

Analysis of the Influence of Psychological Factors on Personal Financial Investment

Jing Yang

Institute of Music, Changchun Normal University, Yuanda Street, Changchun, China

Keywords: Behavioural Finance, Psychological Account, Risk Perception.

Abstract: With the continuous development of the economy, individuals pay more and more attention to financial investment, so the results of investment with different attitudes are also very different. Traditional finance believes that investment should be rational, but the conclusion of behavioural finance is not. This article studies the present from several main factors of behavioural finance, e.g., the kinds of mentality do investors have when investing and methods can be studied to minimize such impacts to maximize profits. In the end, this study did not eliminate the impact of psychological factors on investment and financial management. Instead, by focusing on the two aspects of psychological accounts and risk perception, it was found that risk perception has a close positive correlation with investment decision-making, and emphasized that the sensitivity of individuals to risk perception in the process of investment decision-making is very high. The important thing is not to be overconfident or blindly follow the trend. This study analyses the psychological activities and changes in mentality experienced by investors before making investment decisions, and concludes that such psychological activities will have a significant impact on investors.

1 INTRODUCTION

The conditions that affect decision-making are often caused by personal cognition, psychological factors and behavioural restrictions (Bashar, 2023). Traditional finance believes that investors with rational behaviour should conduct risk assessment before investing, and investment behaviour should be rational, while behavioural finance believes that psychological accounts will affect investors' follow-up decision-making, which is irrational (Almansour & Arabyat, 2017), which is a kind of behavioural deviation. The most basic reason why the author studies behavioural finance is that traditional finance has certain limitations in explaining investors' financial decisions and cannot give a more authoritative explanation. Behavioural finance not only does not deny any financial theory, but also adds psychological knowledge (Bashar, 2023), in order to It is enough to explain some irrational investment behaviours and financial decisions that traditional finance cannot explain. Some typical suggested characteristics of investment risks are listed in Table 1 (Lvo vlaev et al., 2009).

Investment is often to obtain higher returns, so as to improve personal living standards and satisfy the

public's pursuit of high quality of life and enjoyment. With the desire for these interests, individuals always cannot absolutely rationally stop loss or take profit in time according to the current situation when investing. For example, stock investment, firstly, based on speculation, people buy stocks at higher prices, but sell them at lower prices because of lack of confidence, which causes certain losses (Bashar, 2023). Secondly, due to overconfident bias but lack of sufficient financial knowledge, they are used to new things and when old things are connected, representative bias may cause significant losses for buyers to buy stocks with too high prices. Most investors tend to prefer a more stable and stable tendency when investing, and hold a high-risk avoidance attitude (Wildavsky & Dake, 1990). It is precisely because of the perception of low risk by market participants that they are inclined to grazing, which also has an adverse impact on their decision-making (Madaan & Singh, 2019). The collapse of the Saudi stock market in 2006 was also mainly attributed to the irrational behaviour of investors.

Although investors' profits and losses will have a significant impact due to behavioural financial bias, this article is based on this phenomenon. Through research on the investment market, stocks, sinking

costs, purchase commodity utility, etc., it hopes to find a way to reduce the impact of psychological factors in the process of financial investment, so that investors can better Business planning and decision-making. This article still explores the relationship between sunk costs and psychological accounts in the category of behavioural finance, and the intermediary role of risk perception in the Saudi stock market in the impact of behavioural financial factors on personal financial investment decision-making. However, there is no relevant research on risk perception as an intermediary in the Saudi stock market (Bashar, 2023). Although the impact of psychological accounts on individuals is not small, this impact will gradually decrease over time. That's why investors often buy expensive goods that far exceed their psychological expectations (Bashar, 2023). Hence this research which kind of psychological activity did the buyer experience when he bought these high-priced goods. Through the study of these psychological account investment problems, one is inspired by the correct direction and field of investment in the future.

Table 1: Suggested Characteristics of Investment Risk.

Characteristic Category	Percentage of Time Mentioned First
Stock market volatility	35%
Economic uncertainty	22%
Saved amount (exposure)	11%
Characteristics of the investment company	11%
Salary/job uncertainty	7%
Others	15%

2 DESCRIPTIONS OF BEHAVIORAL FINANCE

Because it involves psychological factors, it should be studied from the scope of behavioural finance. Traditional finance believes that investment should be completely rational, so scholars do not consider it from here. After studying behavioural finance, it is concluded that personal cognitive bias and emotional reaction will affect the final investment decision-making. A wide range of behavioural financial factors include bias, risk perception and personality characteristics, etc.

