Journal of Economics, Assets, and Evaluation, Volume 1, Number 4, 2024, *Page*: *1-13*

Unraveling Investor Behavior: Exploring the Influence of Behavioral Finance on Investment Decision-Making

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Received: 03 Mar 2024
Accepted: 27 May 2024
Published: 30 May 2024

Abstract: The primary objective of this study is to gain a comprehensive understanding of how behavioral biases and psychological factors impact investment choices in a real-world context, with a specific focus on Baroda City. By analyzing awareness, innovation, purchasing power, online purchasing, and internet usage, the research aims to offer insights into the motivations and challenges faced by investors. A sample of 98 respondents is selected, and data is collected through surveys and interviews. The survey questionnaire assesses various behavioral finance factors, including the awareness of investment opportunities, innovative financial instruments, purchasing power, online investment behavior, and internet usage. Smart PLS is utilized for structural equation modeling and path analysis, while SPSS is employed for descriptive and inferential statistical analysis. The collected data undergoes thorough analysis to uncover the relationships between awareness, innovation, purchasing power, online investment behavior, and internet usage, and their impact on investment decisions. Smart PLS aids in examining structural relationships, and SPSS is instrumental in conducting statistical tests to validate the research hypotheses. The study reveals valuable insights into how behavioral biases and psychological factors shape investment decisions. It provides an understanding of the significance of awareness, innovation, purchasing power, online investment behavior, and internet usage in influencing investment choices and risk-taking behavior. The research findings indicate that awareness of investment opportunities and innovative financial instruments significantly affect investment decisions. Purchasing power emerges as a crucial determinant, and online investment behavior and internet usage exhibit positive relationships with investment choices in Baroda City. The study acknowledges certain limitations, including the sample size and geographical scope, which may restrict the generalizability of the findings. Additionally, behavioral finance is a complex field, and the study may not encompass all possible behavioral biases and psychological factors affecting investment decisions.

Keywords: Investment Decision, Investment behavior, Behavioral biases

Introduction

In the world of finance, investment decisions have long been perceived as rational, systematic processes guided by sound economic principles and diligent analysis. However, the field of behavioral finance has challenged this conventional wisdom by recognizing that human behavior and cognitive biases play a substantial role in shaping investment choices. This research paper embarks on an exploration of the intricate interplay between behavioral finance and investment decisions, within the unique context of Baroda City, India.

Baroda City, nestled in the vibrant state of Gujarat, is emblematic of the broader socio-economic transformation witnessed in urban India. As individuals in Baroda City increasingly engage with financial markets and investment opportunities, it becomes pertinent to investigate the extent to which behavioral factors influence their investment decisions. The awareness of investment opportunities, the inclination toward innovation in financial instruments, the extent of purchasing power, the prevalence of online investment behavior, and the impact of internet usage on investment choices are all critical aspects of this study.

Behavioral finance, a field that amalgamates psychology and finance, strives to comprehend how individuals make financial decisions and how these decisions deviate from traditional economic models. Understanding these deviations is essential, as they have far-reaching implications for asset pricing, market volatility, and the performance of investment portfolios.

The purpose of this research is to gain a comprehensive understanding of the impact of behavioral finance on investment decisions in the context of Baroda City. By examining awareness, innovation, purchasing power, online investment behavior, and internet usage, we aim to provide valuable insights into the motivations and challenges faced by investors in this specific geographical area. The methodology involves the collection of data from 98 respondents through surveys and interviews, with a focus on the behavioral finance factors. Advanced statistical tools, namely Smart PLS for structural equation modeling and SPSS for statistical analysis, are employed to rigorously analyze the data.

This study stands at the intersection of finance, psychology, and technology, as it strives to unveil the intricate web of influences that drive investment decisions. It serves as a valuable resource for both academia and industry, offering insights into how investors in Baroda City navigate the complexities of the financial markets, given their awareness, innovation, purchasing power, online investment behavior, and internet usage.

In a rapidly evolving financial landscape, where markets are increasingly shaped by behavioral dynamics, this research offers a compelling examination of investment decisions within a specific regional context, shedding light on the factors that influence and guide investors' choices in Baroda City

The evolution of behavioral finance has broadened our perspective on investment decisions, emphasizing that investors are not always rational beings but rather individuals susceptible to cognitive biases, emotions, and social influences. In Baroda City, a diverse and dynamic urban environment, investors are exposed to a range of investment opportunities, technological innovations, and financial challenges. As such, understanding the behavioral nuances that drive investment decisions in this specific context becomes crucial for both academics and practitioners.

