

**EFFECT OF BEHAVIORAL BIASES ON INVESTMENT  
DECISION OF MUTUAL FUND INVESTMENT IN NEPAL**

**A Dissertation submitted to the Office of the Dean, Faculty of  
Management in Partial Fulfillment of the requirements for the Master's  
Degree**

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## **Certification of Authorship**

I hereby corroborate that I have researched and submitted the final draft of dissertation entitled “Effect of Behavioral Biases on Investment Decision of Mutual Fund Investment in Nepal”. The work of this dissertation has not been submitted previously for the purpose of conferral of any degrees nor it has been proposed and presented as part of requirements for any other academic purposes. The assistance and cooperation that I have received during this research work has been acknowledged. In addition, I declare that all information sources and literature used are cited in the reference section of the dissertation.

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## Report of Research Committee

Mr. Sachin Pathak has defended research proposal entitled “*Effect of Behavioral Biases on Investment Decision of Mutual Fund Investment in Nepal*” successfully. The research committee has registered the dissertation for further progress. It is recommended to carry out the work as per the suggestions and guidelines of supervisor Asst. Prof. Durga Datt Pathak and submit the thesis for evaluation and viva voce examination.

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## Approval Sheet

We have examined the thesis entitled “*Effect of Behavioral Biases on Investment Decision of Mutual Fund Investment in Nepal*” presented by Miss Melina Rai for the degree of Master of Business Studies (MBS). We hereby certify that the thesis is acceptable for the award of a degree.

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## Abbreviations

AMC	:	Assets Management Company
CAPM	:	Capital Assets Pricing Model
DF	:	Degree of Freedom
EU	:	European Union
fsQCA	:	fuzzy-set Qualitative Comparative Analysis
IPO	:	Initial Public Offering
MF	:	Mutual Fund
NAV	:	Net Assets Value
NEPSE	:	Nepal Stock Exchange
NIDC	:	Nepal Industrial Development Corporation
OTC	:	Over the Counter Market
SEBON	:	Security Board of Nepal
SPSS	:	Statistical Package for Social Science
SRI	:	Socially Responsible Investments
Std.	:	Standard

## Abstract

The aim of this study is to investigate the effects of behavioral biases such as overconfidence, availability bias, herding variables, disposition effect on mutual fund decision in Nepal. The sample was collected using the convenience method and a total of 200 participants participated in the study. In this study, descriptive statistics, analysis of variance, independent sample t-test, correlation and horizontal analysis were used to analyze the data. Research results show that overconfidence, emotional performance and risk aversion have a positive effect on investment decisions, but the herding effect is not significant. Additionally, the results show that financial literacy has a negative impact on overconfidence, emotional distress, risk taking and animal husbandry. This means that a high level of financial literacy can help reduce the impact of these biases on investment decisions. This study provides insight to policy makers, stakeholders and financial institutions in developing policies and strategies to improve financial literacy. It is also useful for researchers and the public as it provides a deeper understanding of behavior and investment decisions. Future research could expand the research by including new independent variables such as shock and recognition bias. Future research could also investigate the effects of other factors, such as age and gender, on the relationship between negative attitudes and investment decisions. Overall, the research highlights the importance of understanding and managing biases in investment decisions and suggests that good financial literacy can help people make informed decisions about investing more.

**Keywords:** behavior bias, overconfidence, disposition effect, herding, risk aversion, financial literacy, investment decision.

# CHAPTER I

## INTRODUCTION

### 1.1 Background of the Study

The aim of this study is to examine the impact of behavioral biases, such as overconfidence, disposition effect, herding, availability bias, and financial literacy, on mutual fund investment decision making. The sample was collected using a convenient method, and 200 respondents participated in the study. A simple method was used to collect the sample and 200 participants participated in this study. Kulal (2022) states that overconfidence positively impacts the investment decision in India. Shah et al. (2018) and Ahmad and Shah (2020) state that investment decision is negatively influenced by overconfidence in Pakistan and that financial literacy moderates the relationships between the overconfidence and investment decisions. On the other hand, Aziz and Khan (2016) present a positive impact of overconfidence on investment. The majority of Nepalese literature (Kadariya, 2012; Rana, 2019; Shrestha, 2020) primarily focused on accounting data, advocacy recommendations, business image, demographic characteristics, and company-specific variables, as well as market data, as variables impacting investment decisions. Furthermore, previous research has focused on only a few areas of investor behavior, with the most of the studies concentrating on cognitive biases. Furthermore, studies such as (Awale et al., 2018; Risal & Khatiwada, 2019) have discovered the existence of herd mentality in the Nepali Stock Exchange. In Nepalese context, Dangol and Shakya (2017) say pattern of investment is different based on financial literacy of investors. Similarly, Dangol (2018) states that female are less risky than male as female prefer safe investment option. There is no significant impact of gender on heuristics, prospect, and market herding and investment performance (Dhungana et al., 2018). Similarly, Dhungana et al. (2022) present availability bias, overconfidence bias, herding bias as variables having significant impact on investment decision. The study utilized descriptive statistics, ANOVA, independent sample t-tests, correlation, and linear regression analysis to analyze the data. The findings of the study suggest that overconfidence, disposition effect, and risk aversion have a significant positive impact on investment decision making, while herding does not have a significant effect. Furthermore, the results indicate that financial literacy moderate's overconfidence, disposition effect, availability bias, and herding negatively.

This means that a high level of financial literacy can help reduce the impact of these biases on investment decisions. This study provides insight to policy makers, stakeholders and financial institutions in developing policies and strategies to improve financial literacy. It is also useful for researchers and the general public as it provides a deeper understanding of behavior and investment decisions. Investors' decisions and earnings reports also affect these choices. Due to the unstable movement of stock prices, investors cannot get the best stock prices and therefore cannot predict future prices based on price history. Dhungana et al. (2022) studied effect of five cognitive biases on investment decision taking investor of Pokhara valley of Nepal using convenience method of sampling, distributing questioner to 196 individual investor taking margin of error of 7% found that, overconfidence bias, availability bias, herding bias significantly affect investment decision however anchoring and regret aversion bias appear to have no significant effect on investment decision. Pandit (2021) conducted survey based research to find association between experience group and behavior bias ( herding bias, investment decision bias, disposition bias, overconfidence bias, optimism bias) and found that optimism bias and herding bias has significant association with experience group similarly, experience group doesn't have significant association with investment decision bias, disposition effect, overconfidence on the other hand, in case of trading frequency and behavior bias researcher found that trading frequency has association with herding bias, investment decision bias, disposition effect, overconfident and bias. Herding Variables Dangol (2018) observed in her article "Gender differences in financial decision- making" that women are less risk tolerant than males. Likewise, gender disparities in financial decisions are higher in the areas of availability bias, , and investment strategy; furthermore, women have lower risk tolerance in areas associated with financial and investment expertise; and ultimately, women substantially underestimate their financial risk tolerance when utilizing the 13 questions developed by (Grable & Lytton, 2003).

## **1.2 Problem Statement**

Behaviorally biased investors typically make poor decisions about fund style and expenses, trading frequency, and timing, resulting in poor performance. Furthermore, trend-chasing appears related to behavioral biases, rather than to rationally inferring managerial skill from past performance. Mutual funds investor's decisions are closely connected to an individual's emotional, personal, social, economic, and employment success. An individual needs to understand the basics of Behaviorally biased investors and use financial resources

appropriately to function well in society at a personal, professional, business and community level. Empirical studies have confirmed the positive association between Behaviorally biased investors and return on investment. Hilgert et al (2003) documented a positive link between financial knowledge and financial. Agarwal et al (2007) show that financial mistakes are most prevalent among the young and elderly, who are also those displaying the lowest amount of financial knowledge and cognitive ability. Various local studies have been done on this line with various findings. Kempson et al. (2008) carried out a study on Measuring and improving financial capability to know more about current levels of financial capability in Nepal, to understand the potential approaches that could be taken to measure financial capability in a less developed nation where most of the population does not use formal banking services and to explore levels of financial inclusion in Nepal.

**Based on the above empirical issue and research gap, the following research questions are raised.**

- a) What are the demographic variables impact in mutual fund and behavior biases investment decision factors of Nepalese investors?
- b) What connection exists between behavioral biases and Nepalese investors' decisions to invest in mutual funds?
- c) What impact do overconfidence, disposition effect, herding, behavioral biases and risk aversion have on Nepalese investors' decisions to invest in mutual funds?
- d) What moderating influence does financial literacy have on the link between availability bias, disposition effect, and overconfidence when it comes to Nepalese investors' decisions to invest in mutual funds?

### **1.3 Objectives of the Study**

The primary goal of the research is to investigate how Nepalese stock market participants' decisions about mutual fund investments are influenced by overconfidence, the disposition effect, herding, behavioral bias, risk, and aversion. The following are the study's particular goals:

- a) To investigate the impact of demographic variables on behavior bias factors on Nepalese investors' decisions to invest in mutual funds.
- b) To investigate how behavior bias factors and investment decisions affect the investment decisions made by Nepalese investors. In Nepal

- c) To examine how availability bias, herding, disposition impact, and overconfidence effect on mutual fund investing decisions in Nepal.
- d) To examine how financial literacy influences the relationships between overconfidence, the disposition effect, herding, and availability bias when it comes to choosing mutual funds to invest in Nepal.

