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AN EMPIRICAL ANALYSIS OF HERDING BEHAVIOUR ON INVESTMENT DECISIONS OF INDIVIDUAL INVESTORS

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Abstract
Behavioural Finance has been developed because of the inadequacies of the traditional finance theory to anticipate and study the behaviour of individuals. Various ideas, hypotheses and thoughts have been added to the behavioural finance literature over the long haul. Herding Behavior is one of such ideas which are of much significance in the study of investment behaviour of individuals. Herding denotes how individuals act together in a group without any centralized direction. Herding is generally considered as it drives assets price from the basic value and there are concerns it prompts unpredictability, weakens the market, and expands the fragility of the financial market. Do stock market investors act/react to accurate information or noise? Do they trust their own information or do they simply follow the herd? The goal of the study is to look into these common research questions from the standpoint of behavioural finance. This study intended to distinguish the reasons for herding behavior by an individual investor and recognize the potential impacts of the herding behavior of investors on the stock market. The study uncovered that financial investor in India tend to follow the conduct of others while making investments in stock markets to keep away from misfortunes and regrets. This is because there are very few financially literate and is not very much aware with regards to financial exchange working. Thus, they for the most part go with the choices made by market pioneers to procure safe returns out of their investments.

Keywords: Herding, Behavioural, Behavioural Bias, Financially Literate.

Introduction

Numerous exemplary economic and financial theories are predicated on the reason that individuals settle on rational decisions based on all accessible data, and that markets are proficient, i.e. everyone can approach to all accessible data available in the market and investors make rational decisions without getting affected by the mental attributes. Behavioural finance challenges these suppositions and inspect at how individuals and markets really work. It is the study of how psychology affects the behaviour or conduct of investors and financial analysts. It additionally considers the market's response. It also highlights how investors are not generally judicious, have discretion restrictions, and are affected by their own inclinations. Understanding the irrational behaviour merits more significance than it has ever had at any point. The present investment decisions request a superior comprehension of individual investors' social inclinations. The investigation of Behavioural Finance shows how intellectual and passionate variables affect the investment decision of an investment and especially how they influence the rationality in decision making.

The "typical investor" as talked about in the different hypotheses of behavioural finance is really a rational investor who is self-prejudices and needs material information. The venture choice of a retail financial investor is impacted by countless material and unimportant data which eventually arise and develops his investment behaviour. Behavioural Finance is one of the arising and critical themes for us to know the contemplations and mindset of individuals regarding what they think prior to settling on any investment decisions.

Behavioural finance adds to better decision-production by exploring how different intellectual cycles and enthusiastic elements might obstruct or add to ideal decision making in finance. Quite a bit of economic and financial hypothesis is based on the idea that people act judiciously and consider all accessible data in the decision-making process. However, analysts have uncovered a shockingly enormous measure of proof that this is as often as possible is not the situation. Loads of instances of unreasonable conduct and rehashed blunders in judgment have been archived in scholarly investigations. According to the standards of behavioural finance human choices are dependent upon a few intellectual and passionate deceptions. Such deceptions are classified into various ideas like loss aversion, cognitive dissonance, overconfidence, mental accounting etc. One of such deceptions or indeed properly considered as a significant standard of behavioural finance is the herd behaviour.

There is a word in investor behaviour i.e. herding; which implies the conduct shown by investors by following the investment decisions of other investors putting their resources in stock market can cause colossal, unfamiliar troops or cashing based on clearly small elementary proof to rationalize either. Herding is the critical ground of deception in finance. Herding impact in financial market is perceived as the penchant of investors to emulate the activities of others. In herding behaviour the investment decisions shown by investors are dependent on others decisions, which brings in disappointment about returns on investment.

Experts by and large cautiously think about the presence of herding, because of the actuality that investors relies upon bunch information rather than on the information gathered by them which causes value deviation of securities from essential worth; subsequently, numerous great opportunities for investment at the the current time can be affected.

Herd Behaviour is the proclivity of an individual to follow the moves (objective or nonsensical) of a huge gathering. The herd mind is the result of two causes; initially, there might be a prevailing burden of congruity. Generally, individuals would rather not move out of the group they belong to. Also, there is a typical rationale that a huge gathering can't commit errors. Buying stocks based on price momentum while disregarding fundamental financial standards of market interest is referred to as herd behaviour and it leads to faculty decision. It is a counter to not having abundant information and accepting that others around us can really give us an option in contrast to the manner in which decisions are made. Studies have presumed that people find, conflicting with huge number of individuals is exceptionally hard, and this is the reason that they by and large hide their own viewpoint.

Herding in financial markets can be defined as mutual imitation leading to a convergence of action (Hirshleifer and Teoh, 2003). This is the most well-known misstep where financial investor tends to follow the investment choices taken by the majority or group of people. The principle justification for this is pressure from or influence by peers. The Reliance Power IPO, 2008 is an illustration of an occasion where numerous financial investors subscribed in without having full information on the issue. Investors apply to group conduct since they are worried of what others think about their investment choices.

