Factors Influencing Investor's Decision Making in Nepalese Commercial Banks: Moderating the Role of Locus of Control

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Abstract

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This study examines how investors' demographic characteristics-such as age, gender, education, and experience and their investment choices are related with bias, and representational bias-serving as mediators in Nepalese commercial banks. A structured questionnaire survey was used to collect data from 403 participants who worked for various commercial banks in Nepal. To investigate the ways in which behavioral aspects and demographic traits influence investing decisions, a multiple regression analysis was performed. Herd behavior, locus of control, availability biases, and representative biases all have a big impact on investing choices. Furthermore, investing decisions are positively and significantly impacted by age, gender, and educational attainment. Experience is not a significant factor, though more seasoned investors typically depend less on emotional cues. The study's conclusions offer direction for the growth of the Nepalese stock market as well as insights into typical investor behavior patterns.

Keywords: *Representative Biases, Availability Biases, Locus of Control, Herd Behavior*

Introduction

The underlying premise of traditional finance is that investors and markets ought to behave in particular ways. It highlights how rational investors are thought to be, how they engage in efficient markets, and how they often make logical choices. On the contrary, it is observed that investors behave irrationally in the market by trading excessively, purchasing stocks without considering their intrinsic value, basing choices on historical performance, and doing so under the influence of friends and family. Chand (2024) stated that behavioral finance examines how emotional responses and cognitive biases impact investor behavior and market dynamics globally, particularly in poor countries like Nepal. It does this by integrating psychology into financial theory. This study found that herding tendency is the most important behavioral bias influencing stock investment decisions at NEPSE.

Two of the few studies conducted in Nepal, Dangol and Manandhar (2020), have focused on the behavioral elements of investors' investment choices. Bad mental health and an inability to understand complicated information can cause investors to make illogical decisions (Keswani et al., 2019). Behavioral finance, based on psychology, might be useful in this context since it explains why people purchase and sell stocks as well as the emotional and cognitive mistakes that influence investment decisions (Waweru et al., 2008). Rotter (1966) stated that the locus of control is the degree to which people believe they have influence over the events in their lives.

Literature Review

Suresh (2024) asserts that financial literacy for investors entails the capacity to make wise investment choices while steering clear of illogical tendencies and biases, including herd mentality, heuristic bias, framing effects, and cognitive distortions. The interaction of behavioral biases and financial literacy in influencing investing choices is investigated in this study.

Investment Decision Making

Allocating funds to a firm in the hope of receiving returns in the future is known as investing. Generally speaking, conducting thorough research and making unbiased decisions are necessary for successful investing. In order to explain why

even logical investors occasionally make bad choices, research conducted over the past 20 years has proposed the idea of "cognitive unconsciousness"- the existence of perceptions, memories, and thoughts outside of conscious awareness-even though all investors want to maximize their returns (Hilton, 2001). Investors may make illogical financial decisions as a result of emotional and subconscious influences that divert them from logical conduct (Baker & Nofsinger, 2002).

According to conventional financial theories, investors are totally logical, but in practice, people are impacted by a range of behavioral and psychological elements that make it difficult for them to make logical decisions. In order to explore the reasons for this, behavioral finance connects a number of aspects of human nature with financial models (Barber and Odean, 1999). These factors contribute to the fact that investors are not always rational and that behavioral preconceptions impact their decisions. To comprehend investors in the real world, it is crucial to examine investing decision-making through the prism of behavioral finance theories.

Representative Bias and Investment Decision Making

The study found that investment performance is negatively impacted by representativeness bias (Gavrilakis & Floros, 2022). The similar finding was reached by another study: representativeness prejudice and other behavioral biases significantly influence the selection of investors (Jain et al., 2021). The habit of classifying ideas, situations, and arguments according to historical occurrences is known as representativeness bias. This heuristic is characterized by the readiness to generalize about another person or entity, such as stocks, based on a limited set of features (Bazerman and Moore, 2012; Nisbett and Ross, 1980). This is because investors tend to rely on their intuition and mental shortcuts when making financial decisions.

