International Journal of Education, Modern Management, Applied Science & Social Science (IJEMMASSS)
ISSN : 2581-9925, Impact Factor: 6.340, Volume 03, No. 02(III), April - June, 2021, pp.55-60

AN ANALYSIS OF FACTORS AFFECTING INVESTMENT DECISION MAKING OF INDIVIDUAL INVESTORS IN EQUITY SHARES IN INDIA

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ABSTRACT

The investments made by individual investors are influenced by a variety of factors depending upon their experience and knowledge of the financial markets and the financial system. This study is an attempt to understand the driving factors of investors' decisions, the reach of the 'investor awareness and education programmes' and to gain an insight of their mindset while investing in the equity markets. It is based on the quantitative analysis of the investor's responses and attempts to develop a conceptual framework that assesses how much of their investment behaviour is based on analysis and attempts to understand the role their experience span plays. It was found that the investors depended more on shortcuts like taking advice from friends and relatives than doing their own analysis through annual reports of the companies. The most common factors studied for investment in IPOs is company's background and for trading is EPS and the popularity of its products.

Keywords: *Investments, IPOs, EPS, Investor Awareness, Education Programmes*.

Introduction

The primary objective of an investor is to earn maximum returns with minimum risks. One of the most attractive investment alternatives in India is the financial equity markets. The financial markets in the country are broadly categorised into money market and capital markets. While corporations tap money markets to raise short term finance, they use capital markets for equilibrating demand and supply of long-term funds. The capital market is further bifurcated into primary market(for initial public offers of the securities) and the secondary market (where the trading of already issued securities takes place). The growth and future of both primary and secondary capital markets depends upon the quality of investment decisions made by the investors.

Recently, due to the global outbreak of COVID-19, the Indian financial markets suffered, like the rest of the world. The equity markets went through a major correction of more than 30% in quarter 1 of 2020, and then reached all-time highs in January 2021. The volatility and unpredictability of the markets has increased and this study attempts to understand the how. This is to evaluate how investors appraise a stock, while considering investing in it.

These investment decisions are affected by various factors that tend to differ individual to individual. In equity investments, assessment of prospective returns, timing and uncertainty holds significant value. Such decisions can be difficult for an investor with lesser knowledge and/or experience. Understanding investor's decision models comprises of understanding how such assessments are made by them and how these might change in response to the financial reports, information about the industry, economy or company, expectations of the share market and the management of the company in question.

Rationale-Gap Analysis

The financial markets are considered highly volatile, and their movement cannot be predicted to one hundred percent. This could be because the investors don't always act rationally. This has been a

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research topic for many decades. A study (Hemalatha, 2019) concluded that investors' choice for priority among the various aspects of investing like capital appreciation, tax benefit, returns, liquidity, risk, security varies according to demographic variables like age, gender and occupation. There have also been studies on the behavioral factors that lead to investment decisions (Antony & Joseph, 2017), like the overconfidence bias and regret aversion found among the investors in Kerala.

The Indian stock markets experienced massive changes in 2020 as studied through detailed analysis of composite and sectoral BSE indices (Rashmi Chaudhary et al., 2020)during the period. (Mishra et al., 2020)concluded that the impact of COVID-19 on Indian financial markets and stock returns is much severe in comparison to that of demonetization and the GST.

The local individual investors have witnessed a lot of volatility in the markets in the recent past. This study is an attempt to analyze the factors that affect their investment decisions in the present.

Objectives

The basic objective of the research is to study the effect of historical investor experience on their decision making and the various investment strategies:

- To determine the type of information considered relevant by the individual investors in primary and secondary markets.
- To find out the major sources of information regarding the future prospects of investment in various companies and their relative importance to investors with different levels of experience.
- To get a glimpse of the investor perspective towards different investment theories, when they invest in the equity markets.

Research Methodology

Research methodology is the specific procedures or techniques used to identify, select, process, and analyze information about the research topic.

In order to understand the investor's perspective, the survey method has been used to collect data from the respondents. A comprehensive structured questionnaire was designed on Google forms, with carefully chosen questions. Convenience and snowball sampling method of non-probabilistic sampling has been resorted to decide about the sample items to be included in the survey.

- **About the Participants**

A total of 120 respondents participated in the study from different parts of India. However, after the data cleansing process of deleting the duplicates and the irrelevant entries, 105 participants remained. These include 39 females and 66 males, from different walks of life, viz. businessmen (12%), professionals (10%), employees (58%), homemakers (3%) retired persons (2%) and students (15%).These can be classified on the basis of their experience in investing as in Table 1:

Table 1: The investment experience of the respondents as per their occupations

Occupation	< 2 years	2 to 5 years	> 5 years	Grand Total
Business	7	3	2	12
Homemaker	2	-	2	4
Insurance Professional	-	-	1	1
Profession (self-employed)	5	3	3	11
Retired	1	1	2	1
Service (Employment)	26	19	13	58
Student	12	2	1	15
Grand Total	**53**	**28**	**24**	**105**

- **Procedure for Data Collection**

A structured questionnaire was created, consisting of 13 questions related to the subject in two parts and circulated among the participants to collect their responses. The first part collected data regarding the demographical profiles of the participants, while the second part consisted of questions listing out various factors which are likely to affect the decision-making process of investors in different markets. All the participants extended their full co-operation while responding to the questionnaire. The data was analysed, processed and interpreted using MS Excel based on the frequency of the chosen responses to arrive at meaningful conclusions.

