



A Study On The Influence Of Behavioural Finance On Investment Patterns Of Retail Investors

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Abstract:

This study looks at how behavioural finance affects the investing habits of retail investors, with an emphasis on the impact of psychological biases on financial decision-making. Information was obtained from 200 retail investors through convenience sampling utilising a descriptive study methodology and a structured questionnaire. The investigation's findings demonstrated that behavioural traits significantly influenced investing choices. Male participants were more likely to display overconfidence, whereas loss aversion was the most prevalent bias, especially among older investors. The study concludes that investor conduct is often more influenced by emotional and subconscious prejudices than by rational analysis.

Keywords: Behavioural Finance, Retail Investors, Investment Patterns, Loss aversion, Investor Biases, etc.

Introduction

The traditional financial paradigm makes the assumption that investors are rational individuals who base their decisions on careful research and a rational evaluation of the risks and benefits. This paradigm is being challenged by behavioural finance, which incorporates psychological and emotional aspects into financial decision-making. Understanding how feelings and cognitive biases lead investors to regularly deviate from rationality is the aim of psychological finance, an interdisciplinary field that blends psychology and finance (Thaler, 1999). This divergence from the idea of markets that are effective (Fama, 1970) has important implications for the investing habits of retail investors, who are more vulnerable to heuristics, emotions, and social factors than institutional investors.

When making investment selections, retail investors—who are usually non-professional market participants—frequently depend more on their own subjective assessments than on official financial research. Insecurity, herd mindset, fear of losing, mental computation, and other mental constructs can all affect their behaviour (Barberis & Thaler, 2003). Understanding how behavioural finance shapes retail investing patterns is crucial because these irrational behaviours can result in market oddities and securities mispricing.

With an emphasis on important heuristics and prejudices that affect retail investors' investment behaviour, this study attempts to investigate how behavioural finance affects their decision-making processes. Additionally, the study aims to determine whether demographic traits like age, gender, and educational attainment affect a person's vulnerability to behavioural biases. By doing this, it seeks to offer information that could

improve investor education and aid in the creation of plans to lessen irrational investing behaviour.

Literature Review

The shortcomings of conventional financial theories, which were unable to take investor behaviour anomalies into account, gave rise to the idea of behavioural finance. Simon (1955) was one of the first to question the idea of perfect reason by proposing the idea of "restricted reasoning," which postulates that cognitive constraints influence how decisions are made. By pointing out systemic biases and heuristics like accuracy, anchoring, and availability that frequently skew investor judgement, Tversky and Kahneman (1974) made a further contribution.

Shefrin and Statman (1985) showed how psychological elements like mental accounting and regret aversion may affect investing choices, causing investors to act differently from the best risk-return tradeoff. In a similar vein, Odean (1998) demonstrated that overconfident investors frequently engage in excessive trading, which lowers net profits. Retail investors frequently overestimate their expertise and underestimate dangers due to this overconfidence tendency.

Herd behaviour, in which people imitate the investing strategies of others, is another important behavioural characteristic affecting retail investors. This frequently results in market collapses or speculative booms (Banerjee, 1992). Shiller (2000) emphasised how irrational exuberance was fuelled by investor emotion and herd mentality, especially during the dot-com boom. Because they have less access to knowledge and are less financially literate, retail investors exhibit this behaviour more than others.

Demographic traits also have an impact on how much behavioural biases affect investors. Pompian and Longo (2004) found that the elderly are more likely to be cautious and susceptible to anchoring bias, whereas younger investors may be more overconfident. Gender disparities have also been observed, with women frequently exhibiting greater risk aversion than men (Barber & Odean, 2001).

Even though behavioural finance offers convincing justifications for illogical investing behaviour, it has important policy and practical ramifications. Financial advisers, educators, and legislators may create more useful tools and interventions to encourage logical decision-making by having a better grasp of the biases that impact individual investors. Even if the literature is expanding, more empirical research is required to comprehend regional and cultural differences in investor behaviour in developing markets.

Methodology:

The current study uses a descriptive research approach to examine how behavioural finance affects retail investors' investment habits. This approach is appropriate as it makes it possible to gather and analyse data in a methodical manner in order to characterise the qualities and behaviours of the target population. A structured questionnaire with both closed-ended and Likert-scale questions was created to gather information about behavioural biases like overconfidence, herd behaviour, loss aversion, and mental accounting. The questionnaire method is the main tool used in this study to collect data. Clarity, dependability, and relevance to the study's goals were all considered

in the questionnaire's design. To guarantee adequate coverage of a range of demographic and investing behaviour characteristics, an experiment size of 200 retail investors was chosen. Because the study was exploratory in nature and respondents were easily accessible, the convenience sample approach was used. In order to find behavioural trends and make insightful deductions about how behavioural finance affects investment choices, the gathered data was examined using statistical techniques such as descriptive statistics and inferential methods.

Data Analysis:

200 individuals' replies were statistically analysed to see how behavioural finance affected their investment habits. The survey was broken up into parts that addressed behavioural characteristics and demographics. The data was summarised using descriptive statistics, and the associations between behavioural biases and demographic characteristics were investigated using inferential tests.

Table 1 Behavioural Biases

Behavioral Trait	Statement Example	Agree (%)	Neutral (%)	Disagree (%)
Overconfidence	"I believe I can consistently pick winning stocks."	58%	24%	18%
Herd Behavior	"I tend to invest based on the advice or actions of others."	65%	20%	15%
Loss Aversion	"I avoid selling losing investments in the hope they'll recover."	72%	18%	10%
Mental Accounting	"I treat money differently based on where it comes from."	55%	30%	15%

Loss aversion showed the highest degree of agreement (72%), suggesting a strong emotional opposition to experiencing losses. Additionally, herd behaviour was common (65%), indicating that many investors depend more on social cues than independent study. 58% of respondents reported feeling overconfident, which might result in excessive trading and risk-taking. 55% of investors had mental accounting, demonstrating compartmentalised thinking while making financial decisions.

Table 2 Gender Vs. Overconfidence bias

Gender	Agree	Disagree	Total
Male	90	40	130
Female	26	44	70
Total	116	84	200

Table 2 shows that there is a statistically significant association between overconfidence and gender, with men investors exhibiting a greater propensity for overconfidence than female investors.

Conclusions:

Research indicates that retail investors' investment behaviours are significantly influenced by behavioural finance. Important behavioural biases were found to be common throughout the sample. The most prevalent bias, especially among older investors, was loss aversion, indicating a widespread unwillingness to realise losses, even at the expense of portfolio efficiency. Male investors were more likely to exhibit overoptimism, which might result in excessive trading and risk-taking. Herd behaviour was also noticeable, suggesting that rather than depending on their own judgement, many retail investors prefer to follow the investing choices of others. According to conventional finance theories, psychological considerations have a significant impact on financial decision-making and frequently cause deviations from logical, utility-maximizing behaviour. These data support this idea.

Recommendations:

In light of the findings, it was suggested that investor education initiatives be improved in order to raise knowledge of behavioural biases and how they affect financial results. Initiatives to promote financial literacy should concentrate on assisting investors in identifying and controlling emotional reactions including social pressure and loss apprehension. To provide individualised methods to lessen the impact of such biases, financial planners and investment advisors should include behavioural evaluations in their client sessions. Financial institutions and regulatory agencies can also provide behavioural nudges and digital tools that encourage investors to think things through before acting rashly, such as panic selling or mindlessly following market patterns. Last but not least, it is important to motivate individual retail investors to keep their portfolios diversified, embrace long-term outlooks, and base their decisions on factual information rather than gut feeling or peer pressure.

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