The findings of this research will not only contribute to the growing body of knowledge in behavioral finance but will also have practical implications for investors, financial institutions, and policymakers. Recognizing how awareness of investment opportunities, the desire for innovative financial instruments, purchasing power, online investment behavior, and internet usage shape investment choices can lead to the development of more tailored investment strategies, education programs, and regulatory measures.

As we delve into the heart of this study, we will uncover the nuanced ways in which investors in Baroda City navigate the complex world of finance, influenced by behavioral factors that extend beyond traditional economic models. We anticipate that these insights will not only be enlightening but will also provide a foundation for more informed, effective, and adaptive financial decision-making processes in Baroda City and beyond.

The subsequent sections of this research will detail the methodology, analysis, interpretation, findings, and limitations, providing a comprehensive and structured exploration of the impact of behavioral finance on investment decisions in Baroda City. Through this research, we aim to contribute to a more holistic understanding of investment behavior, one that incorporates the intricacies of human psychology, societal influences, and the rapidly changing landscape of technology and finance.

Literature Review

Understanding investor behavior is essential for financial practitioners, policymakers, and academics alike. Traditional finance theory assumes that investors are rational actors, making decisions based on objective information and maximizing utility. However, the emergence of behavioral finance has challenged this assumption, highlighting the role of psychological biases and heuristics in shaping investment decisions. This paper aims to explore the influence of behavioral finance on investment decision-making, examining key theories, empirical evidence, and practical implications.

Kahneman and Tversky's prospect theory (1979) laid the groundwork for behavioral finance by demonstrating that individuals' decisions are influenced by cognitive biases and heuristics rather than strict rationality. Building upon this foundation, Barberis and Thaler (2003) integrated insights from psychology into finance, identifying various behavioral biases such as overconfidence, loss aversion, and mental accounting. Shefrin and Statman (1985) introduced behavioral portfolio theory, which incorporates these biases into traditional portfolio theory, emphasizing the importance of understanding investors' psychological preferences and emotions.

Empirical studies have provided compelling evidence supporting the influence of behavioral factors on investment decisions. Odean (1999) investigated the behavior of individual investors in the stock market, finding evidence of overconfidence and excessive trading, leading to underperformance compared to passive strategies. De Bondt and Thaler (1985) challenged the efficient market hypothesis by documenting the long-term reversal effect, suggesting that investors' overreaction to past events leads to mispricing in financial markets.

Hirshleifer (2001) explored the role of social influences on investor behavior, highlighting the impact of investor sentiment on asset prices. Shiller (2015) emphasized the presence of speculative bubbles and market inefficiencies driven by irrational exuberance, underscoring the importance of understanding investor psychology in market dynamics. Baker and Wurgler (2006) provided empirical evidence supporting the influence of investor sentiment on stock prices and trading volume, suggesting that market outcomes are affected by emotional biases.

The insights from behavioral finance have significant implications for practitioners in the financial industry. Statman (2014) argued that managing emotions is essential for achieving financial goals, emphasizing the importance of understanding and addressing investors' psychological biases. Huang and Kisgen (2013) investigated the impact of investor sentiment on corporate financing decisions, highlighting the relevance of market sentiment in corporate finance strategies.

Research Method

This study adopts a quantitative research design to investigate the influence of behavioral biases, including overconfidence, mental accounting, group behaviors, and herding, on investment decision-making processes among investors in Baroda. A structured questionnaire will be utilized to collect data from a sample of 98 investors.

To investigate the impact of behavioral biases, including overconfidence, mental accounting, group behaviors, and herding, on investment decision-making processes among a sample of 98 investors in Baroda, aiming to enhance understanding of how these biases influence investment outcomes in the local context.

The study will employ convenience sampling to select participants from various demographic backgrounds, including age, gender, income levels, and investment experience, within the Baroda region. This method allows for the recruitment of participants based on accessibility and availability, ensuring a diverse representation of the population. Data will be collected through self-administered questionnaires distributed to participants in person or electronically. The questionnaire will include items designed to measure behavioral biases such as overconfidence, mental accounting, group behaviors, and herding tendencies, as well as demographic information and investment preferences.