#### **1.4 Hypotheses of The Study**

According to Sahi et al. (2013), individual investors have a variety of preferences and beliefs that influence their choices of financial investments. Instead of highlighting mental deficiencies, these biases show how the investor's mind is structured. Moreover, Kumar and Goyal (2016) explain behavior biases arise in different stages of decision-making process; Furthermore, Sharma et al. (2021) explained human behavior that influences individual investment decisions and its subsequent effect on the market. Based on literature various hypotheses are formulated. In this section only alternate hypotheses are presented.

H1: Investing decisions are positively affected by overconfidence bias.

H2: Investing decisions are positively affected by the disposition effect.

H3: Investing decisions benefit from herding bias

H4: Investment choices benefit from risk aversion.

H5: The association between overconfidence bias and investment decision-making is impacted by financial knowledge.

H6: The association between the investment choice and the disposition impact is affected financial knowledge.

H7: The association between herding bias and investment decision-making is affected by financial knowledge.

H8: The association between risk aversion and investment decision-making is moderated by financial knowledge.

#### **1.5 Rationale of the Study**

This work aims to evaluate and comprehend the recent behavioral finance literature that has been offered by earlier scholars. The study considers the eleven years' worth of articles from reputable indexed journals on behavioral biases: prospect rules (like regret aversion, loss aversion, and mental accounting) and heuristics rules (like availability bias, overconfidence, representative bias, and anchoring) that affect investors' financial

decision-making. The body of research now available demonstrates how several psychological fallacies and objective elements like risk, return, safety, etc. influence the process of making financial decisions. Going forward, it is possible to investigate whether of the subjective or objective elements influencing investment decisions is the most important. And the review of selected papers suggested a significant gap in identifying the impact of prospect and heuristics on the selection of available investment avenues. The study would help make the investors aware of the behavioral biases and select the investment product which suits their investment objective and risk appetite. This might be very useful to Policy makers:

The Policy makers will benefit immensely by having information on formulated of investment advice which are fund style and expenses, trading frequency, and timing. Due to the research findings, policy makers will be able to use the gaps in the literacy of the respondents to formulate appropriate education syllabus to increase financial investment literacy leading to better financial decisions. This is important as shown by Bernheim and Garrett (2003) who argue that seminars are often remedial, that is offered in firms where workers do little or no investment. Investors: The study will be invaluable to investors who would benefit from it in that they could make more informed investment decisions while investing in mutual funds, employees and employers. Strategies can be formulated to promote savings for wealth creation and retirement like to automatically enroll workers into employer-provided pension plans. This simple but ingenious method has been proven to be very effective in increasing pension participation. For example, according to Madrian and Shea (2001), after a company implemented a change in its pension plan. The purpose of this paper is to review and understand the current literature on behavioral finance contributed by previous researchers. From reputed indexed journals, the articles of 11 years on behavioral biases: heuristics rules (such as representative bias, overconfidence, anchoring, and availability bias) and prospect rules (such as regret aversion, loss aversion, and mental accounting) impacting financial decision-making of investors are considered for the study. The present literature proves that the financial decision-making process is impacted by various psychological illusions and objective factors like risk, return, safety, etc. Moving further, there is a scope to explore the most prominent factor among the subjective or objective factors impacting investment decisions. And also, the review of selected papers suggested a significant gap in identifying the impact of prospect and heuristics on the selection of available investment avenues. The study would help make the

investors aware of the behavioral biases and select the investment product which suits their investment objective and risk appetite.

### **1.6 Limitations of the Study**

During the research process, the following difficulties were encountered by the study: Due to client confidentiality and apprehension about being exposed to competition, mutual fund companies in Nepal typically do not wish to provide information. The topic might not be interesting to some of the responses. Furthermore, because they believed the information to be important for competition, some respondents would not want to provide it. Given that the respondents are typically extremely busy, it's possible that they didn't have much time to answer questions. It was not feasible to include additional respondents in the study due to time constraints. To improve the study's representation of mutual funds in Nepal and provide a more thorough examination of the consistency of the details provided. The researcher did, however, explore the material for contradictions, but she was unable to find any. If a different model had been applied to the analysis, the data might have produced different conclusions. It's possible that the sample did not fully represent registered mutual fund companies. It's possible that various sampling techniques produced different outcomes.

## **CHAPTER II**

### **LITERATURE REVIEW**

Because of the unpredictable nature and volatility of the stock market, mutual funds are a sort of retail investment designed for those who do not wish to participate directly in the stock market. A mechanism known as mutual funds is used to pool the contributions of novice investors and have fund managers professionally manage them in order to provide a steady return and capital growth. They have proven to be a valuable resource for retail investors. Moreover, Raut (2020) study past behavior, financial literacy and investment decision making process of individual investors and found financial literacy has significant effect on attitude and perceived behavior control which affect investment decision on investors. Likewise, Al-Tamimi and Kalli (2009) studied financial literacy on investment decision taking UAE investors and found financial literacy is affected by income level, education level and workplace activity, adding significant difference on financial literacy level based on gender. In South Asian context studies like Parveen and Siddiqui (2018) explain a positive effect of disposition effect and a negative effect of overconfidence on investment decision. According to Cao et al. (2021), investment decision is impacted positively by herd behavior in Vietnam. Madaan and Singh (2019) state that overconfidence and herding bias have significant positive impact on investment decision in India. Kulal (2022) states that overconfidence positively impacts the investment decision in India. Shah et al. (2018) and Ahmad and Shah (2020) state that investment decision is negatively influenced by overconfidence in Pakistan and that financial literacy moderates the relationships between the overconfidence and investment decisions. On the other hand, Aziz and Khan (2016) present a positive impact of overconfidence on investment. Likewise, as per Hayat and Anwar (2016), financial literacy has a negative moderating influence in herding bias and a positive moderating effect in overconfidence bias with investment decision. Most of the Nepalese literature (Kadariya, 2012; Rana, 2019; Shrestha, 2020) primarily focused on accounting data, advocacy recommendations, business image, demographic characteristics, and company-specific variables, as well as market data, as variables impacting investment decisions. Furthermore, previous research has focused on only a few areas of investor behavior, with most of studies concentrating on

cognitive biases. Furthermore, studies such as (Awale et al., 2018; Risal & Khatiwada, 2019) have discovered the existence of herd mentality in the Nepali Stock Exchange. In Nepalese context, Dangol and Shakya (2017) say pattern of investment is different based on financial literacy of investors. Similarly, Dangol (2018) states that female are less risky than male as female prefer safe investment option. There is no significant impact of gender on heuristics, prospect, and market herding and investment performance (Dhungana et al., 2018). Similarly, Dhungana et al. (2022) present availability bias, overconfidence bias, herding bias as variables having significant impact on investment decision. However, anchoring and regret aversion bias has no significant effect on investment decision. Likewise, Pandit (2021) states that experience group has significant association with herding and optimism biases. Therefore the statement of the study is to study the impact of behavior bias (overconfidence, herding, disposition effect and risk aversion) on investment decision of male and female investor of Nepalese stock market taking financial literacy as moderated variable could strengthen, diminish, negate, or alter relationship between behavior bias and mutual fund investment decision. In this scenario we look at how mutual funds are structured and what types of investments the funds hold. Mutual funds can be structured in two ways. They are open end funds and closed end funds.

### **Closed-end Funds**

An investment fund that operates with a fixed number of existing shares is known as a closed-end investment business. This type of fund raises capital for investments by first selling its shares to the public through an IPO. Following a sale, the issuing company often prohibits stock redemption. When a closed-end fund sells its current stock, it often does not allow investors to buy further shares. The fund's capitalization and number of shares are therefore fixed for the period. Usually, the closed-end fund has a specified maturity period of five to fifteen years. Shares of closed-end funds are traded on reputable stock exchanges or over-the-counter (OTC) marketplaces. It was basically traded at market prices, which are either more or lower than its net asset value (NAV), depending on the circumstances. Shareholders of closed-end funds swap shares on an exchange. Compared to open-end funds, closed-end fund shares are less liquid.

### **Open-end Funds**

An investment that lacks a defined capitalization and maturity time is an open-end mutual fund. Continually based on the current net asset value (NAV), open-end investing businesses are prepared to acquire or sell shares at any moment. Every day, the NAV is computed. The corporation issues fresh fund shares to satisfy the purchase orders placed

by investors who acquire shares in open-end funds. Open-end fund shares can be redeemed at any moment. Because they assured investors that they could always redeem their shares for their NAVs, it gained popularity very rapidly. Due to the company's pledge to redeem shares upon demand, they only invest in highly liquid assets that can be swiftly traded, such as stocks and bonds. Open-end fund shares are exchanged via the company's agents. In essence, open-end fund shares are traded at NAV; but, if they were exchanged through agents, the price that was offered would be traded. Mutual funds can be divided into equities (stock) funds, bond funds, fixed-income funds, or hybrid funds—a blend of all three—based on their investing philosophies. The money that equity funds invest goes toward purchasing and selling shares, or stocks, of publicly traded corporations. Bond funds and fixed-income funds allocate their capital to fixed interest deposit accounts and corporate and government bonds, respectively. All the together is known as a hybrid fund. Bonds, fixed income deposits, and stocks are all invested in by hybrid funds. You can make investments in accordance with your willingness to take on risks. Most of the research depicts Indian investors' experiences with mutual funds. Research on Nepalese investors' perceptions of mutual funds is quite scarce. Because mutual fund investors are often small investors, there hasn't been any extensive research done on them in Nepal.

