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A Study of Behavioural Biases and Investment Decisions: An Empirical Analysis

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Abstract
Investors frequently use emotional and cognitive biases in addition to strictly rational analysis when making decisions. In order to investigate the crucial role that behavioural biases play in influencing investment decisions, this paper synthesizes previous research. This literature-based study examines the relationship between psychology and finance, highlighting important biases like overconfidence, loss aversion, anchoring, herding, and disposition effects, based on a variety of studies carried out in India and Nepal. The paper highlights the relevance of behavioural finance in both developed and emerging markets, with a focus on the behavioural patterns of millennial investors. The results challenge the presumptions of traditional economic theories by indicating that individual investment behaviour is intricate, multidimensional, and heavily influenced by psychological factors.

Keywords: Behavioural Finance, Investment Decisions, Financial Decision-Making, Investment Behaviour

Introduction
Success in investing goes beyond analyzing financial data or tracking market trends—it is deeply influenced by human behaviour. Investment decisions are not always the result of purely rational calculations; rather, they are often shaped by psychological and emotional factors. By examining how cognitive biases and emotions affect financial decision-making, the field of **behavioural finance** seeks to understand these influences. By gaining insights into the psychological drivers behind investment behaviour, investors can make more informed choices and potentially improve their investment outcomes.
At its core, behavioural finance integrates concepts from **psychology and economics** to explore how individuals actually make financial decisions. While **traditional economic theories** assume that investors are rational actors who use logic and objective information to maximize utility, behavioural finance recognizes that this assumption often fails in real-world scenarios. **Cognitive errors, emotional reactions, and mental shortcuts** frequently lead to irrational behaviour, which can significantly affect investment results.
Repeated financial anomalies and crises have highlighted the limitations of conventional finance in explaining market behaviour. Behavioural finance, by incorporating the emotional and psychological dimensions of decision-making, offers a more realistic and nuanced framework for understanding how investors behave under uncertainty.
This paper aims to explore the existing body of literature on behavioural finance and assess how behavioural biases influence investor decisions. In particular, it focuses on how these biases manifest in

various **socioeconomic and cultural contexts**, with a special emphasis on **South Asian markets**, where investment behaviour is often shaped by unique demographic and psychological dynamics.

Objectives

- To identify the key behavioural biases influencing investment decisions.
- To analyze how these biases affect different investor groups.
- To understand how behavioural finance complements or challenges traditional financial theories.

Methodology

This study uses a qualitative literature review methodology. All findings are based on secondary data gathered from peer-reviewed journal articles, research papers, and academic publications related to behavioural finance. The review focuses on seven key studies published between 2017 and 2024 that analyze behavioural biases and investment decisions through various approaches, including surveys, regression analysis, and systematic literature reviews.

Literature Review

(Latifah Wulandari Binti Asbaruna, 2023) states that in the field of finance, behavioural finance is essential for understanding human behaviour, particularly that of investors. The type of data used is secondary data, meaning it was not given to data collectors directly; instead, it was obtained from books, scholarly publications, websites, and other resources pertaining to behavioural finance. A review of literature directly related to behavioural finance was used as the data collection method in this study. This study uses the Systematic Literature Review (SLR) technique, and its findings try to map out the trends in behavioural finance and predict its future direction, which is expected to provide new insights and contributions to the field in the future.

(Dilli Raj Sharma, October 2024): This study examines how individual investors' investment choices, financial risk inclination, and behavioural biases interact in Nepal's developing capital market. It investigates the ways in which biases like overconfidence, loss aversion, herding, experiential, disposition, and familiarity biases affect investment results both directly and indirectly through the propensity for financial risk.

(Dr. Vinay Kandpal, October 2018): The study looks at how investors behave when making investment decisions and what factors they consider. A questionnaire was used to survey Uttarakhand's faculty members. According to the study, behaviour plays a significant role in making wise investment decisions. As a result, when choosing an investment option, an investor must take into account a variety of factors, including their financial goals, spending patterns, income, perceptions of investments, lifestyle changes, time periods, investment nature, thought processes, natural habits, risk-bearing capacity, liquidity, and expected returns.

(Deepak Kumar Baser, September 2023): The study of psychology, sociology, and finance are all included in the broad field of behavioural finance. In addition to addressing anomalies within the efficient market on a macro level, it explores the complex behaviours and biases of investors on a micro level. Since behavioural biases have a significant impact on investor behaviour and human decision-making, behavioural finance is a well-established concept in the modern era. In order to obtain a thorough understanding of behavioural finance and its significance in influencing investors' financial decisions, we will critically review a variety of studies in this field in this essay.

(Utpal Poudel, 2024)With a focus on millennial investors, the study intends to investigate how behavioural biases such as overconfidence bias, anchoring bias, disposition effect, and herding behaviour affect Nepalese investors' decision-making when making investments. 200 active millennial investors in Pokhara participated in the study, which employed a purposive sampling technique to gather primary data. Regression analysis, correlation analysis, and descriptive statistics was used to analyse the data. The results show that overconfidence bias had a major positive influence on investor behaviour and was the most important factor influencing investment decisions. Notable benefits were also demonstrated by disposition and anchoring effects. Herding behaviour, however, showed no discernible influence on investment choices, indicating that Nepalese investors—especially millennials—tend to make their own decisions rather than mindlessly adhering to market trends. For stakeholders, financial institutions, and policymakers looking to enhance investment strategies and financial decision-making in Nepal, this study offers insightful information. It highlights how crucial it is to recognize and control behavioural biases, particularly in a developing market like Nepal.