Herd mentality bias is a term used in behavioral finance to depict a financial investor’s inclination to follow and duplicate what different financial investors are doing. Rather than their own free anaylsis, they are mainly affected by emotion and instinct.

Herding might be characterized as emulating the activities of others in a group. In general form, herding can be defined as how individuals take decisions together in a group without any centralized direction. Herding is one of the significant behavioural biases influencing investor choices. Herding as a behavioural bias acquired its popularity after being the significant reason for the blasting of dotcom bubble in late 1990. The investors and private financial backers put enormous amount into web organizations pursuing the direction without guaranteeing its monetary soundness. Afterward, in 2008 again herding was inferable from the blasting of Real Estate Bubble. As of now the pundits of the cryptocurrency boom in ongoing years recommend that a comparative peculiarity might be occurring in that space.

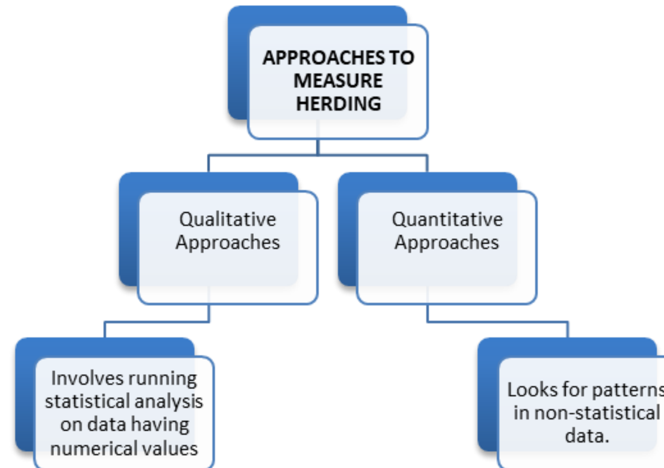
The beginning of herding ages back in 1936 when J.M. Keynes created eminent "General Theory". According to this hypothesis, the long-term investors basically follow the market to ensure sound investment and expert directors’ group with the goal that their reputation isn't hurt because of d contradictory behaviour. Later herding was characterized as "under particular conditions, administrators essentially copy the investment decisions of different managers, overlooking considerable private information". Herding is significant and intriguing for research for its connection and effect on the stockprices. At the point when financial decisions to put resources into a particular stock unite, the ensuing impact is an augmented demand. The fundamental-driven herding is ordinarily useful and assists with deciding the prices, though imitation-driven herding is typically useless and can prompt value turnarounds and an excessive amount of instability. Herding is significant and is all around recognized by the scholastic specialists; as it influences the stock prices which influence the traits of risk and return models and at last influences the asset pricing theories.

Herding can be arranged under two heads: rational herding and non-rational herding. These two ideas depict the beginning of herd behaviour. The rational concept can be portrayed as financial investors accepting other financial investors' investment decisions to secure their own advantages and improving their reputations among other financial investors.

The non-rational concepts centers on financial investor psychology which shows the role of specialists as lemmings, indiscriminately following others and overlooking the rational reasoning. The irrational herding happens when financial investors with deficient data and lacking risk evaluation disregard their past convictions and aimlessly mimic other financial investors activity. The irrational herding can be depicted as investors indiscriminately replicating others decisions, notwithstanding having their own information. The non-rational perspective of herd behaviour centers on investor psychology and expects that financial investor act like imitators, disregarding all rational analysis and following others aimlessly.

Approaches to Measure Herding

Various methodologies have been formulated to measure the herding behaviour. These methodologies can be classified into quantitative approaches.



Literature Review
Numerous studies have been made in the past on Herding Behaviour and Behavioural Finance.

A review of some important research works have been outlined below

1. Research titled **Role of Herding Behaviour in Influencing Investor Decision Making in India** by ***Dheeraj Agrawal*** and ***Tanvi Singhal*** studied how herding behaviour impact the investors decision in stock market. In this paper the researchers have also studied the relationship between different variables related with herding behavior of an individual investor. They analyzed that herding behavior is positively related with stock market performance. They suggested that before making any investment decisions, investors should search for the information which will impact there decision.
2. Research titled **Role of Herding Behaviour in Influencing Investor Decision Making in India** by ***Dheeraj Agrawal*** and ***Tanvi Singhal*** studied how herding behaviour impact the investors decision in stock market. In this paper the researchers have also studied the relationship between different variables related with herding behavior of an individual investor. They analyzed that herding behavior is positively related with stock market performance. They suggested that before making any investment decisions, investors should search for the information which will impact there decision.
3. ***Nizar Raissi*** and ***Sahbi Missaoui*** found in their work, **Role of investor sentiment in financial markets: an explanation by behavioural finance approach,** that behavioural finance is the substitute for the classical approach. The investor's emotions are completely psychological in nature. It was established that emotion is a significant factor in stock returns. Returns are higher if the investor's mindset is positive.
4. A study on **an empirical analysis of influential factors on investment behaviour of retail investors' in indian stock market: a behavioural perspective** by ***E.Vijaya*** examines the various behavioural factors that influence the investment decisions of the investors. According to his analysis he concluded that among all 5 behavioural factors variable Overconfidence has high impact on retail investors' investment decision in Indian stock market and other variable factors have moderate impact.
5. **Gulnur Muradoglu** and **Nigel Harvey** in **Behavioural finance: the role of psychological factors in financial decisions** describes how psychological variables play a key part in financial decision-making.