## **2.1 Theoretical Review**

The theoretical study will begin with an examination of the ideas that served as the foundation for both conventional finance and the emergence of behavioral finance. The Efficient Market Hypothesis, Heuristic Theory, and Prospect Theory are the ideas that will be examined in this research. These theories will provide a clear explanation of the connection between behavioral biases and the process of choosing investments.

### **2.1.1 Overconfidence Bias**

Odean (1999) described that investors with lower brokerage Trading account become more confident and engage in excessive trading. (Pompian, 2006) outlined Overconfidence as a degree of unjustified faith in one's natural reasoning, judgments, and psychological abilities. It is a tendency of investors to overestimate their skills to forecast an occurrence, faithfulness of information and knowledge. Under the effect of overconfidence, investors may become certain of having clear-cut information and they may think that they are smarter than other investors. When investors are too sure about the judgment they are going to make, it is known as certainty overconfidence. When investors show fine confidence

intervals to their investment assessments it is known as prediction overconfidence. Both type of overconfidence i.e. certainty and prediction can lead to investment mistakes that cause damage to any investor's portfolio. It is the investigation of financial market data that has shown a turning point in overconfidence research in the field of finance. The broadly cited work of Terrance Odean and the co-authors (Sec: Oden1999, Barber, Odean2000;2001), studying the trading patterns of individual investors trading taken from a large US brokerage firm, allowed overconfidence to progress from an ignored psychological side effect to a broadly accepted factor influencing the financial decision making of any investor. The fact that excessive trading may be tried among others by the lower performance of active traders who take the high number of trades as the comparison to those who trade very less in number. Such results are demonstrated by barber and Odean (2000) on the data of 35000 US households between 1991-1997, the trading accounts with the highest turnover are the lowest performers. By analyzing that the connection between overconfidence and high-volume trading is established on the same data set by barber and Oden (2001).

### **2.1.2 Overconfidence and Investing**

Investing, which may be complex and require long-term projections, directly benefits from overconfidence. Investors that are overconfident might underestimate their capacity to identify profitable ventures. Conventional financial theories advocate for diversified portfolios; nevertheless, misplaced confidence may work against this advice, leading an investor or their financial adviser to place their faith in a single asset rather than diversifying their holdings. Odean (1998) explained that the overconfident investors take more trades than the rational investors which lower their anticipated utilities. Hence, more overconfidence leads to excessive trading and lower anticipated utility. Overconfidence not solely increases the trading activity, but it also makes the investors way too certain about their feelings. They disregard the opinions of others resulting in no uniformity of investor beliefs. Oden 1998 developed models in which overconfident investors overestimate the accuracy of their information concerning the value of financial security. He witnesses that they overestimate the possibility that their personal valuation of the securities value is more exact than the valuation of others. Overconfidence could also be driven by another characteristic referred to as "self-attribution bias". In opinion, this implies that individuals faced with a positive outcome, following a choice, can read that outcome as a result of their capability and professional skills, and once they face a loss, this point to bad luck or loss.

Daniel, Hirshleifer, and Subramanian (1998) introduced a theory for investor's overconfidence where variations in confidence level result from a self-attribution bias of investment results. According to the theory, underreacting to public information, the investor overstates signals from non-public information. Consequently, an investor who overestimates the trustworthiness of non-public information signals—rather than information signals that are widely received—is considered overconfident.

### **2.1.3 Representativeness Bias**

Tversky and Kahneman (1983) Representativeness appears when investors get confused due to the conditional chances. By investigating the possibility of a particular event or occurrence belonging to the other event or occurrence is strong or not representativeness can be tested. Representativeness is clearly visible while making decisions under uncertainty when investors think that situation A belongs to situation B. (Tversky and Kahneman, 1981: in O'Hagan et al, 2006). Ritter (1991) noticed another fascinating consequence of a decision made under Representativeness bias where investors sale the poor performing IPOs in short-term. While creating investments, individuals believe that the favorable events for a company are also favorable for its stock and such companies turn (Lakonishok et al, 1994).

### **2.1.4 Availability Bias**

Tversky and Kahneman (1973) The availability heuristic, a distinctive psychological strategy in human decision making, clarified with an example of how the method of deciding influences the analysis of related actions. People's decision of the chance and the occurrence of the actions are built on the easiness with which the examples of those events come to the mind. Tversky and Kahneman (1974) Availability is a judgmental heuristic in which a frequency of a closed event is assessed on how informal it is to recall its retrievability, how easy it is to mentally construct its ability to imagine or how easy to subordinate two different occurrences. Tversky and Kahneman (1974) the writer analyzed availability, as a heuristic that uses the strength of association between occurrences to access their probabilities. According to Pompian (2012), availability is a bias in which people take a heuristic (additionally grasp as a rule of thumb or a mental shortcut) method to estimate the chance of an outcome based on hope. Effectively reviewed results are regularly seen as being insignificant likely than that are harder to review or see, thus recent ongoing events are considerably more effortlessly recalled and accessible. Agrawal (2012) keeps up those numerous times, individual behave irrationally and their investment choices are biased.

### **2.1.5 Farming Biases**

The propensity of decision-makers to react differently to different circumstances depending on the context in which a choice is given (or framed) is known as framing bias. Examples include the way data is shown in tables and charts, the way numbers are depicted, and the way news is distributed and presented through text and video. Narrow framing is a sub-categorical phenomenon that falls under the umbrella of framing bias. It is characterized by people focusing too narrowly on one or two parts of a situation, consequently excluding other important components and impairing their ability to make decisions.

### **2.2 Empirical Review**

Dhungana et al. (2022) studied effect of five cognitive biases on investment decision taking investor of Pokhara valley of Nepal using convenience method of sampling, distributing questioner to 196 individual investor taking margin of error of 7% found that, overconfidence bias, availability bias, herding bias significantly affect investment decision however anchoring and regret aversion bias appear to have no significant effect on investment decision. Several explanations have been offered for these two anomalies. Carlin (2009) explains participation in high fee index funds using a model with search costs. he purpose of this research is to supply basic statistics of fees and expenses charged by mutual funds in Thailand, and to investigate the economic determinants of the variations in these charges. The authors have taken the dataset from 2005 to 2007. Smaller funds with more investment risk and a range of income tax benefits are available, but they often come with higher costs and overhead. This essay discusses the expanding body of research that looks into the characteristics of asset management firms outside of the United States and Europe. The results show that mergers do not correlate with increased money flows or investor investment. Usually, before and after the company combines, individual investors withdraw their money from their stakes. Merger theories state that rational investors should support mergers as they are frequently viewed as beneficial and essential for the financial industry.

Louhichi Wael (2004) examined the market behavior around the times of annual earnings announcements made in the Paris Bourse to study both the informational role of accounting numbers and the intraday speed of adjustment of stock prices to new information. Davar and Gill (2007) in their paper on investment decision making revealed that 22 the class of

investors(undoubtedly) with growing age develop maturity and experience for making decisions about the usage of their surplus and available funds in the light of overall economic needs of family. Adam (2008) in his study on efficient market hypothesis to behavioral finance analyzed how investor's psychology changes the vision of financial markets. He found that investors are not always able to correctly value the utility of decision alternatives, cannot update and estimate probability and events and do not diversify properly. Giridhari Mohanta and Sathya Swaroop Debasish (2011) studied that investors invest in different investment avenues for fulfilling financial, social and psychological needs. Goetzmann and Peles (1993) have argued that the same theory of cognitive dissonance could explain the observed phenomenon that money flows in more rapidly to mutual funds that have performed extremely well than flows out from mutual funds that have performed extremely poorly: investors in losing funds are unwilling to confront the evidence that they made a bad investment by selling their investments. When choosing which mutual funds to buy or sell, investors in mutual funds frequently rely on straightforward decision heuristics. In the investment industry, namely the NSE, behavioral variables have been seen to be at play locally. The numerous IPOs and other securities issues amply illustrate this. The not so good outcomes of this have led to poor participation in subsequent IPOs notably Eveready E.A and BRITAK. Wera (2006) conducted a survey on the influence of behavioral factors on investors at the NSE by targeting 100 individuals and 40 institutional investors. The results found that many investors will gamble by holding the stocks for a month with the prospect of breaking even. A considerable percentage chose to sell now to minimize losses, loss aversion theory. The preference for holding stock indicates that all investors are risk averse. Another study by Waweru et al (2008) investigated the role of behavioral finance and investor psychology in investment decision-making at the NSE. Quantitative research was done on the sample size of 339 investors through telephonic interview. They found that information sources and selection criteria employed, and investor behavior are interrelated. Numerous significant aspects are included in the research analysis, such as fund marketing, mutual fund services, intermediary function, fund performance, fund quality, and investor base expansion. The investor's primary consideration when selecting a fund is its quality, which is closely followed by mutual fund services and agent intermediary services. The study sheds light on the process by which investors select different funds depending on historical performance. Stated differently, the success of upcoming innovations in the financial industry is primarily determined by the demands and expectations of investors, who place a high value on investor-oriented service

quality systems. Qureshi, Kutan, Ismail, and Gee (2017) examined the relationship between stock market volatility and mutual fund flows in emerging markets in Asia by employing a panel VAR model. A positive relationship was found to exist between equity fund flows and market volatility, whereas market volatility moves inversely with movements in balanced fund flows. Prosad, Kapoor and Sengupta (2015), studied on the Behavioral biases of Indian investors: a survey which was conducted in New Delhi, India. They have examined that the presence of Behavioral biases among Indian investors namely disposition effect, overconfidence, recency, loss aversion and herding Behavior. The paper gives an insight and overview on the investors profile corresponding to various biases under it.