Data Analysis and Findings

Analysis of the collected data is the most crucial part of a research. The questions asked in the survey and the responses obtained have been observed and interpreted as follows:

Investor Awareness Campaigns

Various campaigns are organized by the Securities and Exchange Board of India (SEBI) that focus on educating the novice investor about the unscrupulous manipulators through regular guidance and awareness messages. These intend to alert the investors about the 'tips' received from unverified or dubious sources, that may cause them to lose their hard-earned money. In this study it was observed that 45% of the participants were not even aware of any investor awareness and education campaigns conducted by Government of India and SEBI. Thus, these campaigns did not impact their investment decisions.

Sources of Information

The respondents were asked about the number of years for which they have been investing, to evaluate the span of their experience. The people with less than two years of experience have been treated as new investors (50%), those with up to five years of experience have been considered to be in the learning process (27%) and people with more than five years of experience have been taken as investors with considerable experience of the rises and falls of the markets (23%).

Table 2: The number of respondents using different sources of information classified as per their span of experience

Sources for information/ Advice	Less Than 2 Years	For 2 To 5 Years	More Than 5 Years
Prospectus/ Abridged prospectus	13	18	12
Annual reports	45	25	29
Sub brokers/ consultants	19	29	13
Friends and colleagues	49	46	54
News channels	19	21	50
Financial newspapers and apps	51	43	75
Experienced investors	38	46	25

(Values in % of the total number of respondents in the respective category)

Based on Table 2, most investors take advice from friends and colleagues as the main source of information for investment decision making. At the same time, new investors include students and those in service and they have a higher reliance on financial newspapers and applications as a source of information. It is also observed that people up to 5 years of experience tend to look up to the more experienced investors for advice. The experienced investors believed in keeping up to date with news, and around 75% of them use financial newspapers and apps. A quite surprising observation of this study is that the inexperienced investors are more likely (45%) to go through the annual reports of a company before investing, than relatively more experienced investors.

Primary Market (IPOs)

Table 3: Criteria chosen by investors for application to IPOs, based on the span of experience

Criteria for investing in IPOs	Less than 2 years	For 2 to 5 years	More than 5 years	Grand Total	Preference out of total
Company's background and reputation of the promoter	36	21	18	75	71%
Viability or feasibility of the project	24	7	10	41	39%
Grey market/unofficial premium	8	10	9	27	26%
Risk factors	29	12	12	53	50%
Gestation period	23	7	8	38	36%
Anchor investors' participation	5	5	6	16	15%
Shares prices of similar companies	17	7	11	35	33%
Tax savings instruments	1	0	0	1	1%
Post issue promoters holding	3	4	6	13	12%
Profitability ratios	23	7	8	38	36%
Debt equity ratio etc	23	7	8	38	36%
Total Respondents	**53**	**28**	**24**	**105**	

Investing in the primary market in equity shares involves investing in Initial Public Offers (IPOs) and Follow-on Public Offers (FPOs) made by the companies to raise equity capital. According to the analysis, the most important factor influencing the investment decision making is the company's background and the reputation of the promoter. This includes studying the business of the company itself, as well as its group companies, if any, and their track record over the years. After that, among the most preferred measures were the feasibility of the project for which the money is being raised and the risk factors involved, keeping in mind the government policies and the social and economic environment in which the business operates. 36% of the respondents also relied on financial ratios analysis, by computing and comparing various profitability ratios (like Return on Investment) and solvency ratios (like Debt Equity ratio) with the company's past performance and with the ratios of other companies in the same industry. The criteria for investing in IPOs as reflected in the responses, remained unchanged irrespective of the experience span of the respondents.

Secondary Markets

Table 4: Yardsticks considered by investors for trading in secondary markets, based on the span of experience

Yardsticks for investment in secondary markets	Less than 2 years	For 2 to 5 years	More than 5 years	Grand Total	%
Company/management track record	25	17	15	57	54.3%
Cash flow or Fund flow analysis	19	9	6	34	32.4%
Corporate governance	12	6	9	27	25.7%
EPS or P/E Ratio	25	16	15	56	53.3%
Industry status and technology used	10	5	6	21	20.0%
Total Paid up capital	6	5	5	16	15.2%
Price to Book value ratio	3	2	4	9	8.6%
Dividend policies	17	9	8	34	32.4%
Other financial ratios	8	3	4	15	14.3%
Market share of products	23	13	7	43	41.0%
Highest or lowest share prices	10	8	11	29	27.6%
Share holding pattern	9	5	7	21	20.0%
Bonus issue record	10	5	3	18	17.1%
Total respondents	**53**	**28**	**24**	**105**	

Investing in secondary market (old issues market) involves buying and selling of already issued shares on a stock exchange. While making an analysis of the most common factors assessed by the investors in secondary markets, the top two factors that are evaluated by more than 50% of the participants are the 'track record of the Company and the management' and the 'EPS and Price-earnings ratio of the share'. This seems reasonable, considering it is important to understand the reputation and track record of the company and the management performance as well as the returns expected from the stock, before investing in it. Apart from these, the common measures the investors take into account are market share of the products of the business, the cash flows generated by them andthe dividend policies to understand the retention ratio and eventually the dividend expectancy. It was noted that the preferences reflected in the responses remained more or less unchanged irrespective of the investment experience span of the respondents.