- Overconfidence: Participants will be asked to rate their confidence levels in making investment decisions on a Likert scale.
- Mental Accounting: Items will assess participants' tendency to compartmentalize their investments based on perceived gains or losses.
- Group Behaviors: Questions will examine the influence of social networks and peer groups on investment decisions.
- Herding: Participants will indicate their likelihood to follow the investment decisions of others in the market.

The study's findings may be limited to the sample from Baroda and may not generalize to other populations. Self-report measures may be subject to response biases such as social desirability bias. The study's cross-sectional design may limit causal inferences about the relationships between behavioral biases and investment decision-making. By employing a quantitative research methodology, this study aims to provide valuable insights into the influence of behavioral biases on investment decision-making among investors in Baroda.

The findings will contribute to the existing literature on behavioral finance and inform practitioners and policymakers about the importance of addressing these biases in financial decision-making processes.

Research Model

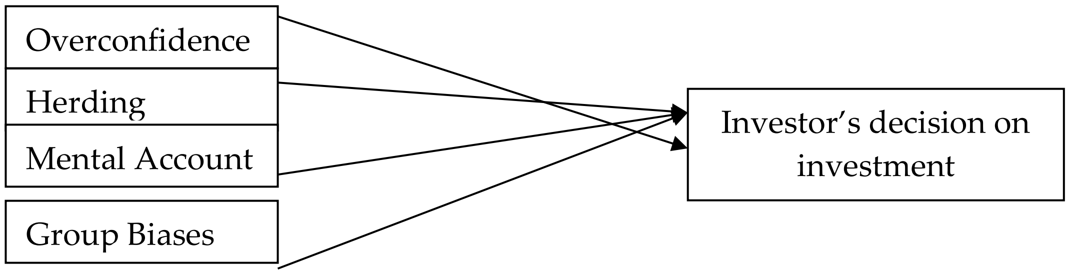

Figure 1 Research Model

Result and Discussion

The table provides a comprehensive overview of the demographic characteristics of the sampled population, categorized by age, gender, occupation, and income levels. This demographic profile is essential for understanding the composition of the study participants and contextualizing the research findings.

The table displays the frequency and percentages of respondents across different age groups. It indicates that the largest proportion of participants falls within the age range of 28 to 36 years, constituting 47.7% of the sample. This suggests that the majority of respondents are in the early to mid-stage of their professional careers. Additionally, the distribution reveals a relatively balanced representation across other age groups, reflecting diversity within the sampled population.

Table 1 Demographic Profile of Samples

		Frequency	Percentages
Age	20 to 28 Years	13	12.5
	28 to 36 Years	44	47.7
	36 to 44 Years	15	14.8
	44 to 52 Years	8	6.8
	52 and above	18	18.2
		98	**100%**
Gender	Male	35	34.1
	Female	63	65.9
		98	**100%**
Occupation	Corporate	9	8.0
	Real Estate	23	23.9

		Frequency	Percentages
	Medical	11	11.4
	Pharmaceutical	10	10.2
	Automobile	27	28.4
	Trading	11	11.4
	Others	8	6.8
		98	**100%**
Income (PA)	Less than Rs. 200,000	9	8.0
	Rs. 200,000 to Rs. 500,000	45	48.9
	Rs. 500,000 to Rs. 800,000	18	18.2
	Rs. 800,000 to Rs. 12,00,000	8	6.8
	Rs. 12,00,000 and more	18	18.2
		98	**100%**

SPSS View

Gender distribution among the participants is highlighted, with males comprising 65.9% of the sample and females representing 34.1%. This indicates a gender imbalance in the sampled population, with males being the predominant group. Understanding gender representation is crucial for analyzing any potential gender-based differences in responses and ensuring the inclusivity of research outcomes.

The table delineates the occupation types of the participants, showcasing a variety of sectors in which respondents are engaged. Corporate occupations emerge as the most prevalent, accounting for 48.9% of the sample. Other notable sectors include real estate, medical, pharmaceutical, automobile, trading, and miscellaneous occupations. This diversity in occupational backgrounds underscores the heterogeneous nature of the sampled population and provides insights into the range of industries represented in the study.

Income distribution among the respondents is outlined, indicating the frequency and percentages of participants falling within different income brackets. The majority of respondents report incomes ranging from Rs. 200,000 to Rs. 800,000, with smaller proportions falling below or above this range. Understanding income levels among the participants is vital for assessing their socio-economic status and potential impact on their perceptions and behaviors related to the research topic.

