IMPACT OF HUMAN BEHAVIOR ON INVESTMENTS

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ABSTRACT:

This term is which emerged some years ago, studies the various psychological factors that can affect financial markets it shows that individuals may not necessarily make decisions on the basis of a rational analysis of all the information based on data derived from some information such as probabilities, statistics and other predictions that are based on numbers. As all this data is useful for investors to make logical decisions, it is very common in making errors based on emotion.

Some biases, acts as a driving force behind behavioral finance
1) Market Paradox.
2) Herding mentality which leads to act as a bubble of a stock market
3) Noise traders & Loss aversion
4) Momentum effect
5) Overconfidence
6) Anchoring,
7) Confirmation bias
8) Emotional gap
9) Mental accounting
10) Self-attribution bias
11) Confirmation bias
12) Representative bias
13) Framing bias
14) Believing

Behavioral finance tries to minimize the miscalculations and misguidance by measuring them, moves that people commit by using their money. The idea behind behavioral finance "is not that people are not rational, where as they they are predicting with their investments irrationally.

(Keywords- behavioral finance, Investments, biases)

INTRODUCTION:

We are all subject to emotions, of whatever type they are either they are positive or negative, which are formed as result of a gathering of factors, such as our beliefs, our experience, our view to the outside world, or our personality.

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based on data derived from some information such as probabilities, statistics and other predictions that are based on numbers. As all this data is useful for investors to make logical decisions, it is very common in making errors based on emotion.

Our current financial and economic theory is based on assumptions that act of an individual is rational as an investor considers to collect all available information in the decision-making process .Various challenges Behavioral finance face are assumptions :

- Finance theory studies the psychological, emotional factors influencing in the process of our decision-making.

-Traditional finance theory is based on the concept that investors are rational. They are not clouded by cognitive errors and use the relevant data to make informed decisions there are several studies done on how the financial market is affected by the emotions and subconscious of its investors.

This study had been an innovative for its time, however, went against the historically established assumption of "efficient financial markets", which held that they were subject only to rationality and approach of behavioral finance it is much opposite as it suggests that, as humans, we all have inherent flaws. We don't always act rationally, and we have to limit
/restrain to our self-control. Instead, emotions, cognitive errors and biases can often influence our choices. The relaxing aspect of these assumptions has implications at both levels either it is at the individual level or at market levels.

It is matter of importance of annotation that, at an individual level, all the market participants, irrespective of their knowledgeable whether it is more or less either they are individual investors or money managers with experience, they may act irrationally or rationally; i.e. All the market participants deviate due to the behavior of investors or in traditional theory of financial matter it is assumed. Some of the deviations are categorized and identified as behavioral biases of investors. Further adding to it , biases of individual behavioral may be improved in a group setting, which further complicates investment processes rationally . One of the concepts that underpin the field of study is the influence of biases their impact on our choices.

Source: Arthur D. Little
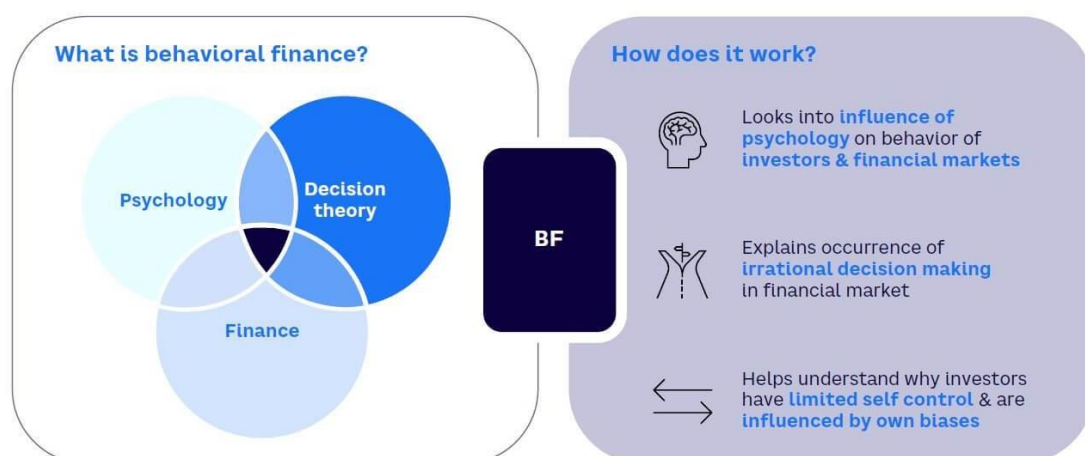
On the contrary , behavioral finance is used to explore individual investor's personality trait, and cognitive biases , managers are more concerned with creating relationship with their investors and are required to cater customers' needs and sometimes with specific requirements more precisely. This will be enabling financial services providers to (re)shape their service model, to make it ever more relevant to their customers by process differentiation.