Investor Perspective

Table 5: Investor's responses to common investment theories

Which of the following statements do you agree with?	Strongly agree	Agree	Can't say	Disagree	Strongly disagree
Higher the risk, higher the return	37	47	17	4	-
Higher the premium (price), better the issue	8	41	35	20	1
It's better not to put all your eggs in the same basket	71	22	7	4	1
Timing of purchase and sale is very important	55	46	4	-	-
Long term investors earn more than a speculator	44	35	23	3	-
One should 'average' down one's purchase price by making further purchases, if the market goes downwards after the purchase	23	50	26	3	3

(Total Respondents: 105)

The investors were asked how strongly they feel about these popular investment theories. About 80% of the respondents readily agreed to the most common notion in investing, "*Higher the risk, higher the return*", as it is also the prime reason why people invest in equity shares, which are also considered one of the riskiest investments. At the same time, the statement "*Higher the premium, better the issue*" didn't have as eager support as 47% of the people replied positively, but 20%of the people also disagreed with it. A good 33% of the respondents felt that a higher premium does not guarantee the better quality of the issue, and hence, chose not to comment on it. The statements like "*It's better not to put all your eggs in the same basket"* and "*Timing of purchase and sale is very important"*got instant agreement, with a very small proportion of respondents disagreeing with them. This is because they are the basics of fruitful investing and are important to lower the probability of incurring a loss and earn the maximum income, respectively. The results of the remaining two statements came back with some interesting insights. "*Long term investors earn more than a speculator"* and "*One should 'average' down one's purchase price by making further purchases, if the market goes downwards after the purchase"* had about 70-75% respondents in favour, but the remaining one fourth of the respondents were indecisive, considering sometimes, with a chance of luck and a careful study, even a speculator can earn a great deal through trading. Similarly, just because the prices of a stock are currently going down in the market, does not guarantee that they will ever rise again and investing more funds in the same stock even after you are losing money on the existing investment, could be liketrying to catch a falling knife.

Conclusion

The research intended to elicit the factors affecting the investment decisions in equity markets for individual investors. When the sources of information were analyzed, it was concluded that enough importance is not given to the annual reports of the companies, which contain the audit reports, directors' notes and the true position of the company. Instead, people look for shortcuts in the forms of analysis by friends and colleagues and financial newspapers and apps. These shortcuts are sometimes the reason why rumors spread in the financial markets

The yardsticks for investment in the new-issues markets were studied, going through the company's background and the risk factors turned out to be the most important factors. However, more importance may be given to the less common factors like post issue promoter's holding in the company and the anchor investors' participating, for ensuring more positive results as these reflect the confidence that the promotors or High Net-worth Individuals or institutions have in the company.

When analyzing the criteria for investing in secondary markets, it was inferred that there is no 'one measure' that almost everybody looks at, since quite a significant proportion of the funds are put in by the speculators. However, studying the management track record, the earnings per share and the market share of the products are some factors considered, to get a better understanding of the business of the company.

This research also evaluates the reach of the investor awareness programs of the government and concludes that they are not easily accessible to close to half of the population.

Different investors have different experiences in the stock markets and these experiences build up their confidence in various investment theories. Different theories were tested to record the reaction of the respondents, and two ideologies that were most pervasive are "*It's better not to put all your eggs in the same basket"* and "Timing *of purchase and sale is very important".*

Recommendations

The investor awareness programs in this country may be good, but they are only useful when they are accessible to the entire population. The individual investors need to understand that doing your own research about a company, through its technical and fundamental analysis, is more important than relying on the word of one's friends and colleagues, as this is how rumors spread in the share markets. Keeping an eye on the news related to the company and the industry is a good start, but a careful analysis of the annual reports and other disclosures is also crucial and must be encouraged.

Limitations

All possible efforts were made to conduct the research in an accurate and decent way. However, conducting a study in a perfect fashion seems next to impossible. Thus, some constraints and limitations crossed the path of this study. The scope of the research had to be contained given the paucity of time and resources. The sample size taken for data collection had to be limited in numbers and the sample items were selected based on convenience. Another major limitation was that the respondents were inclined to give 'ideal' or 'model information', rather than the actual information. They were focusing more on “what it should be” than “what it is”, which is likely to distort the data collected for the research. Finally, the research study as well as the paper assumes that the reader has the basic understanding of the financial terminology.

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