Availability Bias and Investment Decision Making

The notion of availability refers to an individual's inclination to depend on information or knowledge that is immediately accessible without considering other options or alternatives (Adielyani & Mawardi, 2020). Ignoring the company's fundamentals and basing their decisions on their own memories and preferences might lead to investors making increasingly irrational decisions. Javed et al. (2017) described that an individual with availability bias prefers information that is readily available while making decisions rather than considering all of the available

possibilities. Therefore, researcher has communicated that availability bias also results in suboptimal decisions by creating the false perception that a stock with a high return would have a low risk and that a stock with a low return will have a high risk. Investors that choose to invest in local companies that they are more familiar with or where it is easy to gather information about them exhibit this behavior (Waweru et al., 2008). Depending on current facts, investors' risk-taking and choices about a particular security change (Grable et al., 2004). The available knowledge affects investor preferences and may lead to a certain investing pattern (Harris and Raviv, 2005). Sometimes, an investor's decision to invest might be influenced by even unrelated facts (Kirchler et al., 2005).

Moderating Role of Internal Locus of Control

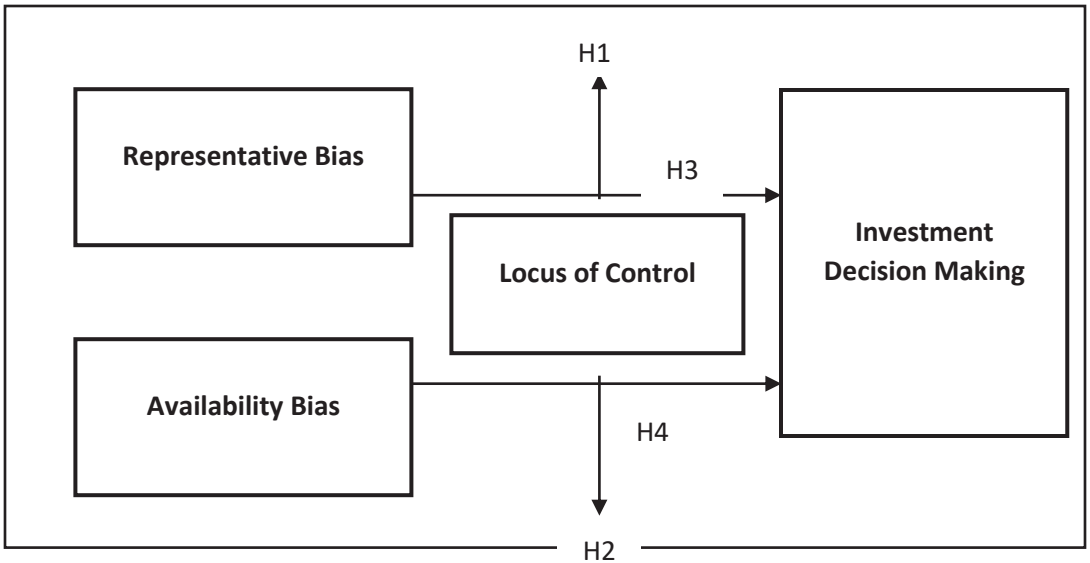
The decision-making process of investors and consumers is similar since both entail the purchase of capital assets. However, no significant research has been conducted on the subject of investing decision making. Research on the factors influencing moral decision-making (Ozbek et al., 2013) and customer decisions both take locus of control, a critical behavioral component, into account. A person who believes that their own skills are the cause of the desired result is said to have an internal locus of control. Because they think they are better than average, these investors will be more irrational in their investing choices (Kaustia and Perttula, 2012). However, when someone thinks that a positive result is the result of external factors like fate, luck, or powerful people, they have an external locus of control (Selart, 2005). If investors feel they have a say in the matter, they will be very inclined to make certain decisions. The locus of control provides a convincing explanation for future events, according to recent study (Hiller and Hambrick, 2005).

