CHAPTER 1
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INTRODUCTION

1.1 NEED AND IMPORTANCE OF THE STUDY

Investment is commonly understood as parting with liquidity for an uncertain future reward. Investment is of three types, viz. Business Investment, Economic Investment and Financial Investment. Whereas business investment is concerned with the capital introduced for carrying on the business, economic investment is the net additions to the assets of an economy during a given period and financial investment is concerned with the investment in the various securities, such as shares, debentures, government securities and so on. Therefore, investment operation is a continuous one involving decisions such as what to invest, when to invest, how much to invest, and when to disinvest and trade off between return on investment and risk.

Investors are of two types, namely, Individual and Institutional. As regards individual investors, the propensity to save is always stronger than the inducement to invest, and the factors which induce the investors to invest have always been weaker or not sufficiently attractive.
The Economic Utility Theory views the individual's investment decision as a trade off between immediate consumption and deferred consumption. The individual investor weighs the benefits of consuming today against the benefits that may be gained by investing unconsumed funds in order to enjoy greater consumption at some point in the future.

The axioms of utility theory, developed by Von Neumann and Morgenstern, reiterate that investors are (i) completely rational, (ii) able to deal with complex choices, (iii) risk-averse and (iv) wealth-maximising. Utility theory further assumes that investors maximize expected utility -- measured in terms of anticipated returns and variances from these expectations, i.e. each investor selects the portfolio that maximizes expected return while minimizing risk.

Other theories of investor preference have made less stringent assumptions about how investors make choices. Competing theories have argued that investors (i) seek investments that maximize geometric mean return, (ii) concentrate on avoiding 'bad' outcome (safety-first models) or (iii) make investment decisions free of assumptions about utility functions or probabilities (stochastic dominance).
The literature on utility theory does not typically address individual investor decision processes. Rather, it focuses on the development and refinement of 'macro' models that explain aggregate market behaviour. Baker and Haslem, for example, believe that dividends, expected returns and the firm's financial stability are critical considerations for individual investors.

Successful investment requires a special kind of judgement and flair in analysing market behaviour which is associated more with psychology than with pure fact and formula. All the movements of men are motivated by their minds. The human mind is more emotional than factual in its decision making. So, it follows, that an understanding and recognition of mass psychology is the dominant factor in making many correct decisions, since the best psychologists are usually the best investors. The appraisal of mental attitudes outweighs statistical valuation.

Mr. Scheinman's view is that most investors lose because they try to apply rational measures, fundamental and technical, to an irrational market of human emotions. He demonstrates convincingly the uselessness of most investment advice, or at least its application by the average investor.

1. Loeb Gerald M. - The Battle of Stock Market profits
   Simon & Schuster, New York, Feb, 1971

2. Scheinman William X. - Why most investors are mostly wrong most of the time - Weybright & Talley, New York, 1970
As he sees it, the unsophisticated investor is mainly governed by hope of profit and fear of loss, especially the latter, and consequently does the wrong thing at the wrong time. To improve his performance, the investor must not only pick the right stocks but must correctly time the purchases and sales by anticipating the actions of others. By knowing himself, he can better interpret market psychology. While individual action is impossible to predict, the action of the crowd can often be anticipated.

In all the above studies, there is one common streak, namely, the investor’s obsession with maximisation of returns from safe investment. However, Schienman’s observation makes a deviation. He feels that an investor by knowing himself, can make a better investment decision. As pointed out earlier, he is of the opinion that while it is impossible to predict individual action, the action of the crowd can be anticipated. It is precisely this observation that provided the cue for the present study on investor behaviour.

The behaviour of the investors is varied and the factors influencing their investment are many. The proposed study on individual investors behaviour is made to identify the variables which tend to have a bearing on the individual investor behaviour, to study the relationship between the personal factors (viz. Age, Education, Income, Investment
experience and influence on Investment decision) and the investors’
behaviour, to identify the pattern of investment behaviour and to study the
nature of responses for determining the suitability of investments for
individual investors.

1.2 SCOPE OF THE STUDY

Investors are of two types -- individual and Institutional. The
study is made with special reference to individual investors -- Investors’
Investment behaviour based on 25 identified variables. The study has
been made with reference to four metropolitan cities of India.

1.3 OBJECTIVES OF THE STUDY

The overall objective of the study is to analyse individual investor
behaviour with a view to aid management of corporate houses to deal
with the individual investors.

The specific objectives include:

1. To identify the variables which tend to have a bearing on
   individual investor behaviour.
2. To study the relationship between the personal factors (viz, Age, Education, Income, Investment experience and influence on Investment decision) and individual investors' behaviour.

3. To analyse the nature of responses of individual investors as regards investment in Corporate securities.

4. To describe the pattern of the exhibited investment behaviour.

5. To suggest guidelines for Corporate Houses with regard to their approach towards Individual Investors.

1.4 METHODOLOGY

In this section, it is proposed to present a detailed account of the research design, size of the sample, sampling technique, nature of data and research instrument used for the present study.

1.4.1 Research Design

The research design used is Exploratory and Analytical. This study is exploratory because the views of the various investors have been ascertained to identify the factors influencing their investment behaviour. This study is also analytical because the study of the
investors' investment behaviour is expected to throw light in determining the pattern of investment behaviour and the suitability of investments for particular individual investor.

1.4.2 Size of the Sample

For a study of this type, defining the universe is no easy task. The size of the population is large. Using a stratified sampling procedure, conforming to the size of large sample, reasonably large well selected sample of 700 individual investors who were actively involved in the Stock Market was drawn from metropolitan cities of Mumbai, Delhi, Chennai and Calcutta. Efforts were taken to contact the respondents personally and to establish a rapport with them. For the purpose of final analysis, 414 completed, filled-in questionnaires were used.

