consider 'Enthusiasm' as the least affecting factor in their investment decision-making. According to their preference and experience, 60% of the respondents assume 'Ambition for profits' as the significant factor, while 05% of the respondents assume 'Satisfaction (in terms of ROI)' as the least affecting factor in the investment decision-making of investors. To test the hypothesis, chi-square test is used. By the analysis of chi-square test, it is found that null hypothesis is true and should not be rejected. By the use of correlation analysis, it is found that the respondents are having positive relationship among their actual and perceived value in terms of behavioural factors affecting financial decisions.

4. LIMITATIONS

However, some limitations were encountered during the study. The study could not investigate all the factors due to time and resource constraint. The area of study was limited as the respondents were pertained to the Karnal city only. It was assumed that the questionnaires were filled by the right persons since drop and pick later method were used to distribute.

5. EPILOGUE

From the findings, the study concludes that investors in Karnal City who are having experience in trading and invested some amount have gained significant profit in terms of returns on their investments. Most of the respondents invest their funds in stock market due to greed for earning more and more returns on their investments. As per their preference for the factors affecting investment decisions ambition for profit should be the main reason for investments. A significant number of respondents believe in impact of behavioural factors rather than rationality due to preferred models of investment. Hence, financial decisions of the investors are influenced by their behavioral factors.

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