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Investors' Awareness, Perceived Risk Attitudes, and Behavior in the Nepalese Capital Market

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ABSTRACT

This study examines investors' awareness, risk attitudes, and behavior in the Nepalese capital market, focusing on individual investors' perceptions. A descriptive research design was employed to provide a comprehensive analysis, using a deductive and quantitative approach. Primary data were collected through questionnaires and analyzed using descriptive statistics, with mode calculations for key responses. Findings indicate that most investors possess moderate knowledge of the capital market and rely on fundamental analysis. Awareness of mutual funds, central depository system (CDS), credit rating agencies, and portfolio management services were prevalent. Investors perceive good news as positively impacting the market, bad news as negative, and informational news as inconsistent. Political and economic changes are major factors influencing investment decisions, while market trends significantly affect investor behavior. A key challenge identified is the lack of investor confidence. Additionally, most investors assess risk and return before investing, preferring moderate risk with moderate returns. They view stock market returns as attractive as riskier as other investments. Government regulations are deemed insufficient in safeguarding investments. Regression analysis reveals that investor behavior is positively linked to awareness, risk perception, social learning, financial literacy, and cognitive-affective factors.

Keywords: investors, behavior, risk attitudes, capital market, stock market, return

Introduction

Behavioral finance blends psychology and economics to explore why investors frequently make irrational financial choices. Unlike traditional finance, which assumes that investors act rationally and markets are fully efficient, behavioral finance acknowledges that cognitive biases, emotions, and social factors often cause systematic errors in decision-making (Kahneman & Tversky, 1979). The Efficient Market Hypothesis (EMH), proposed by Fama (1970), claims that asset prices reflect all available information, making it impossible to consistently outperform the market without additional risk. EMH is divided into weak, semi strong, and strong form efficiency, depending on the type of information reflected in prices. However, various market anomalies such as momentum, value effects, and post-earnings announcement drift challenge EMH's assumptions. Behavioral finance attributes these irregularities to psychological biases like overreaction and reliance on past information.

Market efficiency is often assessed through factors like market capitalization, liquidity, and turnover. Financial literacy and awareness play crucial roles, as more

knowledgeable investors are likelier to engage in riskier assets (Guiso & Jappelli, 2005). Individual risk perceptions also affect investment decisions and vary based on personal beliefs (Elke & Richard, 1997). Common behavioral tendencies include loss aversion, overconfidence, and herd behavior, often resulting in poor diversification and reaction to market noise. In Nepal, despite improvements in market infrastructure and technology, understanding investor behavior remains vital for boosting market efficiency and addressing ongoing challenges (Kabra et al., 2010).

Purpose

The aim of the study is to assess the relationship and effect of investors' awareness, perceived risk and investors' behavior on Nepalese capital market.

Literature Review

Behavioral finance is a field of study that combines psychology and economics to explain why and how investors often make irrational financial decisions. Unlike traditional finance, which assumes investors are rational and markets are efficient, behavioral finance recognizes that cognitive biases, emotions, and social influences can lead to systematic errors in decision-making.

From Efficient Markets Theory to Behavioral Finance, explores the evolution of financial theory from the traditional efficient markets hypothesis (EMH) to the more nuanced and psychologically informed field of behavioral finance. Shiller (2003) a prominent economist and Nobel laureate, critiques the limitations of the efficient markets theory and highlights how behavioral finance offers a more comprehensive understanding of financial markets by incorporating human psychology, cognitive biases, and irrational behavior.

Similarly, Efficient Market Hypothesis (EMH), which argues that financial markets are effective because asset prices fully reflect all available information. According to EMH, it is impossible to consistently outperform the market through expert stock picking or timing since prices already include all known data. This idea, rooted in Fama et al. (1970) work, dominated finance in the mid-20th century. EMH assumes investors are perfectly rational, with equal, instant access to flawless information, no transaction costs, and no market restrictions, allowing prices to adjust immediately. It also presumes that investors interpret information uniformly and that new data arrives randomly with no market manipulation.However, EMH faces criticism due to observable market anomalies like momentum, where recent winners continue to outperform short-term, and the value effect, where stocks with low price-to-book ratios yield higher returns, challenging market efficiency (Shiller, 2003).

Shiller (2003) critiques EMH by highlighting how psychological factors, such as emotional biases and herd behavior, impact investor decisions, resulting in persistent market irregularities. The theory points to bubbles and crashes, showing prices can deviate significantly from true value, excess volatility beyond fundamentals, and predictable return patterns that contradict the theory, ultimately questioning the EMH's accuracy in explaining real-world markets.