1.4.3 Sampling Technique

Apart from the sample size, the only other way of increasing the precision of sample estimate of the population mean is to devise a sampling plan which will effectively reduce the variability in the population. This objective is achieved by Stratified sampling.

When the population is heterogeneous with respect to the variable or characteristic under study, then the technique of stratified sampling is
used to obtain more efficient results. Stratified random sampling involves the following steps:

Stratify the given population into a number of sub-groups or sub-populations known as Strata such that,

(a) the units within each stratum (sub-group) are as homogeneous as possible.

(b) the difference between various strata are as marked as possible.

(c) various strata are non-overlapping.

For the purpose of the present study, stratification of the sampling has been done under four basis. Firstly, geographic spread of the population has been ensured by choosing the respondents from the four major cities of India, namely Delhi, Mumbai, Calcutta and Chennai.

Secondly, the respondents' age group has been stratified into 5 groups. viz. Below 26 yrs; 26 – 35 yrs; 36 – 45 yrs. 46 – 55 yrs. and Above 55 years.

Thirdly, for the income of individuals, three-fold stratification has been followed. Income below Rs.5,000; Rs.5,000 – 10,000; and Above Rs.10,000.
Finally, the occupation of the respondents have been stratified as,

Professionals, Businessmen, Officials/employees and others.

1.4.4 Nature of data

The main type of data used for this study is Primary data. Survey method has been used to collect primary data. Based on review of literature on individual investors' behaviour, the following variables have been identified for the present study. These variables were used for the understanding of the individual investors.

1. Expected Corporate earnings
2. Diversified Business activities
3. The influence of the nature of the firm's product and quality of service
4. Information from Financial statements
5. Reputation of the firm
6. Stock Brokers recommendations
7. Information in Reports and Prospectus
8. The Price of share
9. Past performance of Stock
10. Expected Dividend
11. Institutional Holdings
12. Risk-return analysis

13. Tax concessions/Exemptions

14. Expected Stock market performance

15. Past performance of Investors’ stock portfolio

16. Current Economic indicators

17. Promoters'/Managements' reputation and track record

18. Competing financial needs of investors

19. Recent price movements of firm's stock

20. Friends' or Co-workers' recommendation

21. International operations

22. Exchange listing

23. Influence of tips and information from Business Journals

24. Attraction for non-stock investments

25. Political stability

1.4.5 Research Instrument

In order to study the influence of these variables on the individual’s investment behaviour, a questionnaire was prepared. The questionnaire consists of two sections. In the first section there are statements reflecting the decision making process of individuals. These statements were framed highlighting the twenty-five variables mentioned above. Some of these statements have been positively worded and some
negatively worded and they have been mixed up. The answers to the statement have been graded on a five-point Likert type scale. In the framing of these statements, reference was made to the various literature available on the subject. Further a committee of experts was identified for the purpose of scrutiny of statements. The committee comprised of a Psychologist, an Educationist, a Stock-broker and a Financial consultant/analyst.

The original questionnaire containing hundred and fifty statements was drafted, a pilot study was conducted. After an analysis of the results of the pilot study, minor changes in the wording of the statements and a reduction in the number of statements from one hundred and fifty to one hundred was made in the final questionnaire.

The second section of the Questionnaire consisted of personal data such as age, education, occupation, income level, years of investment experience and influence on investment decision.

Internal consistency of the questionnaire has been ensured by mixing up the statements which would serve as a cross-check. In order to ensure that there was no bias on the part of the respondents, the variables taken up for the purpose of the study were not positively indicated in the questionnaire.
The reliability of the responses was taken care of by using the 'Test and Retest' method and Correlation results.

1.5 LIMITATIONS OF THE STUDY

Firstly, even though the questionnaire was distributed to investors in the four major metropolitan cities of India, namely, Mumbai, Delhi, Chennai and Calcutta, majority of the questionnaires could be collected only from Chennai. The results of the study should be a fair indicator of the behaviour and the patterns of behaviour. The pattern of behaviour of the respondents in Chennai should reflect the general pattern of behaviour in other parts of the country.

Secondly, the results of the study are subject to the personal prejudices and bias of the respondents.

Thirdly, the majority of the respondents are from the age group 26-45 and income group above Rs.5000. The results are based on their views and opinions.

Finally, the study has been made with reference to 25 identified variables only. These variables have been identified based on the review of literature. The possibility of other variables at work cannot be ruled out.
1.6 ARRANGEMENT OF CHAPTERS

The present study on investment behaviour of individual investor has been conducted with a view to studying the individual investor behaviour and to aid management of corporate houses to deal with the investors.

The results of the study have been detailed in eight chapters, as follows:

Chapter 1 deals with the background of the study and traces the need and importance of the study. It also includes the objectives of the study, methodology and limitations of the study.

Chapter 2 highlights the Statistical Tools employed in the analysis of data for the present study.

Chapter 3 presents a review of literature available on the subject of study, both foreign and Indian.

Chapter 4 deals with the various operative definitions of the important concepts, important theories of investment behaviour and other conceptual aspects.
Chapter 5 highlights the results of *Factor analysis* which has been used to identify variables which tend to have a bearing on individual investors' decision.

Chapter 6 deals with the results of *analysis of variance* to study the relationship between the personal factors and individual investor behaviour.

Chapter 7 explains in detail the results of the *Discriminant analysis* and *cluster analysis* that have been used to study the nature of responses and to describe the patterns of investment of behaviour exhibited by individual investors.

Chapter 8 gives the summary of conclusions, suggestions and recommendations based on the study.