Understanding the Psyche of Retail Investors in India and Their Reactions towards Market Highs and Lows While Making Investment Decisions during the Times of Covid-19

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Abstract

Purpose: Behavioral finance explains the market anomalies and how the psychology of investors affects their investment decisions. Amidst the Coronavirus crisis, it becomes very important to understand the psyche of retail investors in India, how would they react to the market ups and downs, assessing their risk profile, and what sources of information they consider reliable while making investment decisions.

Design/Methodology: A primary research was done, and a sample of 64 retail investors was collected using a structured questionnaire. Analysis was done using SPSS 21 and Microsoft Excel

Findings: The results showed that investors are risk-averse and very cautious of where and how much they invest. In the two events when the market reached its lowest on 25th March 2020 and highest on 21st January 2021, the mind of investors was stable as they had somewhat anticipated the events and they did not engage in mindless selling or buying of stocks.

Managerial Implications: Studying the psyche of retail investors is very important and can help the stock broking firms to come out with customized and safe products for investors.

Scope for Future Work: The impact of Covid-19 on retail investors and stock market can also be studied using secondary data. This would validate the findings of primary data.

Limitations: The main difficulty faced during the research was to collect the sample of only retail investors and the spread of coronavirus made it a little difficult to reach out to people

Keywords: Behavioural Finance, Coronavirus crisis, Psyche of investors, Investment decisions, Retail investors

Introduction

In the earlier times, investors were considered rational. This was the base of the various traditional finance models like Efficient Market Hypothesis (EMH), which considered investors as Homo Economicus, which means that they are always rational and that the prices of stocks always reflect all the information, so there are less or no chances of beating the market. But various events like the Dot Com bubble in the 90s and the real estate bubble in 2008, and various investors like Warren Buffett, who gained abnormal returns, showed that there are some happenings that could not be explained by traditional models. This gave way to a new field, i.e., Behavioural Finance, which said that investors while making investment decisions, are often influenced by their psychology and cognitive biases. Such biases force them or rather urge them to make decisions that might not be rational many times. Some of the famous biases are self-attribution bias, overconfidence, herding, hindsight bias, familiarity bias, loss aversion bias, etc.

Herding is the most common bias which affects investors. It is a tendency to copy the actions of others. Herding happens when investors, while trying to make investment decisions look around or mimic each other's' actions believing others to have better knowledge while discounting their own facts and knowledge. Investors moving together in one direction can significantly influence the stock prices and returns. Herding is most commonly seen in times of uncertainty when the market goes exceptionally up or down.

One such uncertain event happened when the whole world got affected due to Covid-19. It started in Wuhan, China, in November 2019 and crossed its borders in early January 2020, and took a toll on everyone's health, life, and the world economy. The death toll rose to over a million around the world. To restrict the spread of the deadly virus, many countries imposed nation-wide lockdowns. The implementation of lockdown hit the world economy really bad, and its adverse effects were seen on the financial markets as well. In recent research by Ramelliy & Wagnerz (2020) studied the behaviour of investors during the phase of Covid-19. According to them, there were three phases of reactions. The Incubation Phase started in early January after pneumonia cases were detected in Wuhan, China. The second phase was The Outbreak which was after 20th January, and the third was Fever Phase which began on 24th February, after Italy imposed a lockdown in its most productive region, Lombardy. In the Incubation Phase, investors who were well informed anticipated what was about to come in the coming weeks and months. There was also fear among investors, which led to a slow fall in the market. In the Outbreak Phase, the attention of investors and analysts grew. The search intensity for 'Coronavirus' on Google increased many folds. It was expected that global trade would face adverse effects soon. As work from home increased telecom industry performed well. It was in the Fever Phase when markets went wild a little bit as there was sudden realization among people that the virus could affect them too. As a result, panic selling started in the stock market. The Health crisis was taking the face of the financial crisis.

A sudden stock market crash was witnessed globally, which was also known as the 2020 Stock Market Crash or The Coronavirus Crash, or The Coronavirus Correction. It began on 20th February 2020 and ended on 7th April 2020. Selling got intensified from early March to Mid March with multiple severe daily drops such as on 9th March, which is known as 'Black Monday 1' when there was a -7.79% decline in the stock market, 12th March known as the 'Black Thursday' when there was a -9.99% decline and 16th March known as 'Black Monday 2' when there was a 12.93% decline. The market and its panic were saved through support from governments around the world, where banks and reserves across the world were told to reduce their interest rates, bank rates, and cash flow rates1.