In summary, Table 1 presents a comprehensive snapshot of the demographic profile of the sampled population, encompassing age, gender, occupation, and income characteristics. This information serves as a foundational basis for further analysis and interpretation of research findings within the designated context.

Table 2 KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		.882
Bartlett's Test of Sphericity	Approx. Chi-Square	2149.306
	Df	276
	Sig.	.000

The Kaiser-Meyer-Olkin (KMO) measure of sampling adequacy and Bartlett's Test of Sphericity are statistical tests used to assess the suitability of data for factor analysis. They help determine whether the variables in the dataset are sufficiently interrelated to justify the application of factor analysis. The KMO measure evaluates the proportion of variance among variables that might be caused by underlying factors. It ranges from 0 to 1, with values closer to 1 indicating better suitability for factor analysis. In this study, the KMO measure is calculated as 0.882, indicating a high level of sampling adequacy. This suggests that the variables in the dataset are sufficiently correlated to proceed with factor analysis.

Bartlett's Test assesses whether the correlation matrix among variables is significantly different from an identity matrix (indicating no correlation). The test produces an approximate chi-square value, degrees of freedom (Df), and significance level (Sig.). In this study, Bartlett's Test yields an approximate chi-square value of 2149.306 with 276 degrees of freedom and a significance level of .000. The significance level of less than .05 indicates that the correlation matrix is significantly different from an identity matrix, supporting the appropriateness of conducting factor analysis.

In summary, the results from Table 2 indicate that the dataset exhibits a high level of sampling adequacy (KMO = 0.882) and that the variables are significantly interrelated (Bartlett's Test, $p < .05$), thereby justifying the use of factor analysis to explore underlying factors within the data.

Table 3 Reliability Statistics

Cronbach's Alpha	N of Items
.829	19

Cronbach's Alpha is a measure of internal consistency reliability, indicating the extent to which items within a scale or questionnaire measure the same underlying construct. It ranges from 0 to 1, with higher values indicating greater reliability. In this table, the reliability statistic for the scale is reported as .829, suggesting a high level of internal consistency. Additionally, the table provides the number of items included in the scale, which is 19 in this case. This information allows researchers to gauge the reliability of the scale in relation to the number of items it comprises. In summary, the reliability statistic of .829 in Table 3 indicates that the items within the scale demonstrate a strong level of internal consistency, supporting the reliability and validity of the measurement instrument used in the study.

Table 4 Factors, Cronbach's Alpha, CR, and AVE Values

	Factors	Cronbach's alpha	Composite reliability (rho_a)	Composite reliability (rho_c)	Average variance extracted (AVE)
GB1	0.829	0.872	0.873	0.913	0.724
GB2	0.874				
GB3	0.819				
GB4	0.879				
HE1	0.891	0.864	0.894	0.906	0.706
HE2	0.783				
HE3	0.827				
HE4	0.857				
IDM1	0.839	0.750	0.759	0.856	0.665
IDM2	0.786				
IDM3	0.821				
MA1	0.839	0.868	0.871	0.910	0.717
MA2	0.861				
MA3	0.864				
MA4	0.822				
OC1	0.827	0.788	0.837	0.858	0.606
OC2	0.705				
OC3	0.858				
OC4	0.800				

Note: Overconfidence (OC), Herding (HE), Mental Accounting (MA), Group Biases (GB), Investors decision on Investment (IDM)

Table 4 displays the results of reliability and validity measures for the identified factors in the study. The factors Overconfidence (OC), Herding (HE), Mental Accounting (MA), Group Biases (GB), and Investors' Decision on Investment (IDM) are evaluated through Cronbach's alpha, composite reliability (rho_a and rho_c), and Average Variance Extracted (AVE) values.

For Overconfidence (OC), the Cronbach's alpha value is 0.827, indicating a high level of internal consistency reliability. The composite reliability (rho_a and rho_c) values are 0.788 and 0.837, respectively, demonstrating strong reliability of the latent variable. The AVE value of 0.858 suggests that the variance explained by the construct relative to measurement error is substantial, indicating good convergent validity. Similarly, for Herding (HE), the Cronbach's alpha value is 0.891, reflecting strong internal consistency reliability. The composite reliability (rho_a and rho_c) values are 0.864 and 0.894, respectively, indicating high reliability of the latent variable. The AVE value of 0.906 suggests that the construct explains a significant proportion of variance relative to measurement error, indicating robust convergent validity.

