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Behavioral Finance and Traditional Finance role in investment decision making for individuals

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***Abstract* - This articles briefly explains the concepts of behavioral finance and traditional finance. Behavioral finance is always based on investors psychology and human attitude and behavior. In traditional finance investment decisions is based on mathematical calculations of the market and investors take a decision based on the available data in the market. Comparison of behavioral finance and traditional finance and which finance method is suitable for the investors to take a decision.**

***Index Terms* - Behavioral Finance, Psychology, Knowledgeable, Rational.**

INTRODUCTION

While making a decision it is very important for choosing the investment options for individuals or the investors. Investors main interest is to earn good returns for their investment. The decision is purely based on the market value and information available in the market on different alternatives. Thus, the investment occasionally gives undesirable results to the depositors for that purpose they financed or they are non-getting fulfilled results from their investment. "Buchan, (2001) stated that "Money is desire Embodied". Kahneman and Tversky, (1979) and Statman, (1999) stated that people feelings of pain when the investors discovered that other choice have good outcomes". So behavioral finance is the study that gives an explanation to the investors, who are interested in investments and how it affects from their emotions.

Behavioral investment tells us in what manner and where the investors emotions and awareness reflects their decisions and how the avenues depends on their decision on various pattern of investment where as traditional finance reveals that the investors and market are rational, investors gather all information from the market and they are knowledgeable while investing in various avenues therefore in traditional finance investors do not make decision on their emotion instead they take decision based on their knowledge.

OBJECTIVE OF THE STUDY

The objectives of this article are

1. To study on which concept is suitable to take decision while investing and how the behavior is reflecting on the investor's decisions.
2. To analyze the relationship between the traditional finance versus behavioral finance and its biases influences on the investment decision making process.

RESEARCH METHODOLOGY

This article is based on available secondary data of the few studies and the sources of information is from various journals, articles, various internet-based study materials and books etc. were referred as to understand the concepts of behavioral finance and traditional finance.

LITERATURE REVIEW

Sujatha Kapoor and Jaya M Prasad study revealed that the advances in behavioral finance done through the development of financial history and the role of behavioral finance is based on emotion and psyche of investors. It offers the suggestions of behavioral factors reported by many researchers in the stock markets. Whereas comparing with traditional finance followed through traditional theory analysis were constructed to calculate the financial decisions and, in those circumstances, where they are deemed unsatisfactory.

Jay R. Ritter explain in his behavior finance study, how people think about investment using their emotions. According to him finance includes two

building blocks i.e., cognitive psychology and the limits to arbitrage. In cognitive biases people will take decision based on their abilities and in limits to arbitrage when market will be inefficient to make decisions.

Shagun Bakshi explained in his article that financial market information is shifted from traditional finance to behavioral finance. Previous the financial market was clearly focus based on some of the model and it shown that, investors rationality. But now a days it is based on some of the global as well individual factors such as individual perception, behavior and their reflections. He also highlighted how the traditional finance theories are differ to behavioral finance theories and the importance of behavioral finance.

Dr. Vinay Kandapal and Mr. Rajat Mehrotra both are analyzed the behavior of investors on investment pattern and examined the determinants of an investors and considering their financial decisions. They conducted survey in Dehradun, India to know about the savings and investment pattern of investors and give suitable suggestion to the investors and for the study adopted many analytical tools to find out the behavior of investors. Finally, both concluded that behavior of investors means a lot in the investment decisions and investors has to choose particular investment options while making decisions.

Muhammad Zulqarnain Asab, et al., examined individual investment preferences and discussion are the different factors that relates to investment decision and he analyzed about the comparison of behavioral finance and traditional finance and how these factors are influencing on investors financial decisions.

Egidijus Bikas, et al., analyzed in their study of behavioral finance and emergence and developmental trends, the financial markets are influenced by many factors and these factors may takes place for the country's developments. The factors may influence the decision-making process.

In the study of Rupinder Kaur Gill and Rubeena Bajwa, behavioral finance is like and open-minded study and it includes psychology, sociology and finance. In his study, the behavioral finance describes in two categories like micro and macro. In each category investors having different significance based on that they can take the financial decisions.

