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FACTORS SHAPING INVESTMENT CHOICES IN THE INDIAN CAPITAL MARKETS

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1.0 Abstract

There are wide difference between academicians and practioners on the issue of factors affecting individual investor's investment decisions in capital markets. One school of thought assumes that investors use all available information and make rational investment decision. Another school of thought argues that investors are not always rational but there are large number of other factors also which affect the individual investor's investment decisions in capital markets. Based upon the growing importance of behavioral finance the present study is an attempt to investigate effect of' socio-economic conditions of the investor on the investment decisions in Indian capital market. The result of this study can be of great importance to the regulatory authorities in creating awareness by educating investors about the importance of behavioral factor .This may help in increasing the investors' confidence in capital market.

2.0 Introduction

Capital markets in India have grown up leaps and bounds in the last few years. The development in Indian market has taken place in terms of depth and breadth in market. Over the last few years the participation of retail investors in Indian capital market has considerably increased. Retail investors take part more actively than before. There are large number of factors responsible for this. Prominent amongst them are ease of operations in capital markets, growth of awareness, increase in economic activities etc. With the growth in market the volatility in the market has also increased leading to more instability. This has increased the risk associated in the market.

Efficient Market Hypothesis (EMH) assumes that the investors use all available information to make rational investment decision **(Waweru, Munyoki & Uliana, 2008; Meditinos, Sevic & Theriou, 2007). Masomi and Ghayekhloo (2011)** observed that under the paradigm of traditional financial economics, people who make the decisions are usually considered to be rational and utility maximizing. According to **Chandra and Kumar (2008),** investor rationality is defined as being reasonable and making decisions that are in their best interest**.**

Somil (2007) observed that the proponent of the theory of rational investor assume that an individual makes a decision on the basis of the principles of maximization, self-interest and consistent choice. According to Somil (2007), rationality also assumes that an investor has perfect information of his surroundings and makes the decisions with the sole objective of profit maximization. The reasoning derivable from this principle of rationality is that the capital market must be efficient. Capital market efficiency implies that all information regarding the market is fully and instantaneously reflected in security prices and available to all investors. But most capital markets operate under inefficient conditions, making rational decisions impossible.

Al-Tamimi (2005) investigated the factors influencing individual investor behavior on the United Arab Emirates (UAE) financial markets. The study found that the six most influencing factors in order of importance were: expected corporate earnings, get rich quick, stock marketability, past performance of the firm's stock, government holdings and the creation of the organized financial markets. He also found the least influencing factors to be expected losses in other local investments, minimizing risk, expected losses in international financial markets, family member opinions and gut feeling on the economy.

Geetha and Ramesh (2012) studied the relevance of demographic factors in investment decisions in Tamilnadu, India, and claimed that the demographic factors have a significant influence over some of the investment decision elements, while insignificant influence was found on some other elements.

Jain and Mandot (2012) studying the impact of demographic factors on investment decision of investors in Rajasthan, concluded that various demographic factors like age, marital status, gender, city, income level, market knowledge, occupations and qualifications have a major impact on investment decision of investors.

Sultana and Pardhasadhi (2012) investigated factors influencing Indian individual equity investors' decision making and behaviour. After applying factor analysis, the 40 attributes were reduced to ten factors of individual eccentric, wealth maximization, risk minimization, brand perception, social responsibility, financial expectation, accounting information, government and media, economic expectation and advocate recommendation factors.

But in real market investors do not do so. There exists a variation in the perception of investors the market and its instruments. Studies also support that investors' deviate from rationality and show repeated patterns of irrational behavior and variation due to greed, fear, emotions, speculation, and subjective thinking while making investment decisions **(Meditinos et al, 2007; Evans, 2006; Gao and Schmidt, 2005; Warneryd, 2001).**

The important research studies in this field were made by **Thaler (1980), DeBondt & Thaler (1985; 1987), Yaari (1987), Samuelson & Zeckhauser (1988).** Finance names them as anomalies in stock market and the basis for naming them anomalies is that they could not be explained in classical financial framework **(Szyszka, 2007).** To deal with anomalies was a challenge for traditional finance theories and a new discipline, behavioral finance emerged. Behavioral Finance is the study of the influence of psychology on the behavior of financial practitioners' decision and the subsequent effect on markets **(Sewell, 2010).** The importance of psychological, emotional, and behavioral factors influencing the decision making of finance practitioners cannot be ignored. Behavioral finance is a fast developing field of study in academics which mainly focuses on the irrationality in decision making of market participants and its affect on stock prices **(Morck, 2004).**

Indian capital markets in the last few decades have grown considerably. The role of retail investors in the capital markets has also increased. In this study an attempt has been made to investigate effect of socio-economic conditions of the investor on the investment decisions in Indian capital market.