Research Framework

This study examines the relationship between investment decisions and demographic parameters, specifically gender, age, education level, and investment experience, with an emphasis on the mediating function of behavioral components. The study builds on previous research by creating a conceptual framework to examine how these factors affect investor choice. Furthermore, the research examines the locus of control interaction effect and assesses the relative explanatory power of representativeness bias and availability bias in causing irrational financial decisions.

Figure 1:

Conceptual Framework



Source: (Rasheed, Rafique, Zahid, & Akhtar 2018).

Research Hypothesis

Based on the four behavioral factors analyzed in this research, the research hypothesis is categorized into four different hypotheses:

- H1: There is a positive correlation between the level of irrationality in investing decisions and representative bias.
- H2: There is a positive correlation between availability bias and the level of irrationality in investing decisions.
- H3: The association between investment decision-making and representational bias is moderated by internal locus of control.
- H4: The association between availability bias and investment decision-making is moderated by internal locus of control.

Research Methodology

The factors impacting investor decision-making in Nepalese commercial banks were examined using a causal comparative research design. 403 full-time workers from well-regarded banks were chosen through the use of purposeful sampling. Structured questionnaires were used to gather data, and 403 out of 460 respondents answered. Closed-ended, rating scale, multiple-choice, and single-answer questions were all included in this research. Respondents' gender, age, occupation, marital status, educational background, investment experience, and investment ideas were among the demographic data gathered. The instrument's applicability for investigating these factors was validated by the results.

Results and Discussion

Data has been analyzed with references to the objectives and hypotheses of the study. The collected data are presented in tabular form in order to facilitate to reach to conclusion. For data analysis, firstly descriptive statistics is used. Then, correlation is used to analyze the relationship between investment decision and declared independent variables which is followed by regression analysis.

Correlation Analysis

A statistical technique for determining the degree and direction of a relationship between two variables is correlation analysis; the correlation coefficient can range from -1 to +1. This study employs Pearson's correlation analysis to investigate how locus of control, availability bias, and representativeness bias relate to one another when making investment decisions. Researchers can use this method to ascertain whether certain factors are statistically reliant on one another.

Table 1
Correlations Coefficient between Dependent and Independent Variables

		IDM	AB	RB	LOC
IDM	Pearson Correlation	1			
	Sig. (2-tailed)				
AB	Pearson Correlation	.433**	1		
	Sig. (2-tailed)	.000			
RB	Pearson Correlation	.453**	.415**	1	
	Sig. (2-tailed)	.000	.000		
LOC	Pearson Correlation	.601**	.485**	.559**	1
	Sig. (2-tailed)	.000	.000	.000	

**. Correlation is significant at the 0.01 level (2-tailed), N=403

The correlation coefficient analysis conducted on data from 403 participants reveals statistically significant positive relationships between investment decision-making (IDM) and the three behavioral factors studied: Availability bias (AB), Representativeness bias (RB), and Locus of control (LOC). The Pearson correlation coefficient between IDM and AB is 0.433, indicating a moderate positive association. This concluded that as investors exhibit higher availability bias, their investment decision-making patterns tend to increase correspondingly. Likewise, IDM and RB show a moderate positive correlation of 0.453, implying that representativeness bias also has a meaningful impact on investment decisions. Most especially, IDM and LOC have the strongest positive correlation at 0.601, reflecting a high degree of association. This stronger correlation indicates that an investor's locus of control plays a more significant role in influencing their investment decisions compared to the other two biases. All correlations have p-values less than 0.01, confirming that these relationships are statistically significant. In summary, locus of control demonstrates the greatest positive influence on investment decision-making, followed by availability bias and representativeness bias, emphasizing the important role behavioral factors play in shaping investors' choices.

Regression Analysis

Regression analysis is a statistical technique that is carried out with SPSS software to evaluate the association between a predictor and a dependent variable and calculate the likelihood that one variable would change for another.

Table 2
Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	.513	.190		2.696	.007
	AB	.170	.048	.160	3.529	.000
	RB	.153	.054	.136	2.847	.005
	LOC	.518	.058	.447	9.007	.000

a. Dependent Variable: IDM

The following outcomes of the regression analysis investigate how different factors affect

Investment Decision Making (IDM).

