

Investor behaviour in Sri Lankan Stock Market

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In traditional theories of finance, it is assumed that the investors are rational. However, research on investor behaviour has documented that many investors do not always take rational investment decisions. Many studies document that their investment decisions are also influenced by behavioural factors. Behavioural finance is a relatively new branch of study in finance, where behaviour of markets is being explained through behavioural characteristics of investors. Sri Lanka being a developing or emerging market with low capitalization and moderate activity levels and high variance in performance levels, compared to even the smaller regional markets, has a unique setting in which investor risk behaviour could be analysed.

The study focusses on behavioural factors of investors, with special emphasis on the demographic and psychographic factors of the individual investors. Behavioural attributes/traits were identified via a comprehensive literature review from which the conceptual framework of investor risk behaviour was developed. One hundred Individual investors investing in the CSE (Colombo Stock Exchange) were selected through probability sampling. Most important factors from the selected demographic and psychographic factors for the investor risk behaviour were filtered out from exploratory factor analysis (Principal Component Analysis). Then by applying hierarchical cluster analysis, investors were grouped into 3 separate risk groups. The three groups of investors were classified as high risk, medium risk and low risk.

It was found that there was significant difference between the groups on overconfidence, age, marital status, number of dependants and the employment sector of those individual investors. Kruskal Wallis Test was used to identify whether there is a significant difference between the traits of each group.