The bias of behavioural finance has a significant impact on investors' profits and losses (Parveen et al., 2020). For example, overreacting, investors always

overestimate the importance of new information. Being too confident in their decision-making will give them a prejudice of overconfidence, resulting in excessively high economic costs and large losses. They will also overreact to negative news and underweight the possibility of rare events, which will eventually lead to inefficient investment or make bad investment decisions (Grable et al., 2020; Kim et al., 2022). In terms of emotional response, people's greed and fear dominate. Investors often have "floating losses are not losses" or are unwilling to give up in time when there is a little profit. Driven by this greed, investors' excessive investment may lead to huge losses, or irrational selling when the market panics will also lead to assets. Fall.

Speaking of crowd psychology, for most investors, they do not have enough financial knowledge to support their rational investment. They often blindly follow the trend, which is very unfavourable to both the stock market and the cryptocurrency market. It is easy to form a stock market bubble or a herd effect. The collapse of the Saudi stock market in 2006 was mainly due to investors' irrational investment and blind follow-up.

3 RISK PERCEPTION

Risk perception is a very important intermediate variable to understand how a person's subjective evaluation of risk affects his final investment decision. Through the study of risk perception, one can fully understand how risk perception and investment decision-making and behavioural factors interact, and finally shape investment decision-making, helping researchers to comprehensively understand the whole process of investment decision-making (Adil et al., 2022). Some typical results are listed in Table 2.

First of all, when it comes to risk, different investors must have different preferences for risk. However, due to the high attention to the degree of risk, the risk perception has gradually increased and the frequency of transactions has also increased, resulting in less investment in the stock market (Ahmed et al., 2022), so there will be different types of investors with different attitudes towards risk. The first risk-averse investor tends to invest in low-risk and more stable assets, such as bonds and time deposits. The second is risk-neutral investors. They will want to seek balance. They may choose the combination of stocks and bonds, that is, portfolio investment. They do not put eggs in the same basket, spread risks, and make full use of the complementarity between different assets in order to

improve the overall investment effect. Such investment will also bring Come to a relatively stable income. The third type of risk-preference investors, who are willing to take high risks in order to obtain higher returns, may invest in cryptocurrencies or venture capital (Ballis & Verousis, 2022). However, one thing is that although they are willing to bear the losses that may be brought about by high risks, most of them may not have sufficient financial knowledge to support their rational investment. At this time, investors will blindly follow the trend due to the psychology of following the crowd, and in the end, they will not achieve the expected high benefits. Some other results are also listed by (Michael & Joseph, 2020).

Table 2: Suggested Characteristics of Investment Risk.

Risk Factor	Mean	t-test (df = 55)	
		t	p
Possibility for very large loss in relation to the amount of money invested.	5.70 (1.49)	—	—
Feeling of loss of control over the course of the investment.	5.20 (1.31)	2.05	.0456
The possibility that your investment does not increase in value so that you do not reach your target retirement income.	5.20 (1.49)	2.58	.0127
The possibility that your investment may still not be enough to provide a proper style of living after retirement.	5.16 (1.63)	2.04	.0459
Lack of trust in the financial adviser.	5.13 1.36	2.27	.0274
Lack of knowledge about particular investments.	5.07 (1.23)	2.73	.0084
Likelihood that cost of life (prices) will go extremely high due to high inflation, which will make you savings unable to cover your life needs.	5.04 (1.32)	2.62	.0115
Lack of confidence in the future performance of the economy and/or the stock market.	4.95 (1.33)	3.03	.0037
Lack of trust in the product provider.	4.93 (1.54)	2.59	.0121
The fear that you might be making a wrong decision.	4.86 (1.46)	3.20	.0023
Lack of trust in the particular company in which you are investing.	4.66 (1.48)	4.07	.0002
The unsuitability of particular types of investments.	4.64 (1.43)	4.53	.0000
Lack of trust in the particular industry.	4.64 (1.38)	4.61	.0000
The worry and anxiety that may be	4.63	3.65	.0006

caused if the value of your investment decreases.	(1.36)		
Equity or fairness of the risk-benefit distributions.	4.39 (1.04)	5.62	.0000
Concern as to whether you will lose state benefits to which you would otherwise be entitled if you did not save for your retirement.	4.30 (1.52)	5.34	.0000
Unfamiliarity with a type of investment.	4.29 (1.52)	8.09	.0000
The fact that investing for a pension is a complex process and something you are not used to doing.	4.21 (1.66)	5.73	.0000
The liquidity of your investment.	4.04 (1.39)	5.89	.0000
General uncertainty about investment products in general.	3.95 (1.65)	6.29	.0000
The fear that you may not be able to meet the saving commitment of £2000 a year.	3.88 (1.70)	5.81	.0000
Lack of confidence in the workings of the financial markets.	3.79 (1.36)	7.45	.0000

4 MENTAL ACCOUNTING

There are five types of psychological accounts, which correspond to different financial decisions, and they influence and constrain each other. However, it is precisely because the distribution of these funds is too meticulous that the limitations of psychological accounts may lead to the distortion of the first risk preference, which may lead to irrational investments, such as including unexpected income in the investment account for high-risk investment and ignoring the comprehensiveness of investment decision-making. The second point leads to misjudgement of capital flow. Investors may make wrong judgments about capital flow, which will affect investment decision-making and capital allocation.

