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A study on Risk bearing capacity and Investment Attitude of Experienced and Common Investors

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Abstract

This paper aims at studying the impact of investment experience on risk bearing capacity and investment attitude of individual investors. It also explores the relationship between both the dependent variables. In this study data has been collected from 271 investors having various years of investment experience. The result of the study shows that risk bearing capacity increases with investment experience. It also concludes that investment attitude of investors move to optimism from pessimism with increase in investment experience. The findings also show a significant association between risk bearing capacity and investment attitude.

Keywords: Investment experience, Risk bearing capacity, Investment Attitude, Investment behavior.

INTRODUCTION

Finance concept has been in a process of rapid development during the last century. The models and techniques covered by the traditional finance assist individuals in their preferences and each individual is expected to make preferences as a standard.

If all investors take standard decisions then there will be perfect financial market with no uncertainty or risk, since all investments are already standard. But in reality extreme volatility has plagued financial markets worldwide.

Investors' sentiments are the key determinants of market movements also these sentiments vary with respect to the experience of investors. In this context, it becomes important to study the impact of investment experience and the role played by emotions like fear, greed and anticipation, which further result in various investment attributes. This study is to find the influence of investment experience on two such investment attributes - risk bearing capacity and investment attitude.

Literature review:

Literature review is divided in two parts, 1. Risk and Return, 2. Attitude of investors.

1. Risk and Return: Quantitative and qualitative research carried out in the past indicates that attitudes to investment risk depend on factors such as personality, circumstances, educational attainment, level of financial knowledge and experience of investment, and extent of financial product portfolio (Conquest Research Limited, 2004; Distribution Technology, 2005). Quantitative research carried out in the US identifies a similar range of factors, including income, wealth, age, marital status, gender and level of education (experience) (Finke and Huston, 2003). In general, it has been observed that the young or common investors have different risk bearing capacity than the experienced, wealthier individuals manifest a greater willingness to invest in equities on the other hand poor are risk averse (Clark and Strauss, 2008). One US survey (of faculty and staff studied at an outsized university) found that a mix of education, financial knowledge, income and occupation explained the foremost between-group variability in risk tolerance. Even so, this

model only explained about 22% of an individual's financial risk tolerance, suggesting that other factors might differentiate levels of risk tolerance more effectively, such as attitudinal or psychological factors (Grable, 2000). Attitudes to risk change over time as needs alter and people's capacity to afford to lose varies (Conquest Research Limited, 2004). The evidence indicates fairly clearly that willingness to bear financial risk decreases significantly among individuals who are retired or nearing retirement (Distribution Technology, 2005; Finke and Huston, 2003). In addition, work administered within the UK on the measurement of investors' risk appetite (which depends on their attitude to risk) suggests that it fluctuates within a comparatively narrow gauge during 'normal' times, but falls sharply during crises (Gai and Vause, 2005). On the whole, UK consumers have been found to be risk averse - particularly non-savers and those on low incomes (Atkinson et al., 2006; Hall et al., 2006; Distribution Technology, 2005; Conquest Research Limited, 2004).

2. Attitude of investors: Behavioural Finance experts have to use a range of concepts while understanding investors and markets. One among such concept is "Attitude" of investor. Behavioral investors consider building portfolios as pyramids of assets, layer by layer. The layers are related to particular goals and particular attitudes toward risk. Behavioral portfolio theory answers some portfolio questions and asks others (Hoje Jo 2008). Selden (1912) in his research article "Psychology of Stock Market" mentioned that once the investor develops positive attitude towards investment, he remains committed towards it, despite of resistance from any internal or external forces. Further, Weinstein, N. (1980) added that individuals who are having positive attitude would really like to prove those that are injecting negativity wrong. As a result, positive attitude actually makes him able to face challenges which the stock exchange will pose because of its fluctuations. Wurgler, J. and K. Zhuravskaya. (2002) have made a similar observation. They stated that, people those that invest on stock exchange won't earn profits each time. Those who are not having positive attitude are not able to be patient even when there is a minor correction in stock markets. They immediately liquidate their holdings. On the other hand, investors who are having positive attitude towards their investment decision are making use of any correction by investing some more amounts by capturing whenever the prices are falling and are able to earn additional profit.