Behavioral finance emerged as a response to the limitations of the Efficient Market Hypothesis (EMH), offering a more realistic view of financial markets by incorporating insights from psychology, sociology, and neuroscience (Shiller, 2003). Central to this field is prospect theory (Kahneman & Tversky, 1979), which shows that people value gains and losses differently, often feeling losses more intensely than gains. This explains why individuals take fewer risks when winning but behave more riskily to avoid losses, challenging traditional rational models. Jolls et al. (1998) extend these ideas into law and economics, highlighting that human behavior is limited by bounded rationality, willpower, and self-interest. Their work suggests that policies and legal rules must consider these human limitations to be effective and improve welfare.

Psychological factors play a key role in explaining market irregularities, challenging the idea that investors are perfectly rational as suggested by the Efficient Market Hypothesis (Simon, 1986). Investors often exhibit biases like overconfidence, mental accounting, and herding, where they follow others to avoid regret or mistakes (Jagongo & Mutswenje, 2014). This herding behavior can drive asset price surges, contributing to bubbles and volatility identified by Shiller (2003). Additionally, reliability theory helps explain how investors' views of system risk affect their financial choices, linking economic performance to investment decisions (Gavrilov & Gavrilova, 2001; Kannadhasan, 2015). These insights support a more comprehensive understanding of market behavior that benefits investors, innovators, and policymakers.

Studies on the Athens Stock Exchange highlight the importance of expected earnings, financial health, and a company's reputation, especially among experienced investors who survived market downturns (Merikas et al., 2011; Chong & Lai, 2011). Beyond these rational factors, behavioral biases also shape decisions. Investors often rely on heuristics and display risk aversion, with herding behavior common among both institutional and individual investors in various markets (Qureshi & Hunjra, 2012; Li et al., 2016; Phuoc & Doan, 2011).

In Nepal, research identifies specific trends such as a preference for common stocks in banking and finance sectors due to perceived returns and risks (Amatya, 2015; Darshandhari, 2018). Investors are becoming more sophisticated, showing increased engagement with government securities and growing awareness of socially responsible investing (Rana, 2019; Prasath & Dwivedi, 2022; Chhetri & Sharma, 2022). Overall, investment choices are shaped by a balance of financial fundamentals, psychological factors, and unique market characteristics, emphasizing the need for a combined approach that blends traditional finance and behavioral insights.

Building upon the reviewed literature, this study aims to analyze investor awareness, perceived risk attitudes, and investment behavior within the unique context of the Nepalese capital market. While voluminous research exists on developed markets, studies in developing economies like Nepal remain limited and exhibit non-uniform findings, preventing the generalization of international empirical results (Amatya, 2015; Rana, 2019). A specific research gap exists concerning academically inclined groups, such as management graduate students and faculty, who possess theoretical knowledge and analytical skills that may distinctively shape their financial decision making. To

address the gap, the study provides novel insights into how academic expertise influences investment behavior, thereby offering a fresh perspective on the dynamics of the Nepalese capital market.

Methodology

This research applied exploratory factor analysis to explore the factors linked to investor awareness and perceived risk attitudes among participants in Nepal's stock market. Additionally, the study incorporated both correlational and causal-comparative research designs. The correlational design was employed to determine the direction and strength of the relationships between investment awareness, perceived risk attitudes, and investment behavior. Meanwhile, the causal-comparative design was used to assess the impact of investor awareness and perceived risk attitudes on investment behavior. The study relied entirely on primary data sources. A structured questionnaire survey was conducted to gather insights into the opinions, perceptions, and characteristics of investors in Nepal's stock market. Actually, the survey was carried out in Kathmandu, distributing 384 questionnaires through email. This study uses primary data from investors trading shares on the Nepal Stock Exchange (NEPSE).

Cronbach's alpha was used to assess the reliability of investors' responses, showing how much the results are free from random errors.

Coefficient of Cronbach's Alpha

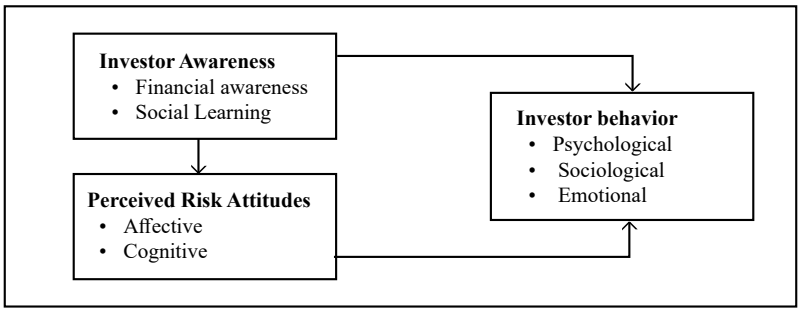
Cronbach's alpha	Standardized Cronbach's alpha	Number of items
0.768	.818	103

Conceptual Framework

The framework forms the theoretical foundation of the study, suggesting that investor awareness and perceived risk attitudes are key determinants of investor behavior. This model underpins the analysis and interpretation of the study's findings.