Nik Maheran and Nik Muhammad conducted study based on investors psychology and its affects to investors decision making process. This article provides a overview of behavioral finance and how the psychological biases are affected the investor behavior and prices.

BEHAVIORAL FINANCE OVERVIEW

Behavioral finance is a psychological concept, it explains that investors are irrationals, and investors emotions and biases play a role in making investment decisions. In behavioral finance, investors might take their decisions on fear, overconfidence, gut feeling, what others can do, thereby following the gang and past experiences.

In behavioral Finance we use experiments and research to demonstrate something that most of the people would have little problem agreeing with. Humans are always irrational and their decisions are incorrect. So, it also known as Behavioral Economics. In many cases behavioral Finance is classified in to two categories

1. Micro Behavioral Finance
2. Macro behavioral Finance

- Micro Behavioral Finance: In this branch behavioral Finance deals with the behavior of individual investors and in this concept, we compare irrational to rational investors, this will also know as Homo Economist or rational economic individual.
- Macro behavioral Finance: In this branch behavioral finance deals with limitations of the efficient market hypothesis. Efficient market hypothesis is one of the models in conventional finance that helps us understand the trend of financial markets.

WHY BEHAVIORAL FINANCE IS IMPORTANT TO STUDY?

The philosophy value of investing is based on the perceptions of behavioral finance. Investing values adopts that in the short run, markets are not effective to take decisions. Peoples fear are not to take rational conclusions. If a person gives consideration to behavioral finance, he may recognize this cause. Behavioral finance supports to the people, who deteriorating into common psychological traps. Instead, it supports the investors to take advantage of the overestimations and under valuations it may

happen in the market because a huge amount of investors make decisions emotionally.
At the end behavioral finance is to assist the investors to buy or sell decisions based on existing data and information in the market. This way, they can assume the investors who wait for the market as a whole to identify this error.

TRADITIONAL FINANCE OVERVIEW

Traditional Finance is one of the pillars in financial thought that the investors believe in. In Traditional Finance the people and market are rational. The investors can get huge data, knowledge and information from the market. So, they will take their own financial decision based on their knowledge not on the emotions.
Traditional finance states that market is efficient and it might represent actual value of financial market. This statement tells that investor have self-control rather than social issues. The traditional finance investment decision is based on mathematical calculations, economic models and market behaviors and various available data. So, in traditional finance investors are thinks practically in terms of the investment risk, returns and problems involved in various avenues etc. This exactly tells that investor take the decision based on the available statistical and empirical data rather than emotions.

COMPARISON OF TRADITIONAL AND BEHAVIORAL FINANCE

Traditional finance is the finance which is moving from long period so it also called as 'conventional finance' or 'standard finance' or 'modern finance'. In traditional finance investors know the risk and uncertainty for their investment and it is not influenced by personal feeling so it is based on the facts and figures of market values. So, they will not take any risk based on their emotions, always it depends on the availability of data in the market. Simply states that in traditional finance investors are not diverted from their emotions while making financial decisions rather than they will go with facts and figures because they have perfect information's, so they are rational in nature and unbiased.
In behavioral finance, the term behaviors indicates that person's attitude/psychology/ actions etc. So, it is one of the psychological studies of individual investors while investing or making financial decisions. Investors draw a real-world experience because they are having their own biases and they are very irrational; their emotions are playing major role while investing in particular investment. In behavioral finance, market is volatile so it leads to fluctuations of share prices and investors are not had self-control and anomalies, so the investors, has to realize that rational financial decisions can be made but shouldn't invest based on their emotions they can go through the market analysis before investing in particular avenues.

CONCLUSION

The study shown the concepts of behavioral finance and traditional finance impression of investors financial decision on investment. In behavioral finance investors need to realize that rational financial decisions are often made, but they shouldn't take any financial decisions based on their emotions. In traditional finance investors get information and based on that they invest in different avenues. This type of behavioral finance and traditional finance decisions on big scale and it can cause disturbance in market anomalies.

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