*Table 1: Summary of Emperor Review*

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
1	R and Christie (2019)	explored the influence of investors' annual income on the behavioral biases exhibited by them	anchoring, availability, mental accounting, gambler's fallacy, regression aversion, representativeness	Data collected from 436 equity investors in Chennai through pre-structured questionnaires	Annual income of investors had a significant effect on Mutual fund investment.	The study examines annual income but may not account for other demographic factors such as age, education, gender, and occupation. Investigating how these additional factors influence behavioral biases could provide a more nuanced perspective.

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
2	Qureshi, Kutan, Ismail, and Gee (2017)	relationships between stock market volatility and mutual fund flows in emerging markets in Asia	market volatility	a panel VAR model	A positive relationship was found to exist between equity fund flows and market volatility	market volatility moves inversely with movements in balanced fund flows
3	Mishra and Metilda (2015)	studying the impact of investment experience and level of education on two specific biases: overconfidence and self-attribution	Gender, education level of education on two specific biases	Gender, education level of education on two specific biases	confidence is highest among men than women and it increases with investment experience and education.	Exploring a broader range of biases (e.g., loss aversion, framing effects) could provide a more comprehensive understanding of how different biases interact and influence investment decisions.
4	Prosad, Kapoor and Sengupta (2015)	studied on the Behavioral biases of investors:	Indian investors namely disposition effect, overconfidence, recency, loss aversion and herding Behavior	Survey	the individual investors make more investment mistakes and result in stronger Behavioral biases	Delving deeper into the psychological mechanism underlying each bias (e.g.,

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
					when stocks are more difficult to value it.	cognitive dissonance for disposition effect, risk perception for loss aversion) could enhance understanding beyond surface-level observations
5	Aydogan, Vardar, and Tunc (2014), Turkish	dynamic relationship between mutual fund flows and stock returns	stock market	Questionnaire Among 980	existence of a long-run relationship between all categories of mutual fund flows and stock returns	The study focuses on the long-run relationship between mutual fund flows and stock returns. Investigating the short-term dynamics and volatility in this relationship could provide insights into market reactions to immediate flow changes.

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
6	Bashir (2013)	studied the influence of behavioral biases	overconfidence bias, loss aversion propensity, availability bias and confirmation bias	questionnaire to understand , 100 responses were collected,	the study found no significant relationship in the responses given by both male and female decision making regarding overconfidence bias. Also, results showed a weak negative correlation among the biases being studied.	The study collected only 100 responses, which is relatively small. Increasing the sample size could enhance the reliability and generalizability of the findings.
7	Lamphun and Wongsurawat (2012) Thailand	the purpose of this research is to supply basic statistics of fees and expenses charged by mutual funds in Thailand, and to investigate the economic determinants of the	economic determinants	dataset from 2005 to 2007.	Funds which are small in asset under management and have higher risk of investment and offer different types of income tax benefits along with expenses and higher charges	Assessing how mutual fund fees in Thailand relate to risk adjusted performance metrics (e.g. Sharpe ratio alpha) could provide insights in whether higher fees are justified by superior fund performance.

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
8	Accordi ng to Pompian (2012),	variation s in these charges. illusion of control bias	choices, tasl familiarity, competition and activ involvement	Sampling	people tend to believe that they can control or influence outcomes t when, in fact, they cannot	Investigating : there are differences illusion of bias and how differences in ent decision-could insights into specific ral patterns.
9	Bailey, Kumar and David Ng(2011 )	studied the behavior al biases of mutual fund investors	Investors (gambler, smart, overconfident, narrow frame and mature)	Sampling	Behavioral ly biased investors always take poor decisions about fund choice resulting in expenses and thereby poor performanc e	Quantitativ ely assessing the impact of each behavioral bias on fund choice, expenses, and performanc e could provide a clearer understandi ng of the economic consequenc es of biased decision-making in mutual fund investing.
10	Sahi and Arora (2010)	made explorat ory research, to explore	overconfidenc e biases, self reliance experts, categorization	A total of 377 respondent s, using eight biase.	Novice learners are the ones who are comfortabl e with	The study might be geographic ally limited. Expanding

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
		on biases among individual investors	tendency, budgeting tendency, adaptative tendency, socially responsible investing bias and spousal effect.		advice from experts follow the advice of herd and behave based on the expertise advise.	the research to include multiple regions or countries could provide a more comprehensive understanding of investor biases across different cultural and economic contexts.
11	Parihar et al. (2009)	Examined the impact of different demographic variables on the approach of investors towards mutual funds.	Demographic variables	Questionnaire Among 1400	Revealed that the mainstream of investors still not formed any outlook towards mutual fund investments	The study does not consider how investor attitudes towards mutual funds might change over time or in response to different economic conditions.
12	Wera (2006)	conducted a survey on the influence of behavioral factors on investors	promotion of fund, service of companies with mutual fund, intermediary role, fund performance, quality of fund along with the	Survey (100 individuals and 40 institutional investors)	most investors will gamble by holding the stocks for a month with the prospect of	Assessing the implications of observed behavioral factors and biases for regulatory policies

S. N	Author	ROs/RQs	Variables	Methodology	Finding	Gap
		at the NSE by targeting 100 individuals and 40 institutional investors	growth of investor base		breaking even	aimed at investor protection, market stability, and promoting fair practices in financial markets.
13	Madhusudhan V Jambodekar (1996)	study to size-up the direction of mutual funds in investors and to identify factors that influence mutual fund investment decision	open-ended scheme, income schemes and open-ended	Newspapers are used 102 Journal of General Management Research as information source	open-ended scheme is most favored among other things and that income schemes and open-ended schemes are preferred over closed-ended and growth schemes.	The study has not looked deeply into the psychological factors and biases influencing investor decisions.
14	(N Capon, 1996)	Comprehend the buying viewpoint of consumers and the decision of mutual fund investors	consider and factor mutual investment	risk return function sample size of 3386 investors through telephonic interview	Quantitative research was done on the selection criteria employed, and investor behavior are interrelated	They found that information sources and selection criteria employed, and investor behavior are interrelated. The study has primarily focused on a specific geographic region, potentially ignoring cultural and regional differences in investment behavior.

### **2.3 Research Gap**

Further research is required to examine the moderating effect on the relationship between cognitive biases and investment decision-making in Nepal, despite the fact that several studies have examined the impact of cognitive biases on investment decision-making in Nepal (Bhattarai & Dhungana, 2020; Koirala, 2018) and the role of financial literacy in investment decision-making (Shrestha & Shrestha, 2014). R and Christie (2019) investigated the relationship between investors' yearly income and the behavioral biases they displayed; however, there is a research gap because the study only looks at annual income and may not take other demographic aspects like age, gender, education, and employment into consideration. Examining the ways in which these extraneous variables impact behavioral biases may offer a more complex viewpoint. additional factors influence behavioral biases could provide a more nuanced perspective. Mishra and Metilda (2015) investigated the influence of gender, educational attainment, and investing experience on two distinct biases: self-attribution and overconfidence. However, there exists a research void in this area. A more thorough knowledge of how various biases interact and affect investing decisions may be obtained by investigating a wider spectrum of biases, such as loss aversion and framing effects. Beyond cursory observations, a thorough exploration of the psychological mechanisms underpinning each bias (e.g., risk perception for loss aversion, cognitive dissonance for disposition effect) might improve comprehension. R and Christie (2019) investigated how investors' yearly income affected their behavioral biases. Overconfidence, mental accounting, loss aversion, availability bias, Herding Variables, disposition effect, and representativeness.

## **CHAPTER III**

### **RESEARCH METHODOLOGY**

This chapter deals with the methodology which shows the effect of behavioral biases on mutual fund investment decision in Nepal. Here for the study purpose, the impact of behavioral biasness has been assessed by two ways one is through reviewing various research papers, published article, journal, conference, working papers etc, and the other way is through the questionnaire data. Data has been collected from the various investors in Nepal, through a designed questionnaire. This questionnaire is divided into four parts. Part-a talks about the demographic profiling of the respondents, part-b talks about the existence of behavioral finance dimensions, part-c and part-d talk about the questions related to behavioral finance dimensions and investment decision making. There are numerous related questions, in total to gauge the responses of the respondents (investors). A few books related to the subject have also been considered while writing or framing the concept. In general, there are many behaviors however biasness, for the study purpose only three behaviors have been studied and these behaviors are as follows over confidence, herding and disposition effect.

#### **3.1 Research Design**

The study's research design is mostly descriptive, while explanatory research types are also acceptable. A descriptive research design aids in describing the current condition of affairs, events, and circumstances. The purpose of descriptive research is to identify and characterize the properties of variables of interest. Furthermore, one or more factors are explained using the explanatory study design, which is frequently used to highlight the importance of the link between investors' perceptions and independent variables that influence investment decisions. Naturally, data from descriptive research may also be analyzed to test hypotheses, and data from an analytical study can also be studied in a descriptive manner. The primary data for this investigation were obtained. Structured questionnaire surveys are employed as a data collecting strategy.

### **3.2 Population and Sample, and Sampling Design**

The study's population consists of all Nepali investors in mutual funds. These answers represent a variety of investor demographics, including retirees, working adults, students, and company owners. Convenience sampling was used in this work to get data from the study's respondents. More than 200 questionnaires were sent to mutual fund investors throughout Nepal, both in person and online, for the study.