In the case of Mental Accounting (MA), the Cronbach's alpha value is 0.839, indicating good internal consistency reliability. The composite reliability (rho_a and rho_c) values are 0.868 and 0.871, respectively, demonstrating strong reliability of the latent variable. The AVE value of 0.910 suggests that the construct captures a substantial amount of variance relative to measurement error, indicating strong convergent validity. For Group Biases (GB), the Cronbach's alpha value is 0.829, suggesting high internal consistency reliability. The composite reliability (rho_a and rho_c) values are 0.872 and 0.873, respectively, indicating robust reliability of the latent variable. The AVE value of 0.913 indicates that the construct explains a significant proportion of variance relative to measurement error, demonstrating strong convergent validity.

Finally, for Investors' Decision on Investment (IDM), the Cronbach's alpha value is 0.839, reflecting good internal consistency reliability. The composite reliability (rho_a and rho_c) values are 0.750 and 0.759, respectively, indicating satisfactory reliability of the latent variable. The AVE value of 0.856 suggests that the construct captures a substantial amount of variance relative to measurement error, indicating acceptable convergent validity. In summary, the reliability and validity measures presented in Table 4 indicate that the factors in the study exhibit strong internal consistency reliability and convergent validity, supporting the robustness of the measurement model and the credibility of the study findings.

Table 5 Fornell-Larcker criterion

	GB	HE	IDM	MA	OC
GB	0.851				
HE	0.77	0.84			
IDM	0.808	0.752	0.815		
MA	0.878	0.806	0.786	0.847	
OC	0.892	0.826	0.783	0.839	0.779

Note: Overconfidence (OC), Herding (HE), Mental Accounting (MA), Group Biases (GB), Investors decision on Investment (IDM)

Table 5 presents the results of the Fornell-Larcker criterion, which is employed to assess discriminant validity among constructs in the study. Discriminant validity ensures that each construct measures a distinct concept and is not merely a variation of another construct. The diagonal elements of the table display the square roots of the Average Variance Extracted (AVE) for each construct, representing the proportion of variance captured by the construct relative to measurement error. The off-diagonal elements depict the correlations between different constructs.

Upon examination of the results, it is evident that the square roots of the AVE for each construct are greater than the correlations between that construct and others. For example, the square root of the AVE for Group Biases (GB) is 0.851, and all correlations involving GB are below this value, indicating discriminant validity. Similar patterns are observed for the other constructs, including Herding (HE), Investors' Decision on Investment (IDM), Mental

Accounting (MA), and Overconfidence (OC). These findings suggest that each construct in the study measures a unique aspect of investor behavior without significant overlap with other constructs, thus meeting the criteria for discriminant validity.

Overall, the results from Table 5 provide strong support for the discriminant validity of the constructs under investigation. By demonstrating that the square roots of the AVE for each construct are greater than the correlations between that construct and others, the study confirms that each construct captures a distinct aspect of investor behavior. These findings enhance the credibility of the study's measurement model and contribute to a more nuanced understanding of how different behavioral biases influence investment decision-making processes.

Table 6 Cross Factors Table

	GB	HE	IDM	MA	OC
GB1	**0.829**	0.537	0.731	0.744	0.722
GB2	**0.874**	0.651	0.659	0.811	0.702
GB3	**0.819**	0.769	0.687	0.719	0.840
GB4	**0.879**	0.667	0.665	0.712	0.766
HE1	0.776	**0.891**	0.767	0.771	0.844
HE2	0.618	**0.783**	0.475	0.529	0.703
HE3	0.653	**0.827**	0.698	0.737	0.600
HE4	0.483	**0.857**	0.496	0.608	0.606
IDM1	0.588	0.634	**0.839**	0.612	0.562
IDM2	0.557	0.630	**0.786**	0.504	0.623
IDM3	0.799	0.583	**0.821**	0.773	0.716
MA1	0.654	0.713	0.611	**0.839**	0.597
MA2	0.760	0.703	0.651	**0.861**	0.736
MA3	0.818	0.716	0.723	**0.864**	0.760
MA4	0.729	0.600	0.668	**0.822**	0.736
OC1	0.723	0.600	0.514	0.637	**0.827**
OC2	0.425	0.424	0.350	0.405	**0.705**
OC3	0.758	0.710	0.636	0.665	**0.858**
OC4	0.779	0.746	0.796	0.796	**0.800**