(Sujata Kapoor, 2017)This study charts the advancement of behavioural finance over the course of financial history. It offers the first proof of behavioural abnormalities in stock markets that researchers have documented. It begins by discussing traditional finance and then analyzes traditional theories when they are thought to be inadequate. The importance of behavioural finance and its special role in bridging the gaps between traditional theories and real-world scenarios are then discussed in the paper.

(Prof.Devrshi Upadhyay, July 2019)The study of behavioural finance is a developing field that examines how psychological aspects influence judgment in ambiguous situations. One of the most crucial topics for understanding people's mindsets and how they approach different investment avenues is behavioural finance. We learned about people's mindsets when they invest in different investment avenues thanks to this study. That is, what do they consider when making investments? This study aims to determine the significant impact of specific behavioural finance concepts on the decision-making process of individual stock market investors. These concepts include overconfidence, perception, Representative, anchoring cognitive dissonance, regret aversion, narrow framing, and mental accounting. By creating a structured questionnaire and gathering a sample of 181 Ahmedabad investors, we carried out primary research. Understanding the effects of behavioural financing on investors and researching its significance and influence on investors' investment decisions were the main goals. On the other hand, our study's secondary goal was to understand the factors that influence investors' decisions to invest as well as the theories and concepts of behavioural finance.

Discussion

The literature review offers strong proof that behavioural biases are prevalent and pervasive in individual investors' decision-making processes.

According to numerous studies (Sharma, Poudel, Upadhyay), overconfidence bias is a common phenomenon that causes investors to overestimate their knowledge and control over investment outcomes, which encourages excessive risk-taking and frequent trading.

By encouraging investors to hang onto losing stocks or sell winning ones too soon, loss aversion and disposition effects seem to control decision-making. These biases are motivated more by emotional reactions than by logical analysis, and they frequently lead to less than ideal portfolio performance.

It's interesting to note that herding behaviour, which is commonly believed to rule investor behaviour in developing markets, was found to be negligible in certain demographic groups, especially among younger investors (Poudel, 2024). This might point to a generational trend toward more autonomous thought, made possible by information availability and digital financial tools.

Often mentioned were anchoring and mental accounting, which show how investors separate money into mental "buckets" or become fixated on starting prices, resulting in inconsistent and illogical decisions.

The study also shows that the degree and kind of bias displayed are significantly influenced by demographic factors like age, income, and education. Research by Kandpal and Upadhyay highlights that behavioural finance is not a one-size-fits-all approach; rather, it needs to take investors' sociocultural background into consideration.

Conclusion

The study of behavioural finance has become a vital tool for comprehending the intricate and frequently illogical actions of investors. Although fundamental, traditional financial theories are predicated on the notions of market efficiency and investor rationality, which have been repeatedly called into question by actual occurrences like market bubbles, crashes, and irregular investment trends. This literature-based study confirms that psychological biases and emotional inclinations play a major role in influencing financial decisions, which are not only influenced by market fundamentals or logical analysis.

Strong evidence that behavioural biases, including overconfidence, loss aversion, anchoring, herding, and the disposition effect, significantly impact investment behaviour can be found in the reviewed studies. These biases cause investors to stray from the best course of action when making decisions, which frequently leads to poor financial results. Understanding investor psychology becomes even more complex and context-dependent when considering the ways in which these behavioural patterns are further influenced by cultural, demographic, and socioeconomic factors, especially in markets like South Asia which is developing and emerging.

For instance, although overconfidence bias is present in all investor groups, its severity and effects vary depending on age groups and financial literacy levels. Similarly, research on millennial investors in Nepal revealed that herding behaviour, which is typically assumed to be common in developing markets, had less of an impact on some younger, better-informed investor groups.

The necessity of incorporating behavioural insights into financial education, investment advisory services, and policymaking is highlighted by this expanding corpus of literature. In order to help investors become more self-aware and disciplined investors, financial literacy programs should incorporate elements that teach investors about their cognitive biases and emotional influences. By adjusting their recommendations according to each client's unique behavioural profile, financial advisors and institutions can also improve their services and provide more individualized and successful financial planning.

Additionally, when developing regulations or investor protection mechanisms, policymakers in emerging economies ought to take behavioural factors into account. Better-informed policies that reduce systemic risks can result from acknowledging that investors are not always logical, particularly during periods of market volatility.

To sum up, behavioural finance offers practical insights into making better investment decisions in addition to deepening our understanding of how those decisions are made. Stakeholders in the financial ecosystem can create more robust, logical, and inclusive investment environments by recognizing and addressing the psychological aspects of investing. The role of behavioural finance in influencing investing in the future will only grow as financial markets continue to change, especially with the increase in retail participation and digital platforms.

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