Reviewing related literature the dependent variables in the given study were resorted to risk bearing capacity and Investment attitude of investors, whereas investors' experience is independent variable.

Investment Experience: To understand the effect of experience on investment attributes the investors are classified in two categories – Experienced investors, having more than 5 years investment experience and Common investors, having less than 5 years investment experience.

Both experienced and common investors have different approach towards the same exposure i.e. behavioral pattern of experienced and common investors differs.

Risk bearing capacity: It is the risk taking Behaviour of individual. It is the extent to which a person is willing to take a chance. On the basis of this investors are classified into conservative, moderately conservative, moderate, moderately aggressive, Aggressive. The components of risk bearing capacity considered in this study are: Investment Choice, Investment Volume, Investment Tenure, Investment Frequency, Willingness to use borrowed funds for long-term investments, Willingness to use borrowed for short- term investments and Willingness to gamble or participate in game shows.

Attitude towards Investment: Investment and savings attitudes and behavior are influenced by the structure, complexity, transparency and perceived past and future performance of different kinds of investment options. Attitude, in this is study is composed of eight components - Essentiality of financial planning concept, Regular update evaluation and revision of portfolio, Learning new things about investment, Sense of Responsibility for the investment process, Perception about performance of financial market, Coping with stress caused by investment, Trusting of Financial Advisors and Fee payments to Financial Advisors over and above commission, Attitude towards the financial informational contents.

Objectives of Research:

- To analyse relationship between experience of investors and their risk bearing capacity.
- To analyse relationship between experience of investors and their attitude towards investments.
- To analyse relationship between attitude towards investment and risk bearing capacity.

Research Hypotheses: In the wake of this information, researcher wanted to test the following hypotheses

1. Experience of investors and Risk bearing capacity

H0. Investment experience and risk bearing capacity of investors are independent

H1. Investment experience and risk bearing capacity of investors are dependent

2. Experience of investors and attitude towards investment

H0. Investment experience and attitude of investment are independent

H2. Investment experience and attitude of investment are dependent

3. Risk Bearing capacity and attitude towards investment.

H0: There is no association between Risk Bearing capacity and attitude towards investment

H3: An association between Risk Bearing capacity and attitude towards investment exists.

Methodology:

To test the above mentioned hypotheses, primary data was collected from a sample of 338 financial investors.

Out of the total 338 responses 67 of them had to be rejected because of Failure to respond to all items in the scales and Failure to answer all items of the questionnaire data sheet. Finally, after the elimination of 67 responses, the sample size for the study was reduced to 271.

The sample was chosen randomly from financial investors related to broking firms in Uttar Pradesh. Random sample is selected out of population with no bias. The study uses a survey research method, using questionnaire with questions on risk bearing capacity and attitude towards investment. The risk taking capacity in this study is measured using set of 7 questions responses of which converted into five point likert scale later.

Analysis and results:

Descriptive statistics:

The demographic profile of the respondents is depicted in Table 1.

Investors are divided into two parts common investors and experienced investors. Common investors are those who have less than 5 years of investing add investors having investment experience of more than five years are considered experienced investors.

Table 1 Type of investors –Experienced or common

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Common-Less than 5 Years	144	53.1	53.1	53.1
	Experienced-more than 5 years	127	46.9	46.9	100.0
	Total	271	100.0	100.0	

1. Experience of investors and Risk bearing capacity:

H0: Investment experience and risk bearing capacity of investors are independent

Table 2 shows the risk perception of the categorized respondents on the basis of their experience of investing.