The world equity markets saw a 50% decrease taking into account the short-term impact of Covid-19 on the economy. Foreseeing the long-term adverse effects of Covid-19, governments around the world introduced multi-trillion relief packages to save their economies. The Indian government also took some major steps to save its economy from the drastic downturn. A relief package of Rs 1.7 trillion was declared by the Finance Minister on 26th March 2020. A relief package of Rs 20 trillion for Covid-19 was again declared by the Prime Minister of India on 15th May 2020. A comprehensive stimulus package of Rs 2.65 lakh crore was declared by the finance minister on 14th November 2020. To give a stimulus to the Indian economy, some relief measures were announced by the Reserve Bank of India on 27th March 2020 and 17th April 2020. These were some major liquidity measures taken at a time of liquidity crunch. The repo rate was reduced by 75 basis points from that time, current 5.15% to 4.40%. For one year, the CRR of all banks was reduced by 100 basis points to 3%. This step gave liquidity of Rs 1,37,000 crore to the banking system. The liquidity coverage ratio was also reduced from 100% to 80%. The combined effect of all these measures was expected to give liquidity of Rs 4.74 lakh crore to the Indian economy. This was a short-lived bear market, and stock markets entered a bull phase in April 2020, which is still continuing. The market also saw its historical peak of Sensex, reaching 50000 points on 21st January, 20212.

Amidst such uncertainty, it becomes very important to study the psyche of retail investors towards investment in the stock market, to know how they reacted when the market reached its lowest during the lockdown and then revived back and reached its highest. It also becomes important in the times of Covid-19 to find out and judge their risk profile and what sources of information do they consider reliable while making investment decisions in the stock market. Such research would help broking firms to come up with better services and customized new products of investment.

Review Of Literature

Alam et al. (2020) studied the effects on the Indian stock market due to the lockdown that was imposed during Covid-19. They also studied whether the consequences of the lockdown and market reactions would be the same in the pre and post-lockdown periods during the phase of Covid-19. 31 companies listed on the Bombay Stock Exchange (BSE) were studied and Market Model Event Study was done. During the lockdown period, the market reacted positively, and there were positive Average Abnormal Returns (AAR) because there was anticipation among the investors regarding the lockdown. It was only during the pre-lockdown period that investors had panicked, which got reflected in the negative AAR, but after that, the situation and performance of the stock market improved. Mishra et al. (2020) studied the impact of Covid-19 on the stock returns of companies and compared the outcomes with the outcomes of demonetization and Goods and Services Tax (GST). Using daily stock returns from 2003 to 2020. It was found that stock returns for all indices were negative during the outbreak of Covid-19 and the impact was much severe when compared with the time of implementation of demonetization and Goods and Services Tax (GST) in India. Ramelliy & Wagnerz (2020) tried to analyze the impacts of Covid-19 on the stock prices and how real shocks and financial policies drove firm value. It was initially found that companies with an international orientation underperformed as they had trade with China. The markets moved feverishly as the virus spread in Europe and the United States. During this phase, investors and analysts were concerned about firms that had high corporate debt and little cash. In general, their study showed that retail investors had anticipated the real economic effects of Covid-19, which would find its way into the financial channels.

Research Objective And Design

The research objectives were:

Objective 1: What was the investors' psychology while making investment decisions during the times of Covid-19.

Objective 2: What were the investors' reactions to the market highs and lows during the phase of Covid-19.

Objective 3: Analysing the risk profile of investors under different situations.

Objective4: What were the important sources of information taken into consideration by investors while making investment decisions.

For the present research, primary data was collected by framing a structured questionnaire. The respondents (retail investors in the stock market) were asked 6 questions under objective 1, 2 questions under objective 2, 3 questions under objective 3, and 1 question based on the Likert scale on objective 4.

Judgemental sampling was done, and a total of 64 responses were received. Statistical Package for Social Sciences (21) and Microsoft Excel were used for the data analysis.

Results And Analysis

Retail investors investing in the stock market in India were asked to fill a structured questionnaire. A total of 64 responses were received. Of the total respondents, 67.19% were Males, and 32.81% were Females. Maximum respondents, i.e., 28.13% worked in a private organization, 23.44% were retired, 21.88% were professionals, 17.19% were government employees, and 9.38% were entrepreneurs. Maximum respondents, i.e., 43.75%, belonged to the monthly income bracket of less than Rs 50000, followed by 37.50% who were from the monthly income bracket of Rs 50000-Rs 1.5 lakhs. Maximum respondents, i.e., 48.44%, were from the age group of 20-30 years, followed by 35.94% from the age group of 30-40 years.

