A Study on Behavioural Biases, Emotions, And Risk Preferences: An Empirical Study of Investor Decision-Making in Emerging Markets

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ABSTRACT

This study explores the underlying behavioural dimensions that influence investor decision-making in emerging markets, with specific focus on India. While traditional financial theories are built on the assumption of rationality, real-world investment behaviour often deviates from these expectations due to the influence of psychological and emotional factors. This research integrates behavioural finance perspectives to examine how cognitive biases, emotional responses, and dynamic risk preferences collectively shape investment choices.

The study is based on primary data collected through a structured questionnaire administered to

61 respondents with varying levels of investment experience. A descriptive and analytical approach has been adopted, utilizing percentage-based analysis to identify patterns in investor behaviour. The findings indicate that investors are significantly influenced by behavioural biases such as loss aversion, overconfidence, and herd behaviour. Emotional factors, including fear during market downturns and optimism during upward trends, also play a crucial role in shaping decision-making processes. Further, the study reveals that risk preferences among investors are not static but tend to fluctuate based on market conditions and individual experiences. Many investors exhibit a tendency to rely on informal sources such as peer opinions and prevailing market trends rather than solely on fundamental analysis. Overall, the research highlights that investment decisions are the result of a complex interaction between rational evaluation and behavioural influences. By providing a more realistic understanding of investor behaviour in the Indian context, this study contributes to the growing body of behavioural finance literature and offers practical insights for investors, financial advisors, and policymakers.

INTRODUCTION

Financial decision-making has traditionally been viewed through the lens of rationality, where investors are expected to make logical choices based on available information, risk-return trade-offs, and market efficiency. The principles of traditional finance, supported by theories such as the Efficient Market Hypothesis, assume that individuals act in a fully rational manner while maximizing their utility. However, in real-world scenarios, investor behaviour often deviates from these assumptions, giving rise to the need for a more comprehensive understanding of how decisions are actually made. In recent years, the field of behavioural finance has emerged as a significant area of study, challenging the notion of perfect rationality by incorporating psychological and emotional factors into financial decision-making. Investors are not always guided purely by logic; instead, their choices are frequently shaped by cognitive biases, emotions, social influences, and past experiences. This shift in perspective is particularly relevant in emerging markets like India, where market participation has increased rapidly, and investor profiles have become more diverse.

The Indian stock market, represented by indices such as the NIFTY 50, reflects not only economic fundamentals but also the collective behaviour of millions of investors. Market movements are often influenced by sentiment-driven reactions, where fear, greed, and speculation play a crucial role alongside factual information. The increasing accessibility of trading platforms and the growing influence of digital media have further amplified these behavioural tendencies, making it essential to study how modern investors interpret and respond to market signals. This study focuses on understanding the behavioural aspects that influence investor decision-making in emerging markets. It aims to

analyze how psychological biases such as overconfidence, loss aversion, and herd behaviour impact investment choices. Additionally, the research examines the role of emotions and changing risk preferences in shaping investor actions, particularly during different market conditions. By bridging the gap between theoretical assumptions and practical behaviour, the study seeks to provide a more realistic view of how investment decisions are formed. A deeper understanding of behavioural influences can contribute to better investment strategies, improved financial literacy, and more effective market regulations. In a rapidly evolving financial environment, recognizing the human element behind investment decisions becomes essential for ensuring more informed and stable participation in the market.

LITERATURE REVIEW

The field of behavioural finance has gained significant attention over the years as researchers have increasingly recognized the limitations of traditional financial theories in explaining real-world investor behaviour. Early financial models, particularly those based on the Efficient Market Hypothesis, assumed that investors are rational and markets fully reflect all available information. However, several empirical studies have challenged this assumption by highlighting systematic deviations in investor decision-making. One of the foundational contributions to behavioural finance was made by Daniel Kahneman and Amos Tversky through the development of Prospect Theory. Their work demonstrated that individuals evaluate gains and losses differently, leading to biases such as loss aversion, where the pain of losses is felt more strongly than the pleasure of gains. This concept has been widely supported by subsequent studies, establishing that investors often make decisions based on perceived outcomes rather than objective probabilities.