3.0 Research Methodology

3.0.1 Objectives

1. To identify factors affecting individual investor's investment decisions in capital market.
2. To study the impact of demographics on factors affecting individual investor's investment decisions in capital market.

3.0.2 Date Collection: Primary data was used for the purpose of this research.

3.0.3 Development of Survey Instrument

For the purpose of collection of data a self made questionnaire was used. In order to develop the questionnaire extensive review of literature and discussion with practitioners and academicians was done. The review of literature and discussion led to identification of 38 items / statements.

These 38 items were circulated to a panel of experts possessing vast experience in the field of capital markets. The panel suggested certain changes which were incorporated finally leaving the total number of items/statements as 28. The questionnaire was made on Likert scale and responses were marked as 5 = Strongly Agree, 4 = Agree, 3 = Neutral, 2 = Disagree, 1 = Strongly Disagree.

3.0.4 Sample Size

The questionnaire was circulated to a total of 400 respondents. Out of which only 369 were received back. 23 questionnaires were discarded due to ambiguous responses or missing data thus the total no of respondents were 346 resulting into 86% response rate.

3.0.5 Defining Variables

Independent Variable: -- The first 06 questions of the questionnaire included questions about respondent's age, marital status, occupation, gender, income, education. Practioners and researchers have considered these variables as very effective in determining factors considered important while investing in capital markets.

Dependent Variable: -- Factors influencing investment in capital market were determined by each respondent's response on the 22 questions given in the questionnaire.

Table-1: Demographic Characteristics of the Sample

	Number	%
Total number of Respondents (Sample Size)	346	
Number of Males	208	60
Number of Females	138	39.8
Number of Bachelor respondents	186	53.7
Number of Married respondents	160	46.2
Number of Graduate respondents	102	29.4
Number of Post Graduate respondents	244	70.5
Number of respondents in the income group of up to Rs.2 lakh	22	6
Number of respondents in the income group of Rs.2 lakh to 5 lakh	86	24.8
Number of respondents in the income group of Rs.5 lakh and above	234	67.6
Number of respondents in the age group of 20 to 35 years	139	40
Number of respondents in the age group of 36 to 60 years	182	52.6
Number of respondents in the age group of 60 years and above	25	7

3.0.6 Factor Analysis

Factor analysis is conducted on the survey data using SPSS to determine the factors affecting investment decisions in capital market. The factor analysis resulted into following 5 factors:

1. **Past Performance**: Q3, Q7, Q8, Q9, Q10
   Past performance depicts the past share market performance of company's share in capital market. It shows the perception of customers affecting their buying attitude. It shows how much importance a respondent gives to the past performance of a company's share.
2. **Future Prospectus** : Q11, Q12, Q13, Q14, Q15
   This depicts the customers perception related to a stock and its future prospects in accordance with his calculation/study. What important role does this factor have in changing the buying attitude of customers can be studied.
3. **Dividend Policy**: Q16, Q17, Q18, Q19, Q20, Q21, Q28
   Whether a company follows a dividend policy and how does it effects the buying attitude of a customer is depicted by this factor. How much importance does a person gives while selecting a company in the capital market.
4. **Ownership / Management**: Q22, Q23, Q24, Q25, Q26, Q27

Up to what extent does the ownership or the management of the company and their decision effects the respondents buying or selling attitude in the market. How their decisions are going to affect the share pricing of the company.

5. **Market Scenario**: Q1, Q2, Q4, Q5, Q6
   What is the present market status and how will it impact the decisions and sentiments of the buyer respondents. What is the level of impact and can its result be seen directly or indirectly.