Under Objective 1: What was the investors' psychology while making investment decisions during the times of Covid-19? The following were the questions and their results:

Q1. How many times do you keep a check on your investment?

Results: Out of 64 respondents, 22 (34.92%) said they kept a weekly track of their investment, 20 (31.75%) kept it daily, 19 (30.16%) once in a month, and 2 (3.17%) many times a day

Q2. Usually, what is the percentage of your monthly income you invest in the stock market?

Results: Out of 64 respondents, 58 (90.63%) invested between 10%-25%

Q3. What is your risk appetite

Results: Out of 64 respondents, 38 (59.38%) were ready to take the medium risk, and 19 (29.69%) opted for low risk

Q4. What is your objective of investing in the stock market?

Results: Out of 64 respondents, 24 (37.50%) opted for their objective of investment being creating long term wealth, 20 (31.25%) opted for a combination of both income and capital gain

Q5. From the options given below, select the ones you think affect you as an investor while making purchasing or selling decisions in stock market (you can select more than one)

Results were as follows:

Variables That Can Affect Investors While Making Purchasing or Selling Decisions	*Count*	% %
You have enough knowledge about the stock market so you do your own fundamental analysis of stocks and market	20	31.3
You go with the advice of your research analyst	23	35.9
You keep in touch with the online mediums and news channels that give advice about stock markets and go with them	29	45.3
Many times, you just blindly take a decision based on what maximum investors around you are doing	12	18.8
You go with your intuition or gut feeling	9	14.1

Q6. From your past, what can you say about the percentage of chance that your financial decisions taken during extreme market conditions (market high or market low) proved to be right.

Results: Out of 64 respondents, 58 (90.63%) believed that 50%-80% times their investment decisions were correct, while 6 (9.38%) opted for 80% and above

ANALYSIS:

From the results of the above 6 questions, it can be said that investors are more cautious of where and how much to invest. Maximum investors, i.e., 90.63%, invested 10%-25% of their monthly income in the stock market, and 34.92% of investors kept a weekly track of their investments. 59.38% of investors were ready for medium risk, and maximum investors wanted to create long-term wealth or a combination of income and capital gain. During the market ups and downs, maximum investors, i.e., 90.63%, said that investment decisions taken by them were correct for about 50%-80% times. Maximum investors said that stock market advice given by news channels, online mediums, and their research analyst affected their investment decisions. Very few relied on their gut feeling, intuition, and blindly following others. So, from the above, we can say that nowadays, investors are much more knowledgeable and rational. They look for better advice for making fruitful investments, and they do not just go blindly following others. They are much more cautious and invest just a part of their income in the stock market.

Under Objective 2: What were the investors' reactions to the market highs and lows during the phase of Covid-19? Following were the questions and the results

Q1. How your investment decision making was affected when the first lockdown was declared in India on 25th March 2020, and the market reached its lowest

Results: Out of 64 respondents, 49 (76.56%) opted for 'My mind was stable, and I decided to hold my stocks and take a decision after a little bit of analysis since I have knowledge about the market,' 9 (14.06%) opted for 'I was in fear and panic, so I decided to consult my broker or analyst before making any decision,' 3 (4.69%) opted for 'I was in fear and panic, so I decided to sell my holdings with the fear of market going down more' and 3 (4.69%) opted for 'I was in fear and panic, so I decided to do what others around me were doing.'

Q2. The Sensex recently reached its highest history at 50000 points on 21st January 2021. Seeing this market high, what were your reactions or sentiments towards your investment in the stock market?

Results for each of the options:

Statements	Count	%
You did your own analysis, and in order to make a profit out of the high, you decided to immediately sell your stocks:	8	12.9
You saw other investors around you selling their stocks in order to make a profit, and you did the same	7	11.3
Your analyst or friends suggested you stay invested, and you went with their advice	11	17.7
You did your own analysis and decided to stay invested	36	58.1

ANALYSIS

From the results of the above questions, it can be said that in both the cases when the stock market reached its lowest and highest during the phase of Covid 19, retail investors who actually had knowledge about the market decided to stay invested and took the decision only after doing some analysis. This shows that investors have confidence in their decisions and also have knowledge about the market.

Under Objective 3: Analyzing the risk profile of investors under different situations, following were the questions and the results

Q1. Which option would you select if you are thinking of making an investment of Rs 20000?

Results: Out of 64 respondents, 36 (56.25%) opted for 'There is a 30% probability of a return of more than 25% on this investment' and 28 (43.75%) opted for 'There is a 70% probability of earning a return of less than 25% on this investment.'