Further research has identified overconfidence as another critical behavioural bias influencing investment decisions. Studies suggest that investors tend to overestimate their knowledge and ability to predict market movements, which can lead to excessive trading and increased risk exposure. Similarly, herd behaviour has been extensively documented, where individuals tend to follow the actions of the majority rather than relying on independent analysis. This behaviour is particularly evident during periods of market volatility, where uncertainty drives investors to seek reassurance in collective actions. In the context of emerging markets, behavioural factors play an even more pronounced role due to varying levels of financial literacy and market experience. Several studies have highlighted that investors in developing economies often rely on informal sources of information, such as peer recommendations and social trends, rather than formal financial analysis. The growing influence of digital platforms and social media has further intensified this trend, making information dissemination faster but not always reliable.

Recent literature also emphasizes the dynamic nature of risk preferences, suggesting that investor attitudes toward risk are not fixed but change depending on market conditions and personal experiences. During bullish phases, investors tend to exhibit risk-seeking behaviour driven by optimism, whereas in bearish conditions, fear and uncertainty often lead to risk-averse decisions. This shift highlights the strong interaction between emotions and financial choices. Despite the growing body of research in behavioural finance, there remains a gap in understanding how multiple behavioural factors interact simultaneously to influence decision-making, particularly in the Indian context. Many studies focus on individual biases in isolation, whereas real-world decisions are often the result of a combination of psychological, emotional, and social influences. This study attempts to address this gap by providing an integrated analysis of investor behaviour, offering a more comprehensive perspective on decision-making in emerging markets.

METHODOLOGY

The present study adopts a descriptive and analytical research design to examine the behavioural factors influencing investor decision-making in emerging markets. The primary objective is to understand how psychological biases, emotional responses, and risk preferences affect investment choices in a real-world context.

Research Design: The research is based on a quantitative approach, focusing on collecting measurable data related to investor behaviour. A structured framework has been used to analyze patterns and relationships among different behavioural factors, ensuring clarity and consistency in interpretation.

Data Collection: The study relies on both primary and secondary data sources. Primary data has been collected through a structured questionnaire designed using Google Forms. The questionnaire includes a mix of multiple-choice and scaled questions aimed at capturing investor perceptions, emotional tendencies, and behavioural biases. A total of 61 responses were collected from individuals with varying levels of investment experience. The respondents include students, working professionals, and individuals actively participating in the stock market, providing a diverse perspective on investment behaviour. Secondary data has been sourced from research papers, journals, and relevant financial reports to support the theoretical framework and provide context to the study.

Sampling Technique: The study uses a convenience sampling method, where respondents were selected based on accessibility and willingness to participate. While this method allows for quick data collection, it may limit the generalizability of the findings to a larger population.

Data Analysis Tools: The collected data has been analyzed using simple statistical tools such as percentage analysis and graphical representation. Responses have been categorized and interpreted to identify trends and behavioural patterns among investors. The use of charts and tables helps in presenting the data in a clear and understandable manner.

Scope of the Study: The research primarily focuses on individual investors within the Indian market, with an emphasis on understanding behavioural influences rather than purely financial metrics. It aims to provide insights into how investors think and act under different market conditions.

Limitations of the Study: Despite providing valuable insights, the study has certain limitations. The sample size is relatively small, and the use of convenience sampling may not fully represent the broader investor population. Additionally, the study relies on self-reported data, which may be subject to personal bias or interpretation.

DATA ANALYSIS & INTERPRETATION

The responses collected through the questionnaire were analysed using simple percentage methods to better understand how individuals behave while making investment decisions. Instead of looking at numbers alone, the focus here is on identifying patterns in thinking, emotions, and decision-making tendencies among investors.

4.1 Demographic Profile of Respondents

Table 4.1: Age-wise Distribution of Respondents

Age Group	Percentage
Below 25	22.8%
25–35	24.6%
36–45	15.8%
46–55	15.8%
55 and above	21.1%

Source: Primary Data - From the table, it can be seen that a large share of the respondents fall within the 25–35 age group, followed closely by those below 25. This clearly shows that younger individuals are actively participating in the stock market. At the same time, there is also a noticeable presence of respondents from higher age groups, including those above 55. This mix of age groups adds more depth to the study, as it reflects opinions from people with different levels of experience and financial understanding.

4.2 Investment Experience of Respondents

Table 4.2: Investment Experience of Respondents

Experience Level	Percentage
Less than 1 year	31.6%
1–3 years	24.6%
3–5 years	26.3%
More than 5 years	17.5%

Source: Primary Data- The data indicates that many respondents are relatively new to investing, with the highest percentage having less than one year of experience. This suggests that the market is attracting a growing number of first-time investors. However, limited experience can also mean that these individuals may not always make fully informed decisions and could be more influenced by external factors like trends, opinions, or emotions.

