A Behavioural Model to Assess the Risk Perception and Behaviour of Individuals in Investment Decisions

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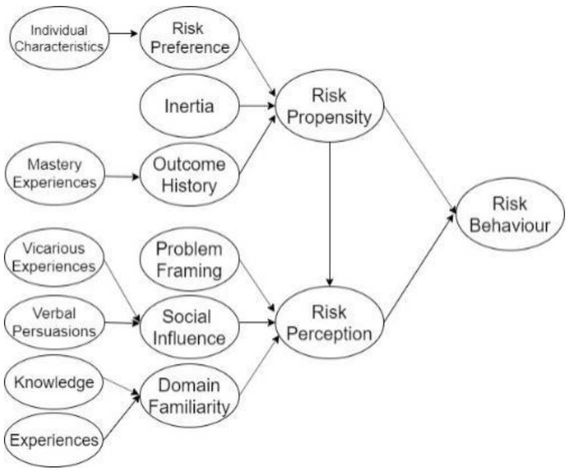
Risk behaviour is the controlled conduct of people in contexts with uncertainty, where there is a possibility of the outcome received deviating from the outcome expected. As any kind of investment bears a certain proportion of risk, investors qualify as a competent sample in analyzing risk behaviour. Investor behaviour depends on external factors such as macro stability, expected earnings, broker recommendations, dividends paid and stock marketability, as well as internal factors such as herd behaviour, optimism and risk appetite of the investor. In developing countries like Sri Lanka, the investment markets are less informationally efficient and investor risk appetite is a less prominent factor. Therefore, the need of upgrading the investment culture of a developing country through a customized model which accurately determines the investor risk appetite has become a timely need. Although numerous studies have been carried out, use of a psychological approach to explain the investor behaviour remains relatively unexplored. The overarching goal of this study is to assess the determinants of risk behaviour and how these factors can be used in developing a comprehensive model that facilitates categorization of people according to their risk profiles. This study focuses on interpreting the individual investor behaviour through a combination of the cognitive psychological approach of perceived self-efficacy and the reconceptualized model of risk behaviour in a developing country context. Perceived self-efficacy is the concept where people's beliefs and perceptions on their own personal abilities affect their actions taken to reach designated goals. The reconceptualized model suggests that an individual's risk behaviour is dominated by two major characteristics, namely risk propensity and risk perception. It was further specified that risk propensity positively affects the risk-seeking behaviour while risk perception has a negative effect on it. The reconceptualized model incorporates the cognitive psychological approach of perceived self-efficacy to the risk behaviour model. The risk behaviour model has been adjusted by removing the organizational-related factors from it. The developed model is validated through expert opinion and data obtained from investors who engage in high risk investments.

Keywords: Investors; Risk Behaviour; Self-Efficacy; Behavioural Model



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