Are we our own greatest enemy?

Are we our own greatest enemy? Before diving into the topic of behavioral finance, we first need to look at the real costs of our choices. Historically, stock markets around the world have trended up, as shown in the charts below.
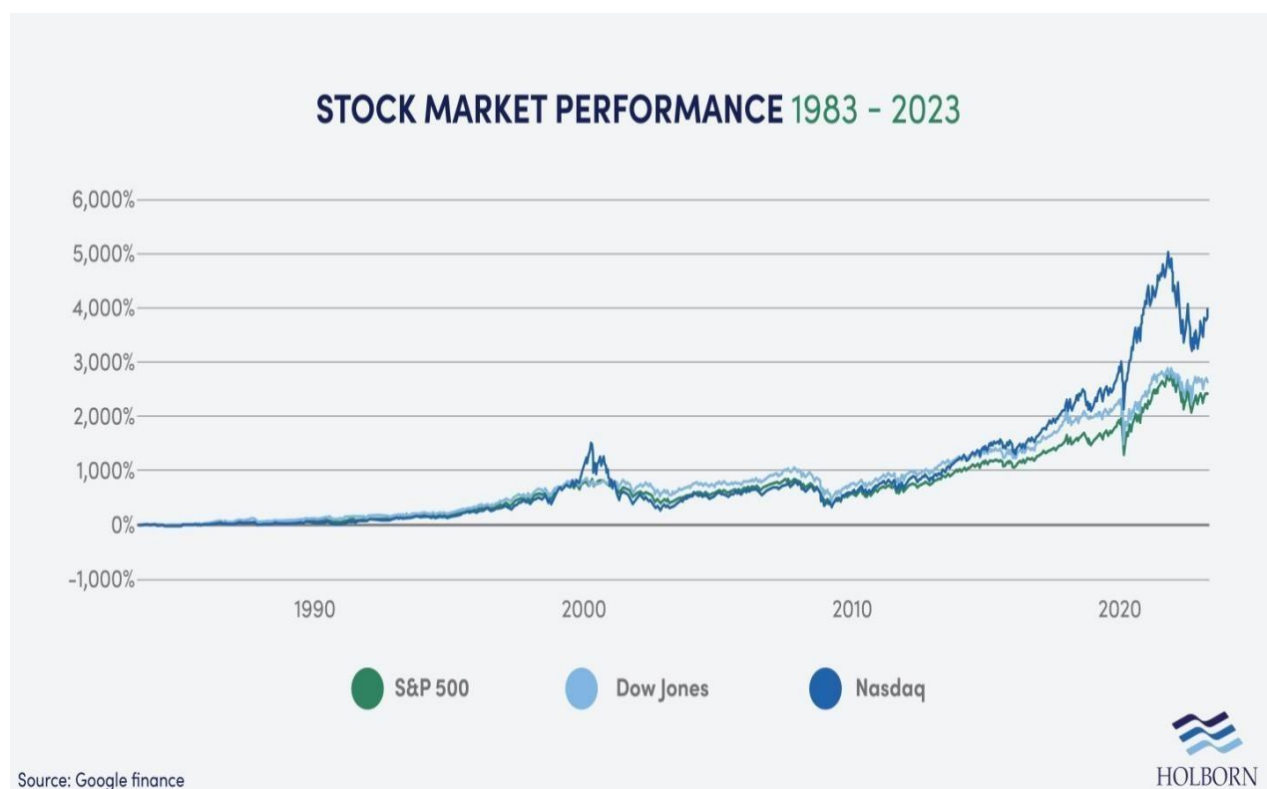
If investor's invests in a diverse portfolio and leave it alone, investors will earn a lot of money. But this isn't always the case. As, there have been dips there are other factors to consider.
Are we our own greatest enemy when it comes to being successful in the markets? The biggest

Question that arises

One thing that we must need to understand that investor's emotions can influence their financial decisions, it is easier to step back and take an objective view. By identifying the most common behavioral biases, investor can optimize investments and not to yield as per emotional pressures that may harm judgments.