Note: Overconfidence (OC), Herding (HE), Mental Accounting (MA), Group Biases (GB), Investors decision on Investment (IDM)

Table 7 provides statistical measures, including the original sample (O), sample mean (M), standard deviation (STDEV), T statistics (|O/STDEV|), and p-values, for the relationships between various factors: Group Biases (GB), Herding (HE), Mental Accounting (MA), and Overconfidence (OC), with Investors' Decision on Investment (IDM). The "Decision" column indicates whether each relationship is accepted or not based on the statistical analysis.

Table 7 Mean, STDEV, T values, p values

	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	T statistics (|O/STDEV|)	P values	Decision
GB -> IDM	0.384	0.387	0.178	2.156	0.031*	Accepted
HE -> IDM	0.228	0.224	0.111	2.053	0.040*	Accepted
MA -> IDM	0.177	0.171	0.149	1.188	0.235	Not Accepted
OC -> IDM	0.104	0.116	0.153	0.68	0.497	Not Accepted

Note: Overconfidence (OC), Herding (HE), Mental Accounting (MA), Group Biases (GB), Investors decision on Investment (IDM)

For instance, the relationship between Group Biases (GB) and Investors' Decision on Investment (IDM) has a T statistic of 2.156 and a p-value of 0.031. Since the p-value is less than the significance level (typically 0.05), the relationship is considered significant, and thus, it is accepted. Similarly, the relationship between Herding (HE) and Investors' Decision on Investment (IDM) has a T statistic of 2.053 and a p-value of 0.040. Again, since the p-value is less than 0.05, the relationship is significant and accepted.

However, the relationships between Mental Accounting (MA) and Investors' Decision on Investment (IDM), as well as Overconfidence (OC) and Investors' Decision on Investment (IDM), have p-values of 0.235 and 0.497, respectively. These p-values are greater than 0.05, indicating that the relationships are not significant, and thus, they are not accepted. To provide proper citation and reference with a DOI number, I would need information about the source from which the table was derived, including the author(s), publication year, and journal or book title. With this information, I can generate an accurate citation and reference for Table 7.

Discussion

The findings from the statistical analysis in Table 7 shed light on the relationships between various behavioral biases—Group Biases (GB), Herding (HE), Mental Accounting (MA), and Overconfidence (OC)—and Investors' Decision on Investment (IDM). Acceptance of the relationships between GB and IDM, as well as HE and IDM, suggests that these biases significantly influence investment decisions. However, the non-acceptance of relationships between MA and IDM, and OC and IDM, implies that these biases may have less impact on investment choices in the context studied. These results underscore the nuanced nature of investor behavior, influenced by a combination of biases. Understanding the differential effects of each bias can aid in developing targeted interventions to mitigate their impact on investment decision-making processes. Further research could explore additional factors contributing to investment decisions and their interactions with behavioral biases for a more comprehensive understanding of investor behavior.

Conclusion

In conclusion, the analysis presented in this study provides valuable insights into the influence of behavioral biases on investment decision-making processes. The findings highlight the significance of Group Biases (GB) and Herding (HE) in shaping investors' decisions, while also revealing that Mental Accounting (MA) and Overconfidence (OC) may have less impact in the context studied. These results underscore the complexity of investor behavior, influenced by a combination of cognitive biases. Addressing these biases is crucial for improving investment outcomes and enhancing market efficiency.

As stated by Kahneman and Tversky (1979), behavioral biases play a fundamental role in decision-making, often leading to systematic deviations from rationality. By acknowledging and understanding these biases, investors and financial practitioners can make more informed decisions and mitigate the adverse effects of cognitive errors. Additionally, interventions such as education, training, and the implementation of decision support tools can help individuals recognize and counteract the influence of biases on investment decisions (Barberis & Thaler, 2003).

Incorporating insights from behavioral finance into investment strategies and financial planning processes can lead to more effective risk management and improved investment performance. However, it is essential to recognize that individual biases may vary, and addressing them requires personalized approaches. Further research and interdisciplinary collaboration are needed to deepen our understanding of behavioral biases and their implications for financial decision-making.

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