Figure 1

Conceptual Framework



Source: Guiso and Jappelli (2005)

Results

Demographic profile of the respondents provides the personal characteristics of the respondents in terms of their gender, age, educational qualification, marital status.

Table 1

Demographic profile of the respondents

Respondent's profile	Frequency	Percentage
Gender		
Male	237	61.71
Female	147	38.28
Total	**384**	**100**
Age (Years)		
Under 30	154	40.10
30-40	169	44.01
40-50	50	13.02
50 above	11	2.87
Total	**384**	**100**
Educational qualification		
Below masters	157	40.93
Masters and above	227	59.07
Total	**384**	**100**
Marital status		
Single	152	39.53
Married	232	60.47
Total	**384**	**100**

Source: Responses on survey questionnaire 2025

Kendall's Tau-b Correlations Coefficient for Investors' Behavior and its Determinants

The table showed the details correlation coefficients for other pairs of determinants, such as social learning (SL), financial awareness (FA), affective (AFF), and cognitive (COG) factors. Symbols (***, **, *) denote significance levels at 1%, 5%, and 10%, respectively. IB represents investors' behavior, IA stands for investor awareness, and PR refers to perceived risk attitudes. These findings highlight the interconnectedness of various factors influencing investor behavior.

Table 2

Kendall's Correlations Coefficient of Investors' Behavior and its Determinants in Nepalese Capital Market

	IB	IA	PR	SL	FA	AFF	COG
IB	1.000						
IA	.513*	1.000					
PR	.408*	.474*	1.000				
SL	.474*	.777*	.428*	1.000			
FA	.454*	.759*	.425*	.487*	1.000		
AFF	.345*	.326*	.668*	.303*	.272*	1.000	
COG	.374*	.491*	.735*	.437*	.467*	.341*	1.000

Source: Responses on Survey Questionnaire, 2025

The study also identifies a positive and significant association between investors' behavior and social learning. Similarly, financial awareness shows a positive and significant correlation with investors' behavior, suggesting that higher financial awareness leads to increased stock market participation. The tau coefficient for affective factors is positive and significant at the 1% level, indicating a strong link between emotional influences and investor behavior. Likewise, cognitive factors exhibit a positive and significant relationship with investors' behavior, highlighting the role of rational decision-making. It explores the relationship between investors' behavior and personal characteristics such as age, gender, education, marital status, occupation, and gross annual income. It presents Kendall's correlation coefficients for these pairs, with IB representing investors' behavior. Variables like AGE (age), GENDER (gender), EDU (education), MS (marital status), OCCUP (occupation), and GI (gross income) have been analyzed. Symbols (***, **, *) denote significance levels at 1%, 5%, and 10%, respectively. These findings provide insights into how personal attributes influence investment behavior in the capital market

Table 3

Kendall's Correlations Coefficient of Investors' Behavior and its Determinants related With Investors' Personal Characteristics

	IB	AGE GROWTH	GENDER	EDU	MS	OCCUP	GI
IB	1.000						
AGE GROWTH	-.014**	1.000					
GENDER	.017	-.041	1.000				
EDU	.019**	-.107	-.150**	1.000			
MS	.018	.595*	.068	.007	1.000		
OCCUP	-.053	-.395*	.099	.056	-.405*	1.000	
GI	-.014	.540*	-.108	.043	.470*	-.422*	1.000

Source: Responses on Survey Questionnaire, 2025

The results indicate a negative but significant relationship between investors' behavior and age at the 5% level, suggesting younger investors are more active in the stock market than older ones. A positive and significant correlation is found between investors' behavior and gender, as well as educational qualification, implying that higher education levels correlate with greater stock market participation. However, the association between investors' behavior and marital status is positive but insignificant, indicating married investors tend to invest more than single individuals.

The relationship between investors' behavior and occupation is negative and insignificant, implying business professionals may invest less compared to others. Similarly, gross annual income shows a negative and insignificant association, suggesting those earning less than 1 lakh invest more actively. It presents Kendall's tau correlation coefficients between investors' behavior and decision-making determinants like RETURN (returns), RECOM (recommendations), RISK (risk level), MTREND (market trends), IMAGE (company reputation), and SELFK (self-knowledge). Symbols (***, **, *) denote significance levels at 1%, 5%, and 10%, respectively, highlighting key factors influencing investment decisions.