Some concepts, preconceptions / biases, acting as a driving force behind behavioral finance. There are multiple reasons to perform an investor perception study

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These biases and the heuristics that helped to create them affect investor 's behavior, market and trading psychology, cognitive errors, and emotional reasoning etc.

CONCLUSION & RECOMMENDATION:

Recommendations Classifying investors into various types which are based on their characters, which include level of tolerance of risk, approach to investing which is preferred, and behavioral characteristics , is useful in providing insight of financial decision making but they should be used with some cautiousness.

The relationship between Adviser and client which is required for decisions of finance in order to be more satisfying and effective if investors take behavioral factors into consideration. Including the biases of human behavior in construction of portfolio may result in closer and efficient portfolio as in accordance to traditional finance, which is easier for the client's understanding and accepting as a suitable proposal. By considering biases of human behavior, makes it possible to make the effect moderate.

- Before purchasing or planning to purchase a stock or any mutual fund, decide up to what it would be going to any direction either downward or upward before an investor would sell it. Creating a long-term financial plan will also help in keeping distracting due to emotions.

- Since losses hurt investors more than gains received by them or makes them feel better, and to accentuate all the negative while thinking about saving and, investing.
  Investors well know quote: - "I'm saving to create a nest egg for the future."

- Keep a proper track of decisions which are made for money and then re-evaluate them in a pre-decided time or in an year as it prevent overconfidence for making future investing decisions.

- One should be trying to get out of bubble in-spite of thinking of how much and more certain an investor be , instead of just following the heard and following/dissenting strategies and views Don't blindly follow investing trends.

INTERPRETATION

It is really important to know that they financial advisors, investors, or market participants, irrespective of their expertise, exhibit /showcase different behavior from that assumed in traditional finance. Behavioral finance is implemented for the financial advisory It can be tough to undertake a study, as an investor may hear views that challenge his decision, and it could present issues that you have not been considered yet. But that helps to gain at that edge of competition by overcoming challenges, and which can't do that until one understand what ever these challenges are. The main cognitive psychology, and the limits to arbitrage, constituents are the ones who can interpret diversification in the market scenarios whereas they are highly influenced by the human psychology in financial decisions occurs. Hence, understanding cognitive bias is like understanding overconfidence, herd mentality, and loss aversion l. Furthermore, the forces of arbitrage may fail, and this limit to the arbitrage process contributes to the persistence of financial market anomalies. In totality we can conclude that the study tries to explain about the investor's irrational decisions and which tries to unveil market behavior.

The concept of the problem is that the behaviors of investor's when it is combined with their different biases already discussed above make them difficult to predict the market and outcomes. The basic concept behind behavioral finance "is not that people are NOT rational, where as they are predict with their investments irrationally out of their biasness, In short we can say that Stock <u>Turnover are affected.</u>

It is important to remember that all investors, financial advisors or all market participants, regardless of expertise, may exhibit behavior that differs from that assumed in traditional finance. The main essential component ,of behavioral finance are cognitive psychology which limits to arbitrage, which can be interpreted in diversified market situations where ever the stimulus of human mindset in financial decisions are occurring. Hence, understanding cognitive bias like herd mentality, overconfidence, and aversion loss is beneficial. Furthermore, the forces of arbitrage may fail, and this limit to the arbitrage process contributes to the persistence of financial market anomalies. In summarize that the behavioral finance is the study which tries to explains the investor's non rational decisions and tries to disclose their market behavior, the basic problem behind the investors behaviors is due to combining their different biases/mind sets which makes them difficult to predict.

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