

IMPACT OF BEHAVIORAL FACTORS ON INVESTORS' INVESTMENT DECISIONS OF COLOMBO STOCK EXCHANGE

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INTRODUCTION

Capital markets are an essential part of the financial sector of modern economies and even more in emerging economies. Well-developed capital markets promote economic growth through increased savings and mobilization, access to external savings, the spread of financial risk, and the facilitating role in converting savings into investments. The people of the society act as two groups called investors and savers. They tend to spend their savings in various investing ways depending on their level of financial literacy and risk-taking ability. Among an investment portfolio, risk-taking investors like to invest their money in the stock market rather than invest in savings accounts like risk-averse individuals (Rathnayake et al., 2014). When it comes to investors, there are two types of investors: institutional and retail investors. Retail investors, also known as individual investors, are the leading role players in the stock market. Examining their behavior in the stock market is essential for academic and professional purposes (Akbar et al., 2016). Accordingly, individual investors' decision on the stock market plays a vital role in determining the market trend, which then affects the economy (Rathnayake et al., 2014). To understand and provide an appropriate explanation for the investors' decisions, it is imperative to explore which behavioral factors influence investors' decisions in the stock market. Individual investors make their financial decisions according to their perspectives. As a result, behavioral finance is considered worldwide (Akbar et al., 2016). Market anomalies and irrational behavior cause investors' changes in the stock market, which has led to an investigation into the impact of various behavioral biases and factors affecting decision-making for individual investors. Although, a thorough analysis of individual investor behavior helps to mitigate the risk associated with the investment decision and, in turn, investment in the stock markets.

Numerous financial theories assume people make rational decisions and use all available information when investing. However, when conventional financial theory fails to provide adequate explanations for investor behavior, behavioral finance has been developed to help. Determining which behavioral factors are more critical when making an investment decision has not been entirely resolved by studies in this modern field. On the other hand, different researchers have yielded inconclusive findings, creating a vacuum for further studies. Therefore, researchers expected that this study would enrich awareness in this domain. Consequently, the main objective of this study was to explore the impact of behavioral factors on investors' decisions at the Colombo Stock Exchange (CSE). The representativeness, overconfidence, and anchoring were identified as the proxies of the independent variable, whereas investment decisions were identified as the dependent variables of the present study. This study will contribute significantly to developing this field in the Sri Lankan context.

However, the study begins with the existing theories in behavioral factors, based on which hypotheses were proposed.

METHODOLOGY

The conceptual framework presented in Figure 01 indicates the relationship between the dependent and independent variables proposed in the present study.

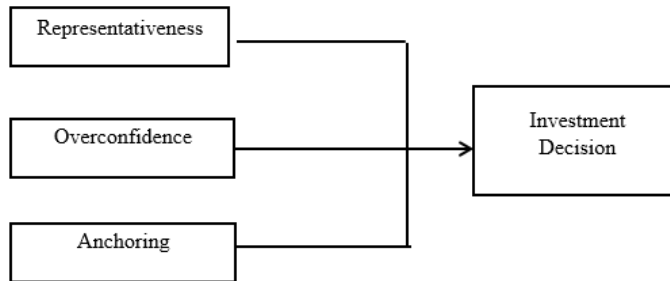


Figure 1 Conceptual Framework of the Study

Accordingly, three behavioral factors, representativeness, overconfidence, and anchoring, have been selected as the independent variables where investment decision was the study's dependent variable. The current study was a deductive and quantitative type study. The population of this study was the registered individual investors in CSE in Sri Lanka. However, with the time limitation, the study's sample size ended with 160 individual investors in the CSE. The researchers used the convenience sampling technique to select the sample for this study. Accordingly, the study's unit of analysis was an individual investor in the CSE in Sri Lanka. The following three hypotheses were developed based on the existing literature and tested during the present study, aligning with the study's objective.

H₁: There is an impact of representativeness bias on investment decisions making of individual investors in CSE.

H₂: There is an impact of overconfidence bias on investment decisions making of individual investors in CSE.

H₃: There is an impact of anchoring bias on the investment decisions making of individual investors in CSE.

This research study mainly depended upon the primary data collection method, which was collected using a survey questionnaire. The primary data collection procedure was a structured questionnaire based on a five-point Likert scale. The gathered data were analyzed using descriptive statistics, correlation analysis, and multiple regression analysis. Apart from these primary analyses, data screening and cleaning were carried out using normality tests and reliability (Cronbach's Alpha) tests.

RESULTS AND DISCUSSION

The Cronbach's Alpha values of the reliability test were more significant than the standard value (the most negligible value was 0.748, and the highest value was 0.810), confirming the

continuation suitability for the primary analyses. The findings of the main analyses were tabulated in following tables.