Impact of Gender on Factors Affecting Investment in Capital Market

Table 2: T-Test for Influence of Gender				
Factor	**Mean Value**		**t-Value**	**Sig**
	Male	**Female**		
Past Performance	4.56	3.27	2.575	0.007
Future Prospectus	4.07	3.12	1.343	0.066
Dividend Policy	4.91	3.94	2.680	0.005
Ownership / Management	4.33	3.51	2.755	0.003
Market Scenario	4.82	3.05	1.575	0.082

The table above shows the results of the independent t-test. It is clearly seen that there is a significant difference of gender on factors influencing investment decisions in capital market. The results imply that the gender of investors matters when making investment decision based on past performance, dividend policy, ownership and market scenario. Male investors reported significantly higher preference for past performance, dividend policy, ownership and market scenario. However, it was observed that factor Future prospectus has insignificant effect for gender. This is reasonable, because both males and females are ambitious and expectant of the bright future gains from their investments.

Impact of Age on Factors Affecting Investment in Capital Market

Table 3: T-Test for Influence of Age					
	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Past Performance	31.600	5	4.540	7.657	0.000
Future Prospectus	19.401	5	3.140	4.064	0.000
Dividend Policy	34.712	5	5.365	7.160	0.000
Ownership / Management	24.774	5	3.177	4.886	0.000
Market Scenario	32.517	5	5.026	6.620	0.000

The table above shows that there is a significant difference among different age groups for all the five factors. This leads us to a conclusion that age is a factor affecting investment decisions in Indian capital markets.

Impact of Marital Status on Factors Affecting Investment in Capital Market

Table 4: T-Test for Influence of Marital Status					
	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Past Performance	25.310	2	12.544	15.737	0.000
Future Prospectus	20.754	2	9.266	11.620	0.000
Dividend Policy	21.130	2	9.413	10.012	0.000
Ownership / Management	12.715	2	5.706	6.301	0.000
Market Scenario	19.510	2	8.644	9.065	0.000

The table above shows that there is a significant difference based on different marital groups for all the five factors. This leads us to a conclusion that marital status is a factor affecting investment decisions in Indian capital markets.

Impact of Educational Qualification on Factors Affecting Investment in Capital Market

Table 5: T-Test for Influence of Educational Qualification					
	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Past Performance	16.412	4	3.545	4.702	0.000
Future Prospectus	13.010	4	2.672	3.275	0.001
Dividend Policy	16.726	4	3.626	3.726	0.001
Ownership / Management	10.500	4	2.067	2.248	0.009
Market Scenario	12.031	4	2.419	2.434	0.007

All the five factors showed significant difference among the different educational groups. This reveals that education is a factor affecting investment decision of investors.

Impact of Income on Factors Affecting Investment in Capital Market

Table 5: T-Test for Influence of Income					
	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Past Performance	7.523	5	1.616	1.046	0.061
Future Prospectus	2.882	5	0.688	0.773	0.381
Dividend Policy	12.040	5	2.520	2.573	0.002
Ownership / Management	7.055	5	1.502	1.560	0.130
Market Scenario	5.080	5	1.107	1.076	0.205

The results indicate that only the factor Dividend Policy shows significant difference among the different income groups of the respondents. Rest all other four factors were insignificantly different among the different income groups of the respondents.

4.0 Conclusion

In spite of many finance techniques that anticipate financial trends, there have been major depressions in the financial markets due to behavioural nature of investors. Unlike institutional investors, individual investors are believed to be less informed, have psychological biases and also thought of as the proverbial noise traders in the stock market **(Kyle, 1985; Black, 1986)**. Due to which researchers in finance tend to give credence to the behaviour of institutional investors. They believed that the performance of individual investors hardly ever influenced the stock prices. Thus major of strategies and policies were confined to institutional investors. They were a major source of attraction for policy makers, investment advisors. **Kaniel et al. (2008).** Thus impeding the interests of retail investors.

In order to target any market, it is must for the organization to understand the market, customer and the product. There must be a perfect fit between the customer's expectation regarding quality and the product, which is given to the customer. Financial product especially capital markets products is not the odd one out. Capital markets instruments are subjected to risk, investors must be aware of this risk. The research identifies five factors considered by investors while investing in capital markets they are Past Performance, Future Prospectus, Dividend Policy, Ownership / Management, Market Scenario. Further the research found that demographic factors like gender, age, marital status, educational qualification and income significantly affected an individual's investment decisions in capital market.

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