6. Another study by **Etse Nkukpornu, Prince Gyimah, & Linda Sakyiwaa** on **Behavioural Finance and Investment Decisions: Does Behavioral Bias Matter?** examines in a developing country, the relationship between behavioural bias and investment decisions. The researchers came to the conclusion that the presence of behavioural biases has a significant impact on investment decisions. The study discovered a number of connections between various biases and investor decision-making**.**

Objectives

- The aim of this paper is to study how herding behaviour influence the investment decisions of the individual investors.
- To discuss detail about herding behaviour as one of the variable of behavioural bias.

Research Methodology

The study is mainly conceptual and descriptive in nature Secondary data was collected through literature review, reports, articles, and websites.

Reasons of Herding Behavior

The researcher investigated why investors in India were behaving in herding manner.

- **Dread of Losing Money:** Indian investors are terrified of losing money by making their independent decisions on stock market investments. They believe that if they make an investing decision based on their own experience, they will be more likely to lose money in the stock market due to more volatility.
- **Diversification of Risk:** Indian investors believe that if a large number of people invest their money in a single security, the risk associated with that security will diversify. When a large number of investors invest in a specific stock, the price of that stock rises, yet this behaviour frequently overvalues the price of that asset in the market.
- **Historical Performance:** Indian investors' herding behaviour is influenced by the stock's and decision makers' past performance. Indian investors correlate market leaders' judgments with their own past decisions, and as a result, they begin to exhibit similar behaviour in order to protect their investments and lessen the risk connected with the stock market.
- **Market Image:** Investors in India frequently engage in herding behaviour because the individual or group of people they are following has a positive market image. As a result, the investors believe that they are extremely skilled in making financial decisions, and that their investments will be safe as well.
- **Lack of Financial Literacy:** Financial literacy is a problem for the majority of Indian investors. They have no idea where to put their money to receive the optimum returns. They are also unaware of the various investing possibilities open to them. This is the primary reason, as individuals tend to follow the decisions of a group of people or financial experts.

Impacts of herding

Herding is an endogenous financial instability tool that raises the financial system's volatility and amplitude. When noise traders enter the market, asset prices become extraordinarily volatile, and this volatility cannot be explained just by changes in fundamental values. It has been demonstrated that news about weather, future dividends, and discount rates do not account for a significant portion of price movement. When a high proportion of investors devotes a consistent amount of their money to stocks, even a tiny number of noise traders can have a significant impact on prices. As a result, as the

percentage of sophisticated and noise traders' declines, the impact of noise grows. Volatility was also found to be higher in transparent markets, i.e. marketplaces where traders can see the prices and previous activities of other market players, than in opaque markets. Volatility has a negative relationship with trade size and an opposite relationship with volume transacted. When compared to uneducated traders, it is argued that informed traders trade in bigger volumes. As a result, the lower the number of informed traders, the lower the volatility, and the bigger the number of uninformed traders, the higher the volatility.

As a result, several studies claim that ignorant trading increases volatility, while others claim that volatility is directly and positively associated to herding.

Conclusion

In this study we found that people behave in herding manner due to lack of financial literacy. In India, mostly people don't have knowledge about financial markets, so as an investor, it is very hard to make an investment decision where one can get ideal returns. Due to lack of knowledge, people in India generally follow the decisions made by the most of individuals or market pioneers while making investment decisions. It's not only lack of knowledge but sometimes even people having financial market knowledge are unable to trust their own decisions in the fear of losing their money. This is the reason that they follow either market leaders or group of people who have well past financial records. It is seen that when investors show herding behavior, they by and large don't make rational decisions and cause an abrupt variance in stock price of a security. These kinds of unexpected changes in stock prices generally don't match the financial performance of an organization. In this way, after some time, it might prompt to losses also. Subsequently, it is recommended that while making investment decisions, investors should look for information based on adequate information. They should make a decision by taking into consideration the movement of market pioneers as a whole.

Suggestions

It was feasible to comprehend many reasons that cause investors to exhibit herding behaviour as a result of this research. With the help of this research, judgments may be made about the causes of this behaviour and how to address them. When decision-makers understand the reasons, they may take action to improve the stock market's performance, and individuals can make their own investment decisions rather than relying on others. Certain investor education programmes can be created to educate investors in order to lessen the influence of herding behaviour. Investors' ability to make their own decisions leads to financial independence and increases their confidence. There is need to educate the investors to such level that they can take up their own decisions without any hesitation or if they are following some market leaders or any group of people than they must be able to analyst their suggestion for a better decision.

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