Table 1 Result of Descriptive Statistics

	Mean	Std. Deviation	Skewness	Kurtosis
Overconfidence	4.002	0.650	-0.765	0.476
Representativeness	4.141	0.634	-0.795	0.980
Anchoring	4.138	0.574	-1.006	2.684
Investment Decisions	4.161	0.556	-0.580	0.141

Table 1 indicates that the average overconfidence is 4.002, with the standard deviation of 0.650 and high relative importance. The other two independent variables, representativeness, and anchoring, also have high relevance importance with mean values of 4.141 and 4.138 with standard deviations of 0.634 and 0.574, respectively. The mean value of investment decision is 4.161, whereas the standard deviation of it is 0.566.

Table 2 Result of Correlation Analysis

Variables	Overconfidence	Representativeness	Anchoring	Investment Decisions
Overconfidence	1.000			
Representativeness	0.593**	1.000		
Anchoring	0.691**	0.670**	1.000	
Investment Decisions	0.633**	0.584**	0.704**	1.000

Note: N = 160, **, Significant at the 0.01 level (two-tailed).

As per Table 2, the correlation coefficients of each variable are significant at the 0.01 level. The coefficient value of 0.633 for overconfidence and investment decisions is positive and significant, while the other two variables' associations are also positive and significant at a 0.01 level.

Table 3 indicates the result of the regression analysis. According to the table, it is revealed that all the independent variables indicate a statistically significant and positive impact on the investment decisions of the sample companies. The present findings are more consistent with the previous findings in the field.

Table 3 Results of Regression Analysis

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
Constant	1.035	0.231		4.482	0.000
Overconfidence	0.210	0.066	0.245	3.197	0.002
Representativeness	0.127	0.066	0.145	1.942	0.004
Anchoring	0.424	0.081	0.438	5.261	0.000

R	0.741
R ²	0.548
Adjusted R ²	0.540
F	63.149
Sig.	0.000

The study of Bakar and Amelia (2016) examined the impact of psychological factors, namely overconfidence, conservatism bias, herding effect, availability bias, and investment decision-making in the Malaysian Stock Market and reported that overconfidence has a significant positive effect on investment decision-making in the Malaysian Stock Market. The present study results also show that overconfidence positively impacts investment decision-making in the CSE. Thus, this study's first hypothesis (H₁) was supported.

The second hypothesis (H₂) formulated in the present study was also supported by reporting a positive and significant influence of representativeness on investment decisions. The study's finding goes hand in hand with the result of Kartini and Nahda (2021). The result confirms that investors tend to make decisions based on limited information from their surroundings and ignore other information or significant events that may happen in the future. A study by Luong and Ha (2011) found a positive and significant impact of Anchoring on investment decisions, which is consistent with the present finding. Accordingly, the third hypothesis (H₃) developed in the study was also supported. At this juncture, it can be concluded that the behavioral factors of individuals impact their investments' decision makings positively.

CONCLUTIONS AND IMPLICATIONS

According to recent studies on individual investors, people seem to react to and perceive the same information differently, which results in psychological biases known as behavioral finance. While behavioral finance maintains that investors cannot access all types of information but behave irrationally, suggesting that some cognitive prejudices may influence their investment decision, traditional financial theories assume that investors are rational and possess all types of information when making an investment decision. Consequently, the study aimed to determine how these behavioral characteristics affect investors' investment choices. This study used three behavioral factors: representativeness, overconfidence, and anchoring. The findings reveal that behavioral factors positively influence an investment decision.

In uncertainty, overconfidence can be helpful for investors to do complex tasks and help them forecast and forecast future trends. The findings further showed that representativeness has an impact on investment decisions. Therefore, individual investors at the CSE should increase representativeness, the quality of investment decisions, and perceived market efficiency decrease. The results indicated that behavioral anchoring factors also have a significant and positive effect on the stock decision of individual investors in the CSE. In conclusion, investors follow a rational decision-making process, while psychological factors are also involved in their investment behavior. Individual investors in the market should take educational courses on behavioral biases that affect investment decision-making in order to be able to manage their portfolios. Professionals in consulting and investment management should be exposed to behavioral factors through workshops and seminars so that when decisions have been taken, behavioral finance tendencies will reduce. Fund managers and

investors should apply collective views on investment as this tends to reduce individual personal biases on an investment. The formation of committees could be employed, though the use of committees has implications. In this sense, practitioners studying behavioral factors should learn to recognize their own mistakes and those of others, understand those mistakes, and take steps to avoid them. The research will also add to the knowledge body by enhancing the existing financial literature. Researchers and future academics may utilize the research as a learning tool to deepen their understanding of behavioral finance.

Keywords: Behavioral factors, investment decisions, individual investors

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