### **3.3 Nature and Sources of Data,**

Primary as well as secondary sources of data are employed in this investigation. The core data were collected from respondents in Nepal using a structured questionnaire survey that involved 200 individual investors both in-person and online. A structured collection of questions intended to elicit replies or answers from respondents on a certain topic is called a questionnaire. The purpose of this questionnaire is to gather information on the respondent's perceptions, views, and actions.

### **3.4 The Instrument of Data Collection**

The targeted population's primary data was gathered through the use of questionnaires. 200 individual investors are the source of funding for the study's delivery of pertinent data. Additionally, this study has gathered pertinent secondary data from a variety of publications, including periodicals, journals, published reports, research theses, and the internet, in order to track the performance of mutual funds. This study's primary goal is to determine how well-informed individual investors are when it comes to making mutual fund investments. The chosen method for gathering the necessary primary data is a questionnaire. The selection of a questionnaire as the survey instrument was motivated by factors such as its greater dispersion, gradual decline in distribution, and response bias, in addition to its cost-effectiveness, speed of data collection, sample size, time, and ease of communication. In order to assess a questionnaire's strength and gain further knowledge, it is important to first carefully review questionnaires from earlier studies. This is because, in hindsight, even many well-known instruments appear incredibly flawed. The reference and extant literature also offered guidance on how to create a suitable questionnaire for the investigation. It is anticipated that the constructs will address the fundamentals that are absolutely necessary to provide answers to the research questions. These include the respondents' mutual fund investor profile, their awareness of mutual funds, the factors that influence their investments in mutual funds, their level of risk tolerance, their attitude

toward fund selection, the impact of behavioral factors, and their response to fund performance. The survey instrument's data collecting method is self-administrative in character, and the researcher assisted the respondents directly throughout that procedure. The information contained in the questionnaire was created using data that is freely and commercially accessible from academic institutions, investment companies, and other publicly accessible documents. Examining these types of historical research documents has the benefit of covering subjects that were not covered in previous studies. The surveys are provided in English, and any questions that the respondents may have about filling them out or about reading, understanding, or any other language barrier are carefully explained.

94 There are eight sections in the construction of the survey instrument. The first component looks up the respondents' and mutual fund investors' demographic profile.

Table 2: Measurement of Variables

Variable	Items	Source	Expected sign
Overconfidence	5	Barber and Odean (2008)	Positive
Disposition Effect	8	Odean (1999), Grinblatt and Keloharju (2000) Barber and Odean (2001)	Positive
Herding bias	5	Bikhchandani et al. (1992), Chang e	Positive
Investment Decision	5	Barber and Odean (2008)	Positive
Availability Bias	5	Kahneman and Tversky (1979)	Positive

The basic regression model to analyses the impact of behaviour bias on investment decision is:  $ID = \alpha + \beta_1 O + \beta_2 H + \beta_3 DE + \beta_4 R + \varepsilon$  (i)

here  $\alpha$  denotes the intercept term,  $\beta$  ( $\beta_1, \beta_2, \beta_3, \beta_4$ ) denotes the regression coefficients, while ID, O, H, DE, and R represent investment decision, overconfidence, herding,

disposition effect, and risk aversion likewise,  $\varepsilon$  represent error term. Similarly, for moderating effect of financial literacy (FL) following are the model.

$$ID = \alpha + \beta_1 O + \beta_2 FL + \beta_3 O * FL + \varepsilon \quad (ii)$$

$$ID = \alpha + \beta_1 DE + \beta_2 FL + \beta_3 DE * FL + \varepsilon \quad (iii)$$

$$ID = \alpha + \beta_1 H + \beta_2 FL + \beta_3 H * FL + \varepsilon \quad (iv)$$

$$ID = \alpha + \beta_1 R + \beta_2 FL + \beta_3 R * FL + \varepsilon \quad (v)$$

### 3.4 Data Collection

The primary data collection instrument for this study was a questionnaire, which was used with the purpose of gathering data. One of the most important and useful methods of data collection was the distribution of questionnaires to individual investors. The information gathered from these surveys was subjective, despite efforts to provide a picture of the study from a variety of perspectives and levels. To foster a relationship and encourage responses, the questionnaires are supplied separately. The data gathering procedure may provide an explanation for any suspicions or uncertainties regarding the answers to the questions. When used on groups of respondents, this technique is less expensive and verifies a full response. Through the mutual fund website, secondary data is gathered for additional examination and interpretation.

### 3.5 Method of Analysis

To provide an overview of the participants' demographics, descriptive statistics were calculated. The associations between overconfidence, the disposition effect, herding, and risk aversion on investment decisions were next investigated using hierarchical linear regression, holding constant the demographic variables. The PROCESS macro was used to test for the moderating impact of financial literacy. This made it possible to determine the moderation effect's magnitude and direction as well as the importance of the interaction term between the moderator and predictor factors. To provide an overview of the participants' demographics, descriptive statistics were calculated. The associations between overconfidence, the disposition effect, herding, and risk aversion on investment decisions were next investigated using hierarchical linear regression, holding constant the demographic variables. The PROCESS macro was used to test for the moderating impact of financial literacy. This made it possible to determine the moderation effect's magnitude and direction as well as the importance of the interaction term between the moderator and predictor factors.

### 3.6 Research Framework and Definition of Variables

The main behavioral bias variables and their influence on mutual fund invest decisions are covered by this study paradigm. This study can help investment analysts and brokerage business managers better understand how investors behave in the stock market. They can frequently instruct their clients on how to become profitable investors. The main finding of the study is that the hypotheses and the theoretical model are well supported by the data used in this investigation. This study promotes constructive debate among academic practitioners about theory and proposition, measuring scheme, research methodology, and management implications.

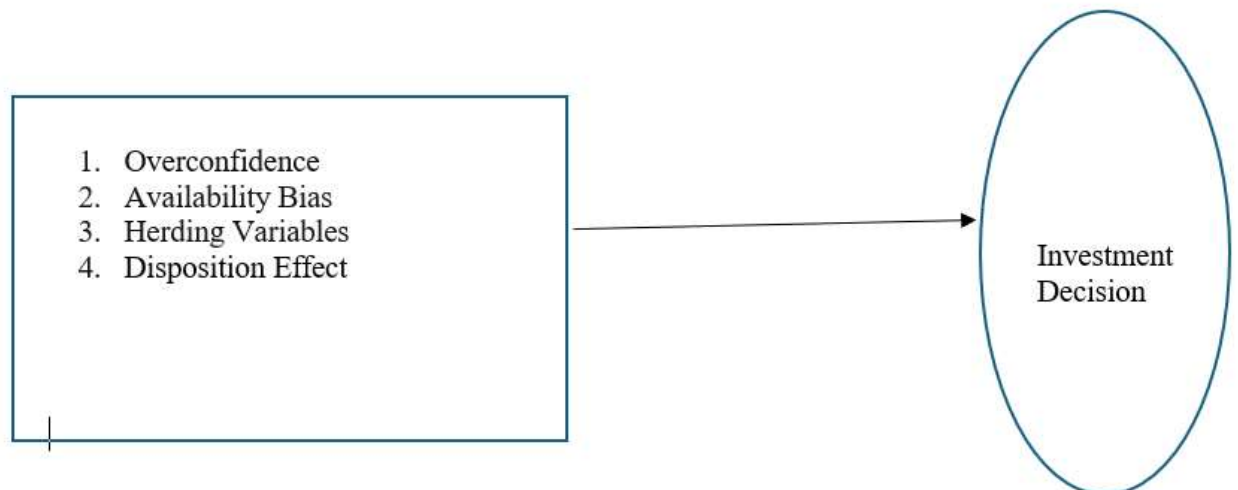


Figure 1 :Research Framework (modified from Adil et al., 2021)

#### 3.6.1 Overconfidence

Overconfidence is a psychological attribute that significantly influences individual investing decisions in the field of behavioral finance. Those decisions can be stock market investment decisions or other investment decisions (Joo, 2017). In behavioral finance, overconfidence mirrored as a common psychological bias, which makes financial markets inefficient by creating mispricing in the form of massive volatility and return variability (Ko & James Huang, 2007). Overconfidence has been defined in a variety of literary works, however the following definition provides a clearer understanding of the term. Overconfidence is a psychological bias that leads an investor to overestimate the importance of a given parameter and assumes that a person's assessments are flawed and deteriorated. With those judgments, an individual would never learn the correct distribution (Dubra, 2004). During overconfidence, it observed that average mutual fund manager underperforms the market (Gruber, 1996). In the realm of economics, overconfidence has not received much attention despite abundant evidence that it is widespread. Much attention and broad applicability of overconfidence bias have been found in the behavior of rational

agents (Dubra, 2004). Researchers argue that overconfidence bias is often directed by the neglect of unknowns (Walters, Fernbach, Fox, & Sloman, 2016). It documented that increased overconfidence leads to excessive trading volume and higher price volatility in stock markets (Graham, Harvey, & Huang, 2009); (Nir Jaimovich and Sergio Rebelo, 2007).

### **3.6.2 Disposition Effect**

Barber and Odean (1998), Shefrin (2000) describe disposition effect as a phenomenon in which investors tend to grip on to losing investments for too long and sell winning investments too primary. However, Kahneman and Tversky (1984) defined disposition effect as a tendency for investors to overvalue investment that they have made and sell them too late.

### **3.6.3 Availability Bias**

A cognitive bias known as availability bias arises when people base their decisions on information that is easily accessible to them rather than looking for extra information that could be more accurate or relevant. Decisions made as a result may be skewed or faulty since the information at hand may not always be accurate.