The regression results indicate that all three independent variables-Availability bias (AB), representativeness bias (RB), and Locus of control (LOC) have a positive significant impact on investment decision-making (IDM). The coefficient for AB is 0.170 means that for every one-unit increase in Availability bias, IDM is expected to increase by 0.170 units. The effect is statistically significant ($p = 0.000$), supporting Hypothesis 1 (H1) that AB positively influences investment decisions. Likewise, the coefficient for RB is 0.153, indicating that a one-unit rise in representativeness bias corresponds to a 0.153 unit increase in IDM. The relationship is significant at $p = 0.005$, confirming Hypothesis 2 (H2) that RB significantly affects investment choices. Most particularly, LOC has the strongest impact, with a coefficient of 0.518, meaning IDM increases by 0.518 units for every unit increase in locus of control. This effect is highly significant ($p = 0.000$), highlighting LOC as the most influential predictor among the three.

In conclusion, the findings reveal that AB, RB, and LOC all positively and significantly influence investment decision-making, with locus of control exerting the greatest effect. These results underscore the critical role of behavioral factors in shaping investors' decisions.

Table 5.2.2
Coefficients of Moderating Variable

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	2.006	.094		21.281	.000
	Int1_AB_LOC	.057	.012	.323	4.904	.000
	Int2_RB_LOC	.060	.011	.348	5.278	.000

a. Dependent Variable: IDM

Int1-AB-LOC p-value is 0.000, below the conventional significance level of 0.05. This finding suggests that Int1-AB-LOC is a powerful predictor of Investment Decision Making, or IDM. The statistically significant and positive effect of Int1-AB-LOC on IDM is further supported by the coefficient $\beta = 0.323$ and t-value of 4.904. Therefore, we accept the H3 that Int1-AB-LOC significantly influences IDM.

The p-value for Int2-RB-LOC is 0.000, which is likewise below the 0.05 threshold, suggesting that Int2-RB-LOC is a statistically significant predictor of IDM. A significant and beneficial impact on IDM is shown by Int2-RB-LOC, with a t-value of 5.278 and a coefficient $\beta = 0.348$. As a result, we accept the H4 that Int2-RB-LOC significantly affects IDM.

Conclusion and implication

The study emphasizes how behavioral biases, including availability and representative biases, have a significant impact on investment decision-making. The quality of investors' decisions is impacted by these biases because they cause them to rely more on heuristics than on objective analysis. The results support behavioral finance theories by highlighting how cognitive shortcuts frequently lead to illogical actions. Investors frequently base their decisions on information that is easily accessible or on stereotypes, which emphasizes the need for efforts to raise awareness and lessen vulnerability to these biases. More logical and successful investing strategies may result from addressing these biases through advisory services and education.

The study's key finding is that locus of control acts as a moderating factor. Investors that have an internal center of control are more confident in their choices, which frequently makes biases more noticeable. This shows people who think they have personal control over results could rely too much on their assessments, which could lead to cognitive errors. People who have an external locus of control, on the other hand, are impacted by outside forces like external opinions or market trends. The psychological complexity of decision-making is emphasized by this duality, which also emphasizes the significance of tailored approaches to deal with these variations.

The results of the study are consistent with Prospect Theory, which contends that investors frequently base their choices on their perceptions of benefits and losses rather than impartial assessments. Heuristics' ability to streamline decision-making is clear evidence that investors' risk tolerance and strategies are influenced by biases. These acts highlight how behavioral finance theories should be used to better understand and forecast investor behavior in unpredictable situations.

Lastly, this study sheds light on Nepalese investors' investment habits and offers a culturally unique viewpoint on financial decision-making. It highlights how biases might have a greater influence in emerging economies where economic difficulties and financial literacy may be more significant. In order to reduce prejudices and promote more logical and knowledgeable investing habits, the findings support investor education initiatives and regulations.

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