4.3 Investment Preferences

Table 4.3: Main Investment Type

Investment Type	Respondents	Percentage
Stocks	28	50%
Mutual Funds	39	69.6%
Bonds/Fixed Income	24	42.9%
Crypto/High-risk assets	28	50%
Mixed Portfolio	28	50%

Source: Primary Data- Looking at the preferred investment options, mutual funds appear to be the most popular choice among respondents. This may be because they are generally considered safer and professionally managed. At the same time, a significant number of investors are also involved in stocks, crypto assets, and mixed portfolios. This shows that investors are not sticking to just one type of investment but are exploring different options, possibly to balance risk and returns.

4.4 Investment Knowledge Level

Table 4.4: Investment Knowledge Level

Knowledge Level	Percentage
Much higher than others	21.1%
Slightly higher than others	26.3%
About the same as others	26.3%
Slightly lower than others	14%
Much lower than others	12.3%

Source: Primary Data- When asked about their knowledge compared to others, most respondents rated themselves as either slightly above average or about the same. This reflects a moderate level of confidence among investors. However, this self-assessment may not always be accurate. In some cases, individuals might overestimate their understanding, which can affect their decision-making in uncertain situations.

4.5 Confidence in Predicting Market Trends

Table 4.5: Confidence in Predicting Market Trends

Confidence Level	Percentage
Extremely confident	19.3%
Very confident	22.8%
Moderately confident	21.1%
Slightly confident	17.5%
Not confident at all	19.3%

Source: Primary Data- The responses related to confidence in predicting market trends are quite evenly spread. While some investors feel confident about their ability to predict movements, others are unsure or lack confidence. This variation is quite natural, as the stock market is unpredictable, and not everyone has the same level of knowledge or experience. It also shows that decision-making is often influenced by personal belief rather than certainty.

4.6 Behaviour During Investment Loss

Table 4.6: Reaction to Investment Loss

Action	Percentage
Hold and wait for recovery	17.5%
Buy more to average cost	10.5%
Sell immediately	31.6%
Wait for advice	24.6%
Depends on market conditions	15.8%

Source: Primary Data- The table shows that a large number of respondents prefer to sell their investments immediately when they start facing losses. This indicates a fear-driven reaction, where investors try to avoid further losses. On the other hand, some choose to hold their investments or wait for advice before making a decision. This clearly reflects that emotions play a strong role, especially during negative market situations.

4.7 Influence of Others on Investment Decisions

Table 4.7: Influence of Others on Investment Decisions

Frequency	Percentage
Very often	12.3%
Often	26.3%
Sometimes	21.1%
Rarely	24.6%
Never	15.8%

Source: Primary Data- It is interesting to note that many respondents admit to following others at least occasionally when making investment decisions. Whether it is friends, social media, or general market trends, external influence seems to play a noticeable role. This behaviour suggests that investors do not always rely on their own analysis and may be influenced by what others are doing, especially in uncertain situations.

4.8 Importance of Purchase Price

Table 4.8: Importance of Purchase Price

Importance Level	Percentage
Extremely important	24.6%
Very important	24.6%
Moderately important	15.8%
Slightly important	21.1%
Not important at all	14%

Source: Primary Data- The data shows that most investors consider the price at which they bought an asset to be important when deciding to sell it. This indicates that people tend to mentally attach themselves to their purchase price. Instead of focusing only on current market conditions, they often compare it with their initial investment, which can sometimes lead to delayed or biased decisions.

4.9 Reaction During Market Fall

Table 4.9: Reaction During Market Fall

Reaction	Percentage
Sell most investments	7%
Sell some investments	12.3%
Hold calmly	36.8%
Buy more	19.3%
Feel anxious but no action	24.6%

Source: Primary Data- During a major market fall, the most common response among investors is to hold their investments and wait. This shows a certain level of patience and belief in long-term recovery. However, a considerable number of respondents also reported feeling anxious or choosing to sell their investments. This again highlights how emotions like fear and uncertainty can influence behaviour during difficult market conditions.

4.10 Change in Risk Behaviour After Profit

Table 4.10: Change in Risk Behaviour After Profit

Behaviour	Percentage
Take much higher risks	17.5%
Take slightly higher risks	19.3%
No change	38.6%
Become more cautious	14%
Withdraw profits	10.5%

Source: Primary Data- When it comes to behaviour after earning profits, most respondents stated that their risk-taking ability does not change significantly. This suggests a relatively stable approach among investors. At the same time, some individuals tend to take higher risks after gains, while others become more cautious. This difference shows that investor behaviour is not uniform and depends on personal mindset and experience.