### **3.6.4 Herding Behavior**

In the financial market, a typical occurrence to see is herding. Humans often refer to, watch, and mimic the actions of others when there is instability in the financial markets (Yu, Dan, Ma, & Jin, 2018). Investors draw illogical conclusions regarding their investments when herding is prevalent. They would prefer to take other investors' opinions and ideas into consideration when making investing selections. Because of this, investors often take the lead from others and show restraint when they feel heard. The herding effect is more pronounced when there are market distress indicators, such as price bubbles, rumors, and anomalies (Mertzanis & Allam, 2018). Herding has been described as a confluence of actions resulting from collective imitation (Philippas, Economou, Babalos, & Kostakis, 2013). Numerous studies have also demonstrated how herding behavior may cause people to move in similar ways and suffer significant welfare losses. One of the study publications defines herd behavior in a novel way: if agents are allowed to approach their network neighbors' tactics, the game outputs observable investment decisions and the network structure is impacted. Anticipated regret quality of the market or stocks that people have while making investment selections is the activity to prevent such outcomes.

## CHAPTER IV

### RESULTS AND DISCUSSION

The findings of the data analysis are shown in this section. Regression analysis and correlation coefficients were used to analyze the research variables, combining descriptive and inferential statistics. The purpose of these analyses was to evaluate the study's Hypothesis and respond to the research question. The primary goal of the study is to ascertain how behavioral biases affect mutual funds in Nepal. The study findings were examined in this part, and SPSS was used to analyze the data. Regression analysis and descriptive statistics were used to summarize the findings.

#### 4.1 Response rate

A variety of questionnaires were distributed to Nepa's mutual fund investors both in-person and online. Every investor agreed to reply to my request.

Table 3: Response rate

Response Rate	Distribution	
	Frequency	Percent
Responded	200	100
No Response	0	
Total	200	100

#### 4.3 Background Information

The background information from the respondents included their age, gender, level of education, years in unit trust investments and type of unit trust invested in.

##### 4.3.1 Gender of Respondents

The respondents' gender breakdown is displayed in Table 5 below 46% of respondents were female, while 54% of respondents were male.

Table 4: Gender of Respondents

Gender	Frequency	Percentage
Male	108	54
Female	92	46

Total	200	100
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### 4.3.2 Age of Respondents

Table 6 shows how the participants were divided into four age groups. 51% of the respondents were in the 20–30 age range, 39% were in the 31–40 age range, 8% were in the 41–50 age range, and 4% were in the 51–60 age range.

**Table 5: Distribution of Respondents' Age**

Age	Frequency	Percent
20-30	101	51
31-40	77	39
41-50	15	8
51-60	7	4

### 4.3.3 Level of Education

The research also looked at the respondents' level of education. The table below shows that 39% of the respondents were undergraduates, 20% were postgraduates, 35% were tertiary/college/diploma while those who had only a secondary school education were 5% whereas those who had other levels of education were 2%.

Table 6: Respondents' Level of Education

Level	Frequency	Percent
Undergraduates	78	39%
Postgraduates	39	20%
Tertiary/college/diploma	69	35%
Secondary	10	5%
Others	4	2%
Total	200	1

#### 4.3.4 Level of Investors

The purpose of the study was to determine if the participants were active or passive unit trust investors. According to the following data, 23.5% of respondents were inactive unit trust investors, whilst 76.5% of respondents were active investors in unit trusts.

Table 7: Unit Trust Investment

Responses	Frequency	Percent
Active	153	76.5
Inactive	47	23.5
Total	200	100

#### 4.3.5 Types of Investors

Additionally, the study discovered that 22% of the sampled investors had invested in equity funds, compared to 59% who had invested in money market funds. Additionally, Table 9 below demonstrates that 17% of investors were in Fixed Income funds, while just 3% had invested in Balanced funds.

Table 8: Types of Investments

Type of Investments	Frequency	Percent
Money Market Fund	117	59%
Equity fund	44	22%
Fixed Income Fund	33	17%
Balanced Fund	6	3%
Total	200	100%

#### 4.4 Duration of Investment

The study found out that 47% of the investors had invested in a unit trust fund less than 1 year while 42% of the investors had invested between 1 – 4 years. Only 7% of the investors had invested between 5 – 9 years whereas 5% of the investors sampled had invested for more than 10 years.

Table 9 : Duration of Investments

Duration of Investment	Frequency	Percent
Less than 1 year	93	47%
1 to 4 years	83	42%
5 to 9 years	14	7%
Above 10 years	10	5%
	200	100%

#### 4.5 Descriptive Statistic

Research data's characteristics are summed up and explained using descriptive indicators, which are numbers. They provide straightforward justifications for the statistics and sample. The data was evaluated for this study, and the independent variables' means, frequencies, percentages, and standard deviations were calculated.

Table 10: Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Investment Decision	200	0	1	0.77	0.425
Overconfidence	200	1.0000	5.0	3.578	0.7138
Availability Bias	200	2.0	5.0	3.775	0.5710
Herding Variables	200	1	5.0	3.87	0.781
Disposition effect	200	2.0	5.0	3.888	0.6826

Table 11: Mean Value Range for Variables

MEAN RANGE	EXPLANATION
Mean<2	Very low variable effect
2< Mean<3	Low variable effect
3< Mean<4	Moderate variable effect
4< Mean<5	High variable effect
Mean >5	Very high variable effect

#### **4.5.1 Mean Value Range for Overconfidence**

According to table 11, Overconfidence had a standard deviation of 0.7138 and a mean of 3.58 indicating that it had a moderate effect on investment decision in choice of unit trust.

#### **4.5.2 Mean Value Range for Availability Bias**

As per table 11, Availability bias had a mean of 3.775, signifying a moderate effect on investors decision in choice of unit trust.

#### **4.5.3 Mean Value Range for Herding Variables**

Loss aversion according to table 11 had a moderate effect on the investor's decision making with a mean of 3.888 and standard deviation of 0.6826.

#### **4.5.4 Mean Value Range for Regret Aversion**

Regret aversion was found to also moderately affect Unit Trust Investors investment decisionmaking with a mean of 3.468 and standard deviation of 0.7178 as depicted on table 11.

#### **4.5.5 Mean Value Range for Mental Accounting**

Table 11 shows that investors' judgments were influenced by mental accounting to a considerable extent, with a mean of 3.81 and a standard deviation of 0.819.

### **4.6 Correlation analysis**

The researcher set out to determine how the study's variables were related to one another. To ascertain this, a correlation study was carried out. The Pearson's correlation coefficient ( $r$ ) was used to establish the correlations, and the purpose of the results was to highlight the direction and strength of linear relationships between the variables. When two variables are positively correlated, it means that higher levels of one variable are linked to higher levels of the other. Negative outcomes are also possible, meaning that higher levels of one variable are linked to lower levels of the other. The correlation coefficient's sign (+ or -) shows which way the link is going. The intensity of the link is indicated by the correlation coefficient's magnitude.

A strong, positive association between two variables is indicated by a correlation of  $r = 0.9$ , whereas a weak, negative relationship is suggested by a correlation of  $r = -0.2$ . There may not be a linear relationship between two continuous variables if the correlation is approaching zero.

Table 12: Relationship between variables

		IDM	Overco nfidenc e	Availab ility Bias	Gamb lers Fallac y	Loss Avers ion	Regret Avers ion	Mental Accoun ting
Overconfid ence	Pearson	.380**	1	-0.065	0.099	.141*	0.030	.134*
	Correlati on							
	Sig. (1- tailed)	0.000		0.182	0.081	0.023	0.334	0.029
Availability Bias	Pearson	-	-0.065	1	.388**	.347**	.295**	0.035
	Correlati on	0.002						
	Sig. (1- tailed)	0.491	0.182		0.000	0.000	0.000	0.313
Disposition Effect	Pearson	0.000	0.030	.295**	.118*	.313**	1	0.045
	Correlati on							
	Sig. (1- tailed)	0.497	0.334	0.000	0.049	0.000		0.265
Hearding Variables	Pearson	0.070	.134*	0.035	.124*	.208**	0.045	1
	Correlati on							
	Sig. (1- tailed)	0.163	0.029	0.313	0.041	0.002	0.265	

\*\* . Correlation is substantial at the 0.01 level (1-tailed).

\* . Correlation is substantial at the 0.05 level (1-tailed).

The results from table 12 above demonstrate the  $r=-0.002$  negative association between availability bias and investment decision making. However, there was a substantial positive link between the following when making investment decisions: overconfidence ( $r = 0.38$ ), Availability Bias ( $r = 0.161$ ), Disposition Effect ( $r = 0.07$ ), and Herding Variables ( $r = 0.082$ ). With  $r=0.00$ , there was a negligible positive link with regret aversion. The research variables exhibit no multicollinearity, since all correlation values fall below 0.75.

Table 13: Model summary

R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
.401 <sup>a</sup>	0.161	0.135	0.395	1.889

From table 13 above, the independent factors account for 16.1% of the variance in investment decision making, according to the R square value (coefficient of determination) of 0.161. The results also demonstrate that there is minimal variance, indicating that the correlation will be perfect, with the standard error of estimate being approximately zero. A number closer to 0 on the Durbin-Watson autocorrelation measure denotes a positive autocorrelation. The value of 1.889 in the findings indicates a positive autocorrelation.