Q2. You are given the following situation. You bought Wipro stock at Rs 450 one month ago. Its current price is going at Rs 430. It is speculated with a 50-50% chance that one month from now, the share price will increase by Rs 20 or decrease by Rs 20. Which option would you choose from the following options

Results: Out of 64 respondents, 53 (82.81%) opted for 'Given equal chances of an increase or decrease, you decide to hold the stock for a month losing an additional Rs 20 or breakeven' and 11 (17.19%) opted for 'Sell the stock now, thereby realizing a loss of Rs 20.'

Q3. Company ABC is in the process of making a vaccine for curing covid-19. There are equal chances of the vaccine being a hit or not working at all. Currently, its price is on the rise. Many of your friends and colleagues start buying shares of ABC anticipating it to rise more. Under such a situation and similar situations, how would you react to such information

Results: Out of 64 respondents, 41 (64.06%) opted for 'Maximum time you immediately take a buying decision without studying the fundamentals,' 18 (28.13%) opted for 'You will avoid it altogether,' and 5 (7.81%) opted for 'Maximum time after giving thought and doing some study about the facts you take a buying decision if you feel its right.

ANALYSIS

From the results of the above questions, it can be said that maximum investors are risk-averse because even if they are given a 30% probability of earning a return of more than 25% on their investment, they will agree to it. If they are given equal chances of an increase or decrease in stock price, maximum investors opt for holding the stock, which shows their patience and confidence. However, sometimes due to instant reactions, they can make a buying decision without studying the fundamentals when a stock is expected to rise.

Under Objective 4: What were the important sources of information taken into consideration by investors while making investment decisions? Following was the question and the result

Q1. Mark the following sources of information on a 5 pointLikert scale (5 being the extremely Important factor and 1 being Not at all Important factor) taken by you into consideration while making an investment decision.

Results were as follows:

News from electronic media and newspapers about economic indicators such as GDP, FII, FDI, etc.: 21 (32.81%) considered it 'Very Important,' and 16 (25%) considered it 'Extremely Important.'

Announcements by companies regarding their future policies, current performances, payouts of dividends, etc.: 28 (43.75%) considered it 'Extremely Important,' and 17 (26.56%) considered it 'Very important.'

Social factors: 19 (29.69%) considered it 'Very Important,' and 18 (28.13%) considered it 'Moderately Important.'

Political factors: 22 (34.38%) considered it 'Very Important,' and 13 (20.31%) considered it 'Moderately Important.'

Information provided by your friends, family, and colleagues: 20 (31.25%) considered it 'slightly Important' and 'Moderately Important.'

Information and suggestions by your broker or your analyst: 22 (34.38%) considered it 'Very Important.'

Advices by the experts in the field: 27 (42.19%) considered it 'Very Important.'

Constantly taking into account what investors around you are doing: 20 (31.25%) considered it 'Moderately Important' and 16 (25%) considered it 'Slightly Important.'

A stock's past performance: 22 (34.38%) considered it 'Very Important.'

ANALYSIS

The sources of information taken into consideration or considered very/extremely important by maximum retail investors while making investment decisions were: News from electronic media and newspapers about economic indicators, Announcements by companies regarding their future policies, current performances, pay-outs of dividends, etc., Social factors, Political factors, Information and suggestions by broker or analyst, Advices by the experts in the field, A stock's past performance. The factors not considered that important by maximum retail investors were: What other investors around them were doing and Information provided by friends, family, and colleagues. So, we can say that investors rely more on fundamentals or reliable sources of information regarding the stock market while making investment decisions.

Conclusion

So, from the above, it can be said that maximum investors nowadays have knowledge about the stock market, and they are very cautious of where and how much to invest. They are ready to take the medium risk and have an aim of creating long-term wealth through the earnings of the market or a combination of income and capital gains. Investors are also risk-averse because, under different situations that were asked, they decided to avoid risk. For their knowledge and investment decisions, investors rely less on gut feeling, intuition, blindly following others, advices from family, friends, and colleagues. Sources of information considered reliable by maximum investors regarding investment decisions are news channels, online mediums, advice by stockbroker, analyst or experts in the field, company announcement and stock past performance, social and political factors. Retail investors also have patience and confidence as during the times of uncertainty like when the market reached its lowest when the first lockdown was declared in India on 25th March 2020 and when the market reached its highest on 21st January 2021, the investors' mind was stable and they decided to stay invested and take decisions only after doing some analysis.

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