ORIGINAL RESEARCH PAPER

Management

DO INVESTORS REALLY REGRET?

KEY WORDS:

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ABSTRACT

"There are only a few people who claim to have no regrets in life and finances". Retail investors are no exception. Investment is a natural process wherein, an individual wants every rupee to earn even more rupees. Eventually, investors get too excited at times about returns and certainly land up in regret zone. Though, behavioral finance has emerged as interdisciplinary, complimentary science to explain stock market phenomenon and regret analysis is one thrust area where much research is sporadic, especially in India. To explore the likelihood of regret and its impact on retail investor behavior in portfolio investments, the present study is conducted. Unfolding the regrets of retail investors while lack of adequate knowledge about portfolio management and peer effect as major reasons for such regrets. However, investors did exhibit regrets in big way as they perceive the stock market to be volatile and risky. Further, there are is wide scope for more studies viz., analysis of variance in regrets among different groups of investors and studies against different demographic factors etc.,

INTRODUCTION

Economic man is very unlike a real man (Edwards, 1954). The decision making process and factors influencing it have a drastic effect on the decision outcomes. Specifically in the investment decisions, there are two significant reasons, why investors do not behave, as we expect them to viz., Improper or substandard financial management would have a direct impact on investor well-being and also investor behavior likely affects the events in the stock markets.

The theory of rational investors has been opposed by neo-classical economic theory which opposes that every investor has limited access to information and an individual is bounded by external constraints as well as one's own behavioral aspects(Somil,2007). Hence, the decision making process is not a strictly rational one, where all relevant information is collected and objectively evaluated, rather, the decision maker makes mental shortcuts in the process(Tversky and kahneman (1974).

The behavioral finance asserted that investor market behavior derives from psychological principles of decision making to explain- why people buy or sell the stock (Al-Tamimi, 2005).

Behavioral Finance Defined....

Behavioral finance is the study of the influence of psychology on the behavior of financial practitioners and the subsequent effect on markets (Sewell, 2005).

Why is behavioral finance necessary?

For a while, theoretical and empirical evidence suggested that CAPM, EMH and other rational financial theories did a respectable job of predicting and explaining certain events. However, as time went on, academics in both finance and economics started to find anomalies and behaviors that couldn't be explained by theories available at the time. While these theories could explain certain "idealized" events, the real world proved to be a very messy place in which market participants often behaved very unpredictably.

Homo Economicus

One of the most rudimentary assumptions that conventional economics and finance makes is that people are rational "wealth maximizers" who seek to increase their own well-being. According to conventional economics, emotions and other extraneous factors do not influence people when it comes to making economic choices.

The anomalies prompted academics to look to cognitive psychology to account for the irrational and illogical behaviors that modern finance had failed to explain. Behavioral finance seeks to explain our actions, whereas modern finance seeks to explain the actions of the "economic man" (*Homo economicus*).

CONCEPTS OF REGRET THEORY

What is "Regret"?

Regret is the negative emotion experienced when learning that an alternative course of action would have resulted in a more favorable outcome.

DEFINITION of 'Regret Theory'

The theory of **regret aversion** or **anticipated regret** proposes that when facing a decision, individuals may anticipate the possibility of feeling regret after the uncertainty is resolved and thus incorporate in their choice their desire to eliminate or reduce this possibility.

Regret theory models choice under uncertainty taking into account the effect of anticipated regret. It was originally developed simultaneously by Graham Loomes and Robert Sugden David E. Bell and Peter C. Fishburn and subsequently improved upon by several other authors.

In general, these models incorporate a regret term to the utility function that depends negatively on the realized outcome and positively on the best alternative outcome given the uncertainty resolution.

Herd Behavior

There are a couple of reasons why herd behavior happens. The first is the social pressure of conformity. This is because most people are very sociable and have a natural desire to be accepted by a group, rather than be branded as an outcast. Therefore, following the group is an ideal way of becoming a member.

The second reason is the common rationale that it's unlikely that such a large group could be wrong. After all, even if you are convinced that a particular idea or course or action is irrational or incorrect, you might still follow the herd, believing they know something that you don't.

RESEARCH METHODOLOGY

Objectives of the Study:

- To find out the existence of regret behavior among retail investors

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- To identify factors for regrets in investments.
- To check whether regret behavior leads to herding or not.

Methodology

For the present study, investors of only Tirupati urban area in Chittoor district are considered. Sample size considered for the study is 80, effectively only 72 samples were found complete and satisfying. Sampling is done using convenience sampling technique.

ANALYSIS

Demographic Analysis of the respondents -Age of the Respondents

S.No.	Age(years)	No. of Respondents	Percentage (%)
1	20-30	9	12.5
2	31-40	24	33
3	41-50	13	18
4	Above 50	26	36
	Total	72	100

From the above table it can be inferred that, 54% of the respondents are above the age of 40 years; and nearly 46% of them are below 40 years.