Table 14: Significance

	Sum of Squares	DF	Mean Square	F	Sig.
Regression	5.785	6	0.964	6.168	.000 <sup>b</sup>
Residual	30.170	193	0.156		
Total	35.955	199			

- a. dependent Variable: Y
- b. Predictors: (Constant), Availability Bias, Overconfidence, Herding bias, Disposition Effect tables above show that independent variables can significantly predict Investment Decision (dependent variable) as the p value is less than 0.005.

#### 4.6 Fitting the Regression Co-efficient Model

Table 15: Regression coefficients

Model	Unstandardized		Standardized	T	Sig.
	Coefficients		Coefficients		
	B	Std. Error	Beta		
(Constant)	-0.201	0.279		-0.720	0.472
Overconfidence	0.217	0.040	0.364	5.362	0.000
Availability Bias	-0.020	0.057	-0.027	-0.347	0.729
Herding Variables	0.074	0.040	0.136	1.851	0.066
Disposition Effect	0.004	0.047	0.006	0.083	0.934

From the Table the following regression equation was derived

$Y = -0.201 + 0.217 \text{ overconfidence} - 0.020 \text{ availability bias} + 0.074 \text{ Herding Variables} + 0.04 \text{ Disposition Effect} + \epsilon$

Fitting the regression model to our study, when factors – overconfidence, Herding Variables, availability bias, Disposition Effect are at zero, investment decision making will be at -0.201. Overconfidence affected investment decision making in unitrust by 0.217, availability bias by -0.020, gambler’s fallacy by 0.074, loss aversion by 0.04, regret aversion by -0.013 and mental accounting by 0.002.

#### 4.9 Regression Analysis

Further details on the direction of the link between the variables may be obtained by regression analysis. It is employed to forecast and characterize the nature of a connection. The influence of independent factors (product characteristics, corporate governance and transparency, performance of mutual funds, fund manager attributes, and ease of investing) on the dependent variable (investment choice) in mutual funds was investigated using multiple regressions. The statistical regression equation is expressed as follows:  $a+bX$

Multiple regression model

$$\hat{Y} = \alpha + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \beta_5X_5 + e_i$$

Where,  $\hat{Y}$  = Investment decision (dependent variable)

$X_1$  = Ease of Investment

$X_2$  = Product features

$X_3$  = Performance of Mutual Fund

$X_4$  = Corporate Governance and Transparency

X5 = Fund Manager Qualities

$\alpha$  = Constant

$\beta_1, \beta_2 \dots \beta_5$  = Regression coefficients of Factor 1 to Factor 5 respectively

$e_i$  = Error term

Table 17: Regression Analysis

#### Model Summary

Model	R	R Square	Adj. R Square	Std. Error of the Estimate
1	.699a	.489	.484	.54886

a. Predictors: (Constant), Fund Manager Characteristics, Product Features, Mutual Fund Performance, Corporate Transparency and Governance, Investing Made Easy, According to the study's model summary, the R square may be utilized to determine the coefficient of variation that is employed in regression. Table 17 shows that the R<sup>2</sup> value is 0.4890, meaning that 48.90% of the independent factors account for the choice to invest in a mutual fund. But this research still doesn't explain 51.1% of the total. The standard error of estimate of 0.54886, which illustrates the variability of the observed value of the investment choice, is also represented by the summary table model.

#### 4.7 Test for Multicollinearity

A multi-collinearity test was used in the study to determine whether there was a correlation between two or more variables. The table below displays the findings.

Table 18: Collinearity Diagnostics

Variable	Tolerance	VIF
Overconfidence	0.9451	1.0581
Availability Bias	0.7352	1.3602
Herding Variables	0.8610	1.1614
Disposition Effect	0.9393	1.0646

The results of the collinearity tests indicate that the variance inflation factors (VIF) ranged from 1 to 10. This suggests that the variables do not exhibit multicollinearity.

#### **4.8 Interpretation of the findings**

Finding out how behavioral biases affect mutual fund investments in Nepal was the study's main goal. Two hundred respondents who represented Nepal's unit trust investors were provided questionnaires. To determine how availability, overconfidence, the gambler's fallacy, mental accounting, loss, and regret aversion affected the respondents' decisions to invest in unit trusts, questions were posed to them. The results demonstrated a substantial positive correlation between overconfidence and unit trust investment decisions ( $r=0.38$ , gambler's fallacy  $r=0.161$ , loss aversion  $r=0.082$ , and mental accounting  $r=0.07$ ). Regret aversion and investment decision making showed a negligible positive correlation ( $r=0.00$ ), whereas availability bias and investment decision making showed a negative correlation ( $r=-0.002$ ). These findings suggest that availability bias had no effect on the decision-making process of unit trust investors. The unit trust investing decisions are influenced by biases, mental accounting, gambler's fallacy, overconfidence, loss aversion, and statistically significant correlations. The following multi-linear regression equation showed the effects of each independent variable on the dependent variable:  $Y = 0.074$  gamblers fallacy +  $0.04$  loss aversion -  $0.013$  regret aversion +  $0.002$  mental accounting +  $0.217$  overconfidence -  $0.020$  availability bias. When all other variables are held constant, an increase of one unit in overconfidence has an impact on investment decision-making by  $0.217$ , whereas an increase of one unit in availability bias has an impact of  $-0.020$ . When all other variables are held constant, a unit increase in gamblers fallacy impacts investment decision-making by  $0.074$ , but a unit rise in loss aversion boosts influence by  $0.04$  on decision-making. With all other variables held constant, a unit increase in regret aversion has an impact on decision-making that is  $-0.013$ , whereas a unit increase in mental accounting has an impact that is  $0.002$ . The independent factors account for  $16.1\%$  of the discrepancy in investment decision making, according to the coefficient of determination ( $r=0.161$ ) R square value. Since there was minimal variance, the correlation will be practically perfect, as indicated by the standard error of estimate of  $0.395$ , which is almost nil.

#### **4.9 Discussion**

The main purpose of this study was to know the attitude of investors in mutual fund. For this purpose, we should examine the behavioral biases affecting investment decision in mutual fund in Nepal. The result consistency to the study of Shrestha and Shrestha (2020). The investors influenced by ease of investment, product features, performance of mutual fund, corporate governance and transparency and fund manager qualities in making

decision at the time of investment in mutual fund. Furthermore, results of this research portray that a significant impact of independent variables on dependent variable. As Shrestha and Shrestha (2020) reported that the corporate governance & transparency and fund manager qualities did not have significant correlation with investment decision; however, there is a positive and significant correlation coefficient of corporate governance & transparency and fund manager qualities with investment decision. In this research, it is found that all independent variables have positive and significant correlation coefficient with investment decision. It indicates that the positive relationship of investors perception and awareness level with investment decision. To know the perception and awareness of investors towards mutual fund, dimensions are preference of investment avenues, investment objectives, investors perception towards mutual fund attributes and awareness about risks of investment in mutual fund. In investment avenues people mostly aware about or prefer equity share and then insurance policy, in thirdly people are prefer to investment in mutual fund. The finding of (Chaudhary, Dhakal & Adhikari, 2021; Kandel, 2020; and Bajracharya, 2017), medium number of people are invested in equity shares and mutual funds due to lack of knowledge and awareness. But they found very few investors are prefer with bond and debentures which is similar to our findings, and they also found majority of the investors are familiar with fixed deposits due to low risk which is totally opposite to our findings. bank deposit has very low preference by investors. Our finding is similar to finding of Wagle (2020) is many investors chose to invest in common stocks rather than mutual funds and people choose to invest in the capital market over a bank deposit. In investment objectives most of the people are invest in mutual fund for wealth creation and then capital preservation. Likewise, in mutual fund attributes most of the respondents are good perception towards reputation of mutual fund managers and their selection of financial instruments of mutual fund. And medium number of investors satisfied with availability of information of mutual fund. Investors awareness about mutual funds significantly influence the investors attitudes towards Islamic mutual funds (Aljaed, MdHusin, Ismail & Aljaud, 2019). This paper also finds that the higher the awareness level of investors towards mutual fund should influence investors investment attitudes towards mutual funds. Awareness and knowledge about risk factors of mutual fund is important and relevant in determining mutual fund returns (Vidal-Garcia, Vidal and Nguyen, 2016). Past performance of European mutual funds has explanatory power for future performance and investors can obtain useful evidence from past performance data (Vidal-Garcia, 2013).

## **CHAPTER V**

### **SUMMARY AND CONCLUSION**

This chapter focuses on presenting the findings of the questionnaire survey as well as analyzing and interpreting the data that was gathered throughout the investigation. The results obtained from the analysis of the information gathered throughout the survey should meet the purpose of this research study. The testing of the theories put forth in the preceding chapter are another major topic of this chapter. This chapter comprises four sub-sections. The respondent profile is covered in the first section, which includes demographic data on the respondents' age, gender, education, occupation, income, and amount of savings per month. Using descriptive analysis and SPSS software, the acquired data is analyzed and interpreted in the second section. Through the correlation of dependent and independent variables, the third section analyzes and interprets the data that has been gathered. Furthermore, the examination of the findings from the study is covered in the fourth and final section.