Table 4

Kendall's Correlations Coefficient between Investors' Behavior and its Determinants for Taking Investment Decision

	IB	RE-TURN	RECOM	RISK	MTREND	IMAGE	SELFK
IB	1.000						
RETURN	-.005	1.000					
RECOM	-.126*	.029	1.000				
RISK	.175**	-.193**	-.004	1.000			
MTREND	.211**	-.362**	-.193**	.155**	1.000		
IMAGE	.095	-.244**	-.460**	.019	.145*	1.000	
SELFK	-.198**	-.051	-.244**	-.407**	-.302**	.080	1.000

Source: Responses on Survey Questionnaire, 2025

The results show a weak, insignificant negative relationship between investors' behavior and returns (cash/stock), making it inconclusive. Advocate recommendations have a significant negative correlation at the 1% level, suggesting higher recommendations may reduce stock market investment. A positive and significant association at the 5% level exists between investors' behavior and risk levels, indicating higher risk tolerance increases investment activity. Market trends also show a positive and significant relationship with investors' behavior. However, the link between investors' behavior and a company's image/goodwill is positive but insignificant. Conversely, self-knowledge about shares has a significant negative correlation at the 5% level, implying greater self-knowledge may reduce investment activity.

Regression Analysis on Determinants of Investors' Behavior

This section focuses on regression analysis to examine the relationship between investors' behavior and its determinants using primary data from 384 observations. The analysis employs Model 1 and Model 2, with statistical tests such as t-tests, F-tests, and adjusted R^2 (Adj. R^2) used to validate the models.

The result displays the regression results for Model 1, analyzing investors' behavior in the capital market. The findings indicate a positive relationship between investors' behavior and both investors' awareness and perceived risk attitudes. As awareness of the capital market increases, so does the level of investment, and vice versa. Similarly, higher perceived risk attitudes correlate with increased investment activity. The regression model, specified as IB = α + b1 IA + b2 PR + et, uses investors' behavior (IB) as the dependent variable, with investors' awareness (IA) and perceived risk attitudes (PR) as independent variables. The table reports intercepts, slope coefficients, t-statistics, F-statistics, and Adj. R^2 values. Significance levels are denoted by '**' for 1% and '*' for 5%. These results highlight the importance of awareness and risk perception in shaping investment decisions in Nepal's capital market.

Table 5

Regression Results on Investors' Behavior and its Determinants Investors' Awareness and Perceived Risk Attitudes

Models	Intercept	Regression Coefficients of		Adj. R-bar^2	SEE	F
		IA	PR			
(1)	1.009	.401	.331	.465	.397	93.936
	(4.937*)	(6.461*)	(5.002*)			
(2)	1.420	0.604		.435	.408	165.513
	(7.661*)	(12.865*)				
(3)	1.487		.614	.362	.433	122.607
	(7.116*)		(11.073*)			

Source: Responses on Survey Questionnaire, 2025

1. The signs ** and * denote that the results are significant at 1 percent and 5 percent level of significance respectively.
2. Dependent variable is investors' behavior.

The result resents the regression results (Model 2) analyzing investors' behavior in Nepal's capital market, with social learning (SL), financial awareness (FA), affective (AFF), and cognitive (COG) factors as determinants. The findings indicate a positive relationship between investors' behavior and all explanatory variables as social learning increases, investment levels rise, and vice versa. Similarly, financial awareness, affective, and cognitive factors also positively influence investment decisions.

The stepwise regression follows the model:

$IB = \alpha + b1SL + b2FA + b3AFF + b4COG + et$

Where, IB (Investors' Behavior) is the dependent variable. The table reports intercepts, slope coefficients, t-statistics (in parentheses), F-statistics, and adjusted R^2 values. Significance levels are marked with * (5%) and ** (1%).

The results confirm that social learning, financial awareness, affective responses, and cognitive reasoning collectively shape investor behavior in Nepal's stock market, with statistically significant relationships observed across key variables.