Qualification of the respondents

S.No.	Qualification	No.of Respondents	Percentage (%)
1	Graduation	32	44.44
2	Post Graduation	16	22.22
3	Other	22	30.55
	Total	72	100

From, the above table it can be inferred that, nearly 45% of the respondents are graduates approximately 22% are post graduates. Notably, there are almost 30% of respondents who fall under others category (viz., matriculation, diploma etc.,)

Investment Preferences:

S.No.	Price Range	No.of Respondents	Percentage (%)
1	High Cap	21	29.16
2	Mid Cap	34	47.22
3	Low Cap	17	23.61
	Total	72	100

This table shows that around 47% of the respondents are mid-cap investors.

Regret Aversion occurs as a desire to avoid the pain of regret arising from poor investment decisions. As a result, investors usually end up taking sub-optimal investment decisions and holding losers in the markets. The respondents opinion on loss experience was close to 50 % agreed that losses are common but can be avoided one can be vigilant. Respondents were inquired about emotional response after a fall in share price, 59% of them felt bad about it. Whereas nearly 58% of them opined that they would feel regret while trading. A composite analysis of the bias is done from the answers.

Contingency Table: Fear of Regret Bias

		Fear of Regret			
Investor Type		Yes	May be	No	Total
Young Investors	Count	14	10	3	27
	% within investor type	51.85	37.03	11.11	100
Aged Investors	Count	5	37	3	45
	% within investor type	11.11	82.22	6.67	100
Total	Count	19	47	6	72
	% within investor type	26.38	65.28	8.33	100

Source: Computed Data

It can be observed that close to 27 % of the investors seem to confirm the bias, while 65 % considered themselves to be possible subjects to regret.

Weighted Scoring

A mean score higher than the reference score, is in indication of more susceptibility to regret bias. From the table below it can be inferred that young investors are more likely to show regressive behavior in a statistically significant way.

Weighted Scoring: Fear of Regret

Investor Type	Weighted Score	Mean	Reference Score	Outcome
Young	103	17.01	15.6	Fear of Regret
Aged	89	14.83	15.6	No Bias
Total	192	15.92	15.3	Fear of Regret

Source: Computed Data

Hypothesis Testing:

Chi-Square test was performed to verify whether the different mean scores for the investor types presented any statistical significance. Following hypothesis was tested –

H0: Both investor types are equally likely to exhibit Regret Aversion

H1: Young investors are more likely to exhibit the Regret Aversion

Chi-Squared Test: Fear of Regret Bias

	Value	Df	Asymp.Sig (2-sided)
Pearsons Chi-Square	4.044a	2	0.132
Likelihood Ratio	4.155	2	0.116
Linear-by-Linear Association	3.864	1	0.047
No.of Valid Cases	72		

Source: Computed Data

0 cells have expected count less than 5. The minimum expected count is 6.00

The high p-values in the above table suggest that the null hypothesis could not be rejected, and thus it could not be statistically confirmed that young investors were more susceptible to regret aversion compared to experienced investors.

Regret Aversion usually leads investors to fall towards herding behavior, hence it is generally found that regret aversion and herding are close related to each other. Hence, a check for correlation analysis was done for the response score of questions exploring regret aversion with that of question like - following others while investing is better than risking alone.

Opinion about following others while investing is better than risking alone

S.No.	Opinion	No. of Respondents	Percentage (%)
1	Strongly Disagree	3	4.17
2	Disagree	2	2.78
3	Neutral	21	29.17
4	Agree	42	58.33
5	Strongly Agree	4	5.55
	Total	72	100

Source: Primary Data

In order to test the relationship between the regret aversion and herding the chi-sqaured test for independence was performed for the following hypotheses:

H0: There is no relationship between regret aversion behavior and herding

H1: There is some relationship between regret aversion behavior and herding

Hypothesis testing for relationship between Regret Aversion and Herding

Chi-Squared Test was done to verify the causal relationship -

	Value	**Df**	**Asymp. Sig(2-sided)**
Pearsons Chi-Square	4.118	3	0.239
Likelihood Ratio	4.281	3	0.221
Linear-by-Linear Association	3.772	1	0.052
No.of Valid Cases	52		

Source: Computed Data

The p-values from the Pearson Chi-square and Likelihood ratio tests were 0.239 and 0.221. This indicates that the null hypothesis could not be rejected in the 95% confidence interval, providing convincing statistical evidence to conclude that regret aversion and herding are interrelated biases.

DISCUSSION AND CONCLUSION

Regret Aversion is a bias that is invariably found in investors; however younger investors are more susceptible to this bias. Empirical evidence of this study shows that investors are either experiencing regret aversion or lurking in the dilemma whether it is regret or not. The brokerage firms and investment advisors need to be conscious about the fact that investors may take sub-optimal decisions or they may not heed to the advice owing to regret averse behavior. The study provides evidence that regret aversion and herding are related and investors might become more likely to follow the herd rather than take calculated risks to optimize their portfolio returns. A comprehensive study can be conducted to explore the relationships among various biases and specifically with regret aversion bias.

Further, there are is wide scope for more studies viz., analysis of variance in regrets among different groups of investors and studies against different demographic factors etc.,

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