The mean rank for the attribute "currently monthly income fall short, meet or exceed"

given by experienced investors is 169.64 and by common investors is 106.33. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Significance value is far less than 0.05. Clearly results are highly significant and unlikely to have occurred by chances alone. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "expectation to begin withdrawing money from investment" given by experienced investors is 171.43 and by common investors is 104.75. . Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "comfort in using borrowed funds to invest in a promising long term investment" given by experienced investors is 175.93 and by common investors is 100.78. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "comfort in using borrowed funds to invest in a promising short term investment" given by experienced investors is 188.29 and by common investors is 89.88. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "In speculation what will you choose" given by experienced investors is 186.06 and by common investors is 91.85. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "percentage of annual income do you invest" given by experienced investors is 191.84 and by common investors is 86.75. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "how do you invest from regular income" given by experienced investors is 185.56 and by common investors is 92.29. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

The mean rank for the attribute "Risk Personality Type" given by experienced investors is 201.94 and by common investors is 77.84. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Since the sig. value is <0.05, the main difference is significant which implies that the difference in response based on the years of experience is significant.

Table 2. Investment experience and risk bearing capacity

	From how long you are investing?	N	Mean Rank	Mean	Std. Deviation	Chi-square	Asymp. Sig.
current monthly income fall short, meet or exceed	Less than 5 Years	144	106.33	1.7565	.75505	51.275	.000
	more than 5 years	127	169.64				
	Total	271					
expectation to begin withdrawing money from investment	Less than 5 Years	144	104.75	2.1107	.75198	56.110	.000
	more than 5 years	127	171.43				
	Total	271					
comfort in using borrowed funds to invest in a promising long term investment	Less than 5 Years	144	100.78	1.9483	.75345	71.098	.000
	more than 5 years	127	175.93				
	Total	271					

comfort in using borrowed funds to invest in a promising short term investment	Less than 5 Years	144	89.88	1.9594	.82227	119.818	.000
	more than 5 years	127	188.29				
	Total	271					
In Speculation what will you choose	Less than 5 Years	144	91.85	1.9779	.83415	109.838	.000
	more than 5 years	127	186.06				
	Total	271					
percentage of annual income do you invest	Less than 5 Years	144	86.75	1.9631	.84685	137.139	.000
	more than 5 years	127	191.84				
	Total	271					
how do you invest from regular income	Less than 5 Years	144	92.29	2.3137	.72607	113.780	.000
	more than 5 years	127	185.56				
	Total	271					
Risk Personality Type	Less than 5 Years	144	77.84	3.0185	1.38899	176.325	.000
	more than 5 years	127	201.94				
	Total	271					

Table 3 depicts frequency distribution of risk personality over the responses from experienced and common investors

Table 3 : Risk Personality Type

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Conservative	51	18.8	18.8	18.8
	Moderately Conservative	54	19.9	19.9	38.7
	Moderate	56	20.7	20.7	59.4
	Moderately Aggressive	59	21.8	21.8	81.2
	Aggressive	51	18.8	18.8	100.0
	Total	271	100.0	100.0	

2. Experience of investors and attitude towards investment:

H0. Investment experience and attitude of investment are independent

Table 4 shows the attitude for investment of the categorized respondents on the basis of their experience of investing. Kruskal Wallis H test shows that there is a statistically significant difference between the groups. Significance value of most of the attributes is less than 0.05. Clearly results are significant and unlikely to have occurred by chances alone. Since the sig. value of most of the attributes are <0.05, the main difference is significant which implies that the difference in responses regarding attitude of investment based on the years of experience is significant.