#### **5.1 Summary**

mutual funds, several indicators that are used to determine investors' perceptions and levels of awareness regarding mutual funds are based on literature research. Investors' decisions to invest in mutual funds are influenced by several variables. Accordingly, the study identified a number of pertinent factors that should be taken into account in order to affect investors' attitudes toward mutual funds, including fund manager qualifications, convenience of investing, product features, mutual fund performance, corporate governance, and transparency. Additionally, the study provides a descriptive analysis of the goals of investments, the preferred channel for investing, risk awareness, and the assessment of mutual fund characteristics. The study used a sample size of 200 respondents, and standardized questionnaires were used to collect responses both in-person and online. In terms of the demographic profile, 108 of the 200 respondents are men and 92 are women. When doing an analysis inside a factor, many things are utilized to comprehend the variables. Each variable is examined using the Likert scale of measurement, mean, standard deviation, correlation, and regression, with matching items under each variable. as well as applying several Likert scale varieties to every goal. 200 questionnaires were distributed, and data analysis and result generalization were conducted using SPSS and Excel. Samples

from several demographic categories, including age, gender, marital status, educational background, employment, income, and savings, were included in the study. The results of the inferential study included investor perceptions of mutual funds, investor knowledge of mutual funds, and variables that influence investors' decisions to make mutual fund investments. All of the independent factors have a positive association with the dependent variables, and there is a positively significant link between them.

## **5.2 Conclusions**

It is concluded that behavioral biases in investment decision-making must be identified and addressed considering the aforementioned results and debate. Poor investing choices can result from overconfidence, which occurs when people overestimate their own skills and the veracity of their information. Suboptimal results can also arise from the disposition effect, which makes people more likely to sell winning stocks too soon and hang onto losing equities too long. Furthermore, overconfident investors might underestimate their capacity to identify profitable ventures. Conventional financial theories advocate for diversified portfolios; nevertheless, misplaced confidence may work against this advice, leading an investor or their financial adviser to place their reliance in a single stock rather than diversifying their holdings. The results highlight how important it is for investors to recognize these biases and think about mitigating them. The relationship between risk aversion, overconfidence, herding behavior, disposition effect, and investment decision-making is positively correlated with financial literacy. This suggests that people with higher levels of financial literacy are better able to navigate the effects of these behavioral biases and make more informed investment decisions. Thus, in order to reduce bias in investment decisions and achieve better investment outcomes, it is necessary to comprehend the financial market. Irrational decision-making leads to losses in investment decisions. By raising people's financial literacy, investors will be better able to identify and overcome prejudices like overconfidence, herd mentality, risk aversion, and the disposition effect, which will enable them to make more thoughtful and logical investment decisions. In a similar vein, it is critical to remember that acquiring financial literacy is a lifelong process that calls for constant learning and instruction. As a result, ongoing initiatives to increase financial literacy should be continued and customized to the specific requirements and traits of various demographic groups.

### **5.3 Implications**

Important new information about the influence of behavioral biases on investing decision-making and the moderating role of financial literacy is offered by this study. According to the research, financial literacy and education are essential for overcoming prejudices and making wise investment choices. The study's consequences can help investors, financial advisers, and legislators create sensible investment plans and regulations that support informed decision-making. Ultimately, the study emphasizes the necessity of more behavioral finance research to deepen our comprehension of the intricate relationships that exist between financial decision-making and human behavior. Based on primary data gathered from an online survey conducted in Nepal, this study on mutual funds has attempted to examine the attitudes of individual investors regarding mutual funds. The research's conclusions have led to the suggestions that follow. Since the study is based on a more extensive investigation conducted in Nepal, it may also be expanded to include the viewpoint of investors from beyond the valley. It is advised that future research enlarge the sample size in order to further ensure reliability and validity, as the current study's sample size is insufficient to allow for result generalization. The majority of investors would rather use stock shares than mutual funds. Thus, our data demonstrates that investors find equities shares more appealing than mutual funds. Thus, the question of how to draw investors to mutual funds rather than stock shares will likely arise in the future. The majority of investor capital is invested in mutual funds for the purpose of creating wealth and preserving capital, meaning that the mutual fund business is primarily concerned with finding ways to grow investor capital and wealth.

#### **5.3.1 Financial Advisors**

Financial advisers can use the results of this study to create more sensible investment plans for their customers. In order to increase their clients' financial literacy, they can help them recognize their prejudices and educate them about money matters. Financial advisers may also assist their customers in avoiding the disposition effect and herd mentality by guiding them to make well-informed investment decisions grounded in unbiased examination of financial data.

#### **5.3.2 Investors**

The study's findings imply that investors should be conscious of their prejudices and think about pursuing financial education to raise their level of financial literacy. They should also

try to make more informed investing decisions based on objective examination of financial facts rather than depending unduly on the judgments of others or their own skewed impressions.

### **5.3.3 Policymakers**

The study's conclusions imply that legislators ought to think about enacting laws that support financial literacy and education. By assisting people in identifying and overcoming their prejudices, these policies can help them make better financial decisions. Furthermore, legislators have to think about creating rules that deter herd mentality and the disposition effect, encouraging investors to make more logical decisions.

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## Appendix

### Research Questionnaire

Dear Respondent,

I am **Sachin Pathak** currently Pursuing MBS degree from Shanker Dev Campus, Putalisadak, Kathmandu. I am conducting research on topic “**Effect of Behavioral Biases on Investment Decision of Mutual Fund Investment in Nepal**” under the supervision of **Asst. Prof. Durga Datt Pathak**. Your genuine opinion on the matter should be regarded as the best response. Please cooperate with me so that I may successfully finish the assignment. I guarantee that the information you submit will be kept private and utilized solely for academic purposes.

#### Part A: Personal Details

1. Gender (Male, Female)

Male  Female  Others

2. Age

18 to 29 years  30 to 44 years

45 to 60 years  60 years above

3. Marital Status

Married  Unmarried

4. Education Qualification

Up to SLC/SEE  Up to Higher Secondary School/PCL

Up to Bachelor  Up to Masters

Up to M Phil & PHD

5. Occupation

Student  Self Employed

Govt. Employee  Private Employee

Business  Retired

Others

6. Monthly Income (Rs)

Below Rs. 10,000  Rs10,001 – Rs.30,000

Rs.30,001–Rs.50,000  Rs.50,001 – Rs.1,00,000

Above Rs. 1,00,000 ( )

7. How much income do you save in a month? Below 20% ( ) 20 – 30% ( )  
30 – 40% ( ) Above 40 % ( )

Part B: Investors Perception Towards Mutual Funds

1. Different financial conditions have been presented in the table below.

Please kindly express your opinion.

*(1- Highly Un-preferred, 2- Some What un-preferred, 3- somewhat Preferred, 4- Preferred. 5- most*

<b>Investment avenue</b>	Highly Un-preferred (1)	Some What Un-preferred (2)	Some What Preferred (3)	Preferred (4)	Most Preferred (5)
Government Securities					
Bank Deposit					
Insurance policy					
Bonds and Debenture					
Mutual Fund					
Equity Shares					

The various financial targets or goals are shown below. Please indicate how important you think these financial objectives are from the standpoint of an investor.

(1- Not at All Important, 2- Not Important, 3- Some What Important, Important, Highly Important)

<b>Investment Objective</b>	Not At all Important (1)	Not Important (2)	Somewhat Important (3)	Important (4)	Highly Important (5)
Capital Preservation					
Recurring Cash Inflow					
Meeting Contingencies					
Wealth Creation					
Provision for Retirement					
Tax Planning and Saving					
Purchase of Assets					

This survey was carried out in order to determine the likelihood that Inverters will use mutual funds.

<b>Investment in mutual funds</b>	Strongly Disagree (1)	Disagree (2)	Neutral (3)	Agree (4)	Strongly Agree (5)
I like to invest in mutual fund					
I am investing in mutual fund					
I am determined to continue investing in mutual fund					

Part C: Influencing Mutual Fund/Scheme Selection

- 1 Please rank the following elements in order of significance when choosing a mutual fund plan and making an investment.

(1- Not At all Important, 2- Not Important,3-Some What Important, 4-Important, 5-Highly Important)

<b>Factors</b>	Not At all Important (1)	Not Important (2)	Some What Important (3)	Important (4)	Highly Important (5)
<b>A. Ease of Investment</b>					
A1. Initial minimum investment requirement					
A2. Liquidity in mutual fund					
A3. Regular income generates by fund					
<b>B. Product Features</b>					
B1.Product innovation/variety of schemes					
B2.Load/charges expenses					
B3.Future growth prospects of mutual fund					
B4.Investment objective of fund					
<b>C. Performance of Mutual Fund</b>					
C1.Return and capital gain by the mutual fund investment					

C2.Diversification and risk minimization in portfolio					
C3.Past performance and dividend history					
<b>D. Corporate Governance and Transparency</b>					
D1.Adoption of investment strategy as per scheme's prospectus					
D2. Compliance to SEBON Guideline and Directives					
D3. Declaration of all material information in timely manner					

**EFFECT OF BEHAVIORAL BIASES ON INVESTMENT DECIS...**

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**ABSTRACT** The aim of this study is to investigate the effects of behavioral biases such as overconfidence, availability bias, herding

variables, disposition effect on mutual fund decision in Nepal. The sample was collected using the convenience method and a total of 200 participants

participated in the study. In this study, descriptive statistics, analysis of variance, independent sample t-test, correlation and horizontal analysis were used to analyze the data

. Research results show that overconfidence, emotional performance

and risk aversion have a positive effect on investment decisions, but the herding effect is not significant

. Additionally, the results show that financial literacy has a negative impact on overconfidence, emotional distress, risk taking and animal husbandry. This means that a high level of

financial literacy can help reduce the impact of these biases on investment decisions. This study provides

insight to policy makers,

stakeholders and financial institutions in developing policies and strategies to improve financial literacy. It is also

useful for researchers and the general public as it provides a deeper understanding of behavior and investment decisions.

Future research could expand the



research

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