Table 6

Regression Results on Investors' Behavior and its Determinants

Models	Intercept	Regression Coefficient of				Adj. R-bar^2	SEE	F
		SL	FA	AFF	COG			
(1)	.920 (4.431*)	.214 (4.074*)	.204 (3.649*)	.265 (4.667*)	.076 (1.434*)	.471	.394	48.710
(2)	1.891 (11.270*)	.487 (11.409*)				.376	.428	130.176
(3)	1.894 (9.945*)		.479 (10.019*)			.317	.448	100.390
(4)	1.871 (8.990*)			.516 (9.263*)		.284	.459	85.803
(5)	2.239 (12.358*)				.407 (8.619*)	.255	.468	74.279
(6)	1.436 (7.706*)	.341 (6.706*)	.259 (4.761*)			.434	.408	83.045
(7)	1.443 (6.788*)			.365 (6.088*)	.261 (5.240*)	.363	.433	61.962
(8)	1.206 (6.070*)	.370 (8.228*)		.308 (5.615*)		.455	.401	90.183
(9)	1.583 (7.986*)		.346 (6.177*)		.221 (4.161*)	.366	.432	62.698

Source: Responses on Survey Questionnaire in Appendix A

1. The signs ** and * denote that the results are significant at 1 percent and 5 percent level of significance respectively.
2. Dependent variable is investors' behavior.

Discussion

Variables like AGE (age), GENDER (gender), EDU (education), MS (marital status), OCCUP (occupation), and GI (gross income) have been analyzed. Symbols (***, **, *) denote significance levels at 1%, 5%, and 10%, respectively. Like this result, Amatya (2015) and Darshandhari (2018) also revealed that investors are becoming more sophisticated, showing increased engagement with government securities and growing awareness of socially responsible investing. Kendall's tau correlation coefficients between investors' behavior and decision-making determinants like RETURN (returns), RECOM (recommendations), RISK (risk level), MTREND (market trends), IMAGE (company reputation), and SELFK (self-knowledge). Symbols (***, **, *) denote significance levels at 1%, 5%, and 10%, respectively, highlighting key factors influencing investment decisions.

Social learning, financial awareness, affective responses, and cognitive reasoning collectively shape investor behavior in Nepal's stock market, with statistically significant relationships observed across key variables. Similar result was found by Rana (2019); Prasath & Dwivedi (2022); and Chhetri & Sharma (2022) also provided investment choices are shaped by a balance of financial fundamentals, psychological factors, and unique market characteristics, emphasizing the need for a combined approach that blends traditional finance and behavioral insights. Similarly, Qureshi & Hunjra (2012); Li et al. (2016); Phuoc & Doan (2011) showed that investors often rely on heuristics and display risk aversion, with herding behavior common among both institutional and individual investors in various markets.

Conclusion

The study reveals significant variations in investor behavior and preferences within Nepal's capital market. Large investors typically gain market knowledge through structured education and professional training, contrasting with smaller investors who rely predominantly on personal networks. Experience levels show most investors are relatively new, with under five years in the market, though investment scales increase with accumulated experience.

Sectoral analysis indicates clear preferences, with commercial banks (63.7%) leading, followed by hydropower (44.7%), development banks (37.2%), and insurance (33%). Investment behaviors vary markedly by size of the organization; larger investors demonstrate more active trading patterns, shorter holding periods, and broader portfolio diversification compared to their smaller counterparts. Market participation shows 54.9% engaging in both primary and secondary markets, though large investors favor secondary markets (42.9%) while small investors prefer primary offerings (42.5%).

Educational preferences highlight that 51.2% of investors value discussion-based learning over formal training programs. Market competency assessments reveal 54.4% possess intermediate knowledge levels, with fundamental analysis being the dominant evaluation method. Modern financial instruments enjoy strong awareness, particularly mutual funds and CDS systems.

Behavioral drivers position market trends as the foremost influence, ahead of return considerations and professional recommendations. Persistent market challenges include limited investor confidence, market scale constraints, and regulatory deficiencies. Risk management practices show overwhelming adoption (93%) of risk-return analysis, with diversification strategies employed by 80.5% of investors. While market returns are generally viewed favorably, existing regulatory structures are widely regarded as insufficient for comprehensive investor safeguarding.

Implication: Scope for Future Research

Subsequent studies should incorporate larger sample sizes and extend coverage to diverse geographical regions across Nepal to yield more comprehensive and representative findings. Second, the respondent pool could be broadened to include policymakers, business professionals, and stock market analysts, which would provide a more holistic perspective on market dynamics. Third, while this study examines certain behavioral aspects, it does not address important factors such as trust, market efficiency, legal frameworks, and trading procedures elements that future researchers should incorporate for more thorough behavioral analysis. Lastly, the current study does not differentiate between brokerage firm, employees and general investors. Future investigations would benefit from establishing clear respondent classification criteria to ensure more precise and meaningful insights. These suggested improvements would significantly enhance the depth and applicability of future research in this domain.

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