Then studying the formation of psychological accounts makes researchers understand that there is no way to eliminate the impact of psychological accounts on investors. The first is that cognitive differences lead people to tend to distribute funds according to source, purpose and feelings, which is unconscious. Another thing is that social and cultural background and education level will affect a person's view of money, which is implicitly formed and basically cannot be changed.

5 LIMITATIONS AND PROSPECTS

Since there is no law to avoid the impact of these psychological factors, one can find ways to reduce these effects. First of all, emotional management training can be carried out, so that investors can maintain a stable mentality and reduce unnecessary losses caused by emotional fluctuations. The second is to learn more relevant financial knowledge. With a certain financial knowledge reserve, investors can have a certain confidence when investing instead of blind confidence or blindly following the crowd (Ahmad, 2022). Finally, build the awareness of long-term investment to help investors build patience to avoid increasing costs due to frequent transactions (Ababio et al., 2020).

6 CONCLUSIONS

In summary, there are many and complex psychological factors affecting personal financial investment, and may even cause irreparable huge losses, but this impact is inevitable. This research can only reduce its impact through various methods. Personal cognitive and psychological changes are often the fundamental prerequisites that affect a person's investment decision-making. From the perspective of behavioural finance, there are many factors that affect investment decision-making. In general, it is difficult for a person to be rational when making investment decisions, often because they do not have enough relevant financial knowledge. There is a keen sense of risk, which leads to blindly following the crowd due to overconfidence and so on. The formation of psychological accounts has both advantages and disadvantages. The advantage is that the detailed distribution allows investors to better plan their property, but it also makes investors have great limitations when investing and cannot consider problems comprehensively, and the investment results are not satisfactory. Therefore, since there is no law to avoid psychological factors when investing, you might as well face the difficulties and consider comprehensive issues as much as possible according to the research results when investing, so as to avoid emotional ups and downs that investment decisions are greatly affected by psychological factors and cause irreparable losses.

REFERENCES

- Almansour, B. Y., Arabyat, Y. A., 2017. Investment decision making among Gulf investors: Behavioural finance perspective. *International Journal of Management Studies*, 24(1), 41-71.
- Ahmed, S. U., Ahmed, S. P., Abdullah, M., Karmaker, U., 2022. Do socio-political factors affect investment performance. *Cogent Economics & Finance*, 10(1).
- Adil, M., Singh, Y., Ansari, M. S., 2022. How financial literacy moderate the association between behaviour biases and investment decision? *Asian Journal of Accounting Research*, 7(1), 17-30.
- Ahmad, M., 2022. The role of cognitive heuristic-driven biases in investment management activities and market efficiency: A research synthesis. *International Journal of Emerging Markets*, 178.
- Ababio, K. A., 2020. Behavioural portfolio selection and optimisation: Equities versus cryptocurrencies. *Journal of African Business*, 21(2), 145-20.
- Bashar, Y. A., 2023. Behavioural finance factors and investment decisions: A mediating role of risk perception. *General & Applied Economics*, 17.
- Ballis, A., Verousis, T., 2022. Behavioural finance and cryptocurrencies. *Review of Behavioral Finance*, 14(4), 545-562.
- Grable, J. E., Jo, S. H., Kruger, M., 2020. Risk tolerance and household financial behavior: A test of the reflection effect. *IIMB Management Review*, 32(4), 402-412.
- Kim, J. J., Dong, H., Choi, J., Chang, S. R., 2022. Sentiment change and negative herding: Evidence from microblogging and news. *Journal of Business Research*, 142, 364-376.
- Lvo Vlaev, Nick, C., Neil S., 2009. *Dimensionality of Risk Perception: Factors Affecting Consumer Understanding and Evaluation of Financial Risk*, 11.
- Madaan, G., Singh, S., 2019. An analysis of behavioral biases in investment decision-making. *International Journal of Financial Research*, 10(4), 55-67.
- Michael, S., Joseph, A., 2020. *Risk Perception: Reflections on 40 Years of Research*.
- Parveen, S., Satti, Z. W., Subhan, Q. A., Janil, S., 2020. Exploring market overreaction, investors' sentiments and investment decisions in an emerging stock market. *Borsa Istanbul Review*, 20(3), 224-235.
- Wildavsky, A., Dake, K., 1990. Theories of risk perception: Who fears what and why. *Daedalus*, 199(4), 41-60