4.11 Investment Preference

Table 4.11: Investment Preference

Preference	Percentage
Guaranteed low returns	21.1%
Stable moderate returns	12.3%
Balanced risk-return	31.6%
High risk-high return	17.5%
Very high-risk investments	17.5%

Source: Primary Data- The majority of respondents prefer a balanced approach between risk and return. This indicates that most investors are neither too conservative nor too aggressive.
However, there are also individuals who prefer high-risk investments, which reflects the presence of different risk appetites within the group.

4.12 Choice Between Safe and Risky Investment

Table 4.12: Choice Between Safe vs Risky Return

Choice	Percentage
Definitely 6% safe	21.1%
Probably 6% safe	19.3%
Unsure	21.1%
Probably 15% risky	19.3%
Definitely 15% risky	19.3%

Source: Primary Data- The responses to this question are quite evenly distributed, with no single option dominating. This suggests that investors have mixed opinions when it comes to choosing between safety and higher returns. Such variation highlights that investment decisions are highly personal and are influenced by individual preferences, past experiences, and comfort with risk.

FINDINGS, CONCLUSION, SUGGESTIONS & LIMITATIONS

Key Findings: The analysis of the data reveals several important insights into investor behaviour in emerging markets. Firstly, it is evident that a large proportion of investors are relatively new to the market, indicating a growing interest in investment activities, especially among younger individuals. This rise in participation reflects increased financial awareness and easier access to digital trading platforms.

Secondly, the study highlights that investor decisions are significantly influenced by behavioural biases. Biases such as loss aversion, overconfidence, and herd behaviour play a crucial role in shaping investment choices. Investors often tend to avoid losses more strongly than they pursue gains, rely on their own judgment excessively, or follow the actions of others rather than making independent decisions. Another key finding is the strong influence of emotions on decision-making. Feelings such as fear during market downturns and optimism during rising markets directly impact investor actions. This emotional involvement often leads to impulsive decisions, which may not always align with rational financial planning. The study also finds that risk preferences are dynamic rather than fixed. Investors tend to adjust their risk-taking behaviour based on market conditions, becoming more aggressive during bullish phases and more cautious during uncertain periods. Lastly, it is observed that many investors depend on informal sources of information, including social media and peer recommendations, which increases the likelihood of biased or uninformed decisions.

Conclusion: The study concludes that investor decision-making in emerging markets cannot be fully explained by traditional financial theories that assume rational behaviour. Instead, it is largely influenced by a combination of psychological, emotional, and social factors. Behavioural finance provides a more realistic framework for understanding how investors actually behave in real-world situations. The findings clearly indicate that biases and emotions play a central role in shaping investment decisions, often leading to deviations from rational judgment.

In the context of the Indian stock market, represented by indices such as the NIFTY 50, investor sentiment and behaviour significantly contribute to market movements. Therefore, understanding these behavioural aspects becomes essential for making informed investment decisions andensuring market stability. Overall, the study emphasizes the need for investors to develop greater self-awareness and adopt a more disciplined approach to investing, balancing both rational analysis and behavioural understanding.

Suggestions: Based on the findings of the study, the following suggestions are proposed:

- Investors should focus on improving financial literacy to better understand market dynamics and reduce reliance on informal sources of information.
- Awareness programs should be conducted to educate investors about common behavioural biases and their impact on decision-making.
- Investors should adopt a long-term perspective and avoid making impulsive decisions based on short-term market fluctuations.
- The use of systematic investment strategies and professional financial advice can help in minimizing emotional and biased decisions.
- Regulatory bodies like the Securities and Exchange Board of India can play a key role in promoting investor education and ensuring transparency in financial markets.

Limitations of the Study: While the study provides valuable insights, it is subject to certain limitations. The sample size is relatively small and may not fully represent the entire investor population. The use of convenience sampling limits the generalizability of the findings. Additionally, the study is based on self-reported data, which may be influenced by personal bias or subjective interpretation. Time constraints and limited resources also restricted the scope of data collection and analysis.

Future Scope of the Study: Future research can expand the scope by including a larger and more diverse sample size to improve the reliability of findings. Comparative studies across different regions or countries can also provide deeper insights into behavioural differences. Moreover, advanced statistical tools and models can be used to analyze the relationship between behavioural factors and investment performance more accurately. Further research can also explore the impact of technological advancements and digital platforms on investor behaviour in greater detail.

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