Table 4: Investment experience and attitude of investment

	From how long you are investing?	N	Mean Rank	Mean	Std. Deviation	Chi-square	Asymp. Sig.
I believe in actively managing my investments.	Less than 5 Years	145	144.36	2.9225	.92170	6.457	0.046
	more than 5 years	126	126.38				
	Total	271					
Active portfolio management can yield supernormal profit	Less than 5 Years	145	145.83	3.1365	.91479	5.454	0.020
	more than 5 years	126	124.69				
	Total	271					
	Less than 5 Years	145	145.92	3.1402			

I regularly review and compare my investment performance with market benchmark	more than 5 years	126	124.58		.89582	5.542	0.019
	Total	271					
I revise my investments to achieve my goals	Less than 5 Years	145	145.00	3.0849	.91297	4.547	0.033
	more than 5 years	126	125.65				
	Total	271					
I prefer to explore new investment options / strategies	Less than 5 Years	145	144.83	2.8967	.91714	4.447	0.035
	more than 5 years	126	125.84				
	Total	271					
I enjoy learning new things about investing.	Less than 5 Years	145	148.33	3.1033	.88424	8.842	0.03
	more than 5 years	126	121.81				
	Total	271					
I can easily change my investment decision once taken.	Less than 5 Years	145	131.69	2.7048	.91971	1.055	0.0304
	more than 5 years	126	140.96				
	Total	271					
Investment is always prior to other expenses in my life	Less than 5 Years	145	139.21	3.1661	.90580	0.582	0.446
	more than 5 years	126	132.31				
	Total	271					
I believe that investment can perform better in downturn market	Less than 5 Years	145	149.38	3.5498	.96432	9.930	0.002
	more than 5 years	126	120.60				
	Total	271					
I don't feel any insecurity in my investment when market trend changes.	Less than 5 Years	145	155.77	3.6273	.99510	21.959	0.000
	more than 5 years	126	113.25				
	Total	271					
I would rather have someone else manage my investments than deal with it myself.	Less than 5 Years	145	158.70	3.3616	.88309	29.186	0.000
	more than 5 years	126	109.88				
	Total	271					
I can cope with the stress associated with investments	Less than 5 Years	145	166.83	3.5535	.89230	56.069	0.000
	more than 5 years	126	100.52				
	Total	271					
I would hesitate in paying financial advisor an adequate fee for his expert advice, despite the fact that he may be getting commission from the company	Less than 5 Years	145	148.62	3.5424	.88037	9.050	0.003
	more than 5 years	126	121.48				
	Total	271					
As financial advisors earn commissions from companies, there is no need to pay them advisory fee.	Less than 5 Years	145	148.64	3.7159	.91312	8.942	0.003
	more than 5 years	126	121.46				
	Total	271					
I carefully review the financial information I receive in the mail.	Less than 5 Years	145	148.02	3.0443	.96890	8.111	0.004
	more than 5 years	126	122.16				
	Total	271					
I want to know all the details in fine print,	Less than 5 Years	145	144.55	3.1292	.90774	4.128	0.042
	more than 5 years	126	126.16				

before I make any investment decision.	Total	271					
The complete information required by investors for correct decision making is generally provided by Financial advisors	Less than 5 Years	145	138.09	3.3247	.94248	0.240	0.624
	more than 5 years	126	133.60				
	Total	271					
Instead of paying a financial advisor, I expect a pay-back from the commission they get from the companies	Less than 5 Years	145	144.36	2.9225	.92170	3.967	0.046
	more than 5 years	126	126.38				
	Total	271					
As financial advisors earn commissions from companies, there is no need to pay them advisory fee.	Less than 5 Years	145	145.83	3.1365	.91479	5.454	0.020
	more than 5 years	126	124.69				
	Total	271					
Financial Advisors pressurize people into making decisions they are not ready to make.	Less than 5 Years	145	145.92	3.1402	.89582	5.542	0.019
	more than 5 years	126	124.58				
	Total	271					
Attitude of Investors	Less than 5 Years	145	157.85	1.4649	.49969	35.846	0.000
	more than 5 years	126	110.85				
	Total	271					

Table 5, depicts frequency distribution of attitude towards investment over the responses from experienced and common investors. It is evident that overall no investor were either pessimistic or highly pessimistic.

Table 5: Attitude of Investors, distribution

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	80	29.5	29.5	29.5
	Optimistic	181	66.8	66.8	96.3
	Highly Optimistic	10	3.7	3.7	100.0
	Total	271	100.0	100.0	

3. Risk Bearing capacity and attitude towards investment.

H0: There is no association between Risk Bearing capacity and attitude towards investment

Table 6 shows the descriptive statistics of various personality types (conservative, moderately conservative, moderate, moderately aggressive, aggressive) in association with attitude towards investment (highly pessimistic, pessimistic, neutral, optimistic, highly optimistic) using cross-tabulation. Evidently, there was no respondent who could be in the pessimist or highly pessimist category.

Table 6: Attitude of Investors * Risk Personality Type Crosstabulation

			Risk Personality Type					Total
			Conservative	Moderately Conservative	Moderate	Moderately Aggressive	Aggressive	
Attitude of Investors	Neutral	Count	12	9	10	24	25	80
		Expected Count	15.1	15.9	16.5	17.4	15.1	80.0
		% within Attitude of Investors	15.0%	11.2%	12.5%	30.0%	31.2%	100.0%

	Optimistic	Count	38	44	43	33	23	181
		Expected Count	34.1	36.1	37.4	39.4	34.1	181.0
		% within Attitude of Investors	21.0%	24.3%	23.8%	18.2%	12.7%	100.0%
	Highly Optimistic	Count	1	1	3	2	3	10
		Expected Count	1.9	2.0	2.1	2.2	1.9	10.0
		% within Attitude of Investors	10.0%	10.0%	30.0%	20.0%	30.0%	100.0%
Total		Count	51	54	56	59	51	271
		Expected Count	51.0	54.0	56.0	59.0	51.0	271.0
		% within Attitude of Investors	18.8%	19.9%	20.7%	21.8%	18.8%	100.0%

Table 7 shows that p-value is less than 0.05 which means the association between risk personality type and attitude toward investing is statistically significant.

Table 7: Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	24.960[a]	8	.002
Likelihood Ratio	25.041	8	.002
Linear-by-Linear Association	8.682	1	.003
N of Valid Cases	271		

a. 5 cells (33.3%) have expected count less than 5. The minimum expected count is 1.88.

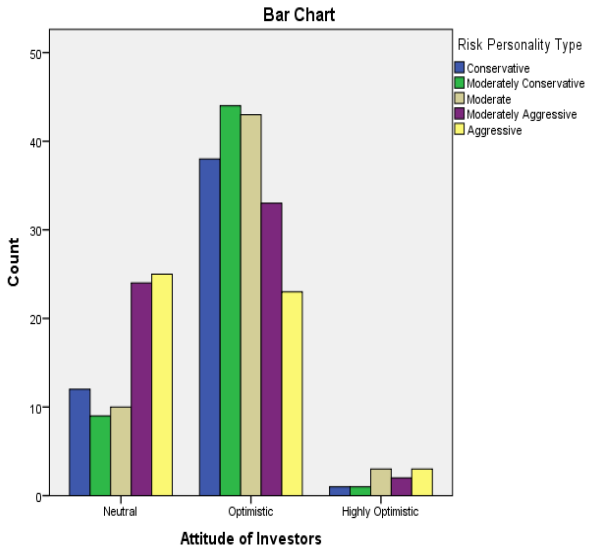

Figure 1: *Attitude of Investors vs Risk personality type (Source: Self-Developed)*

Conclusion:

After the study it can be concluded that risk bearing capacity of the investors is affected by bye years of experience in investing. Also it is clear from the observation that, experienced investors are more risk taker than the common investors. Overall more number of investors fall in moderate and moderately aggressive risk bearing categories. Though attitude towards investment has mixed responses from the investors, but overall all investors do not fall in highly Pessimistic and Pessimistic categories. It can be concluded that it no additional motivation is required to keep the investors attitude optimistic. It has also been observed that optimistic investors do not have much spread in their risk personality types in comparison to neutral and highly optimistic investors.

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