

Behavioral Challenges Facing Individual Investors in Emerging Financial Markets: Case of Egypt

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Abstract

Decision-making from an investment point of view is basically defined as a rational choice among alternatives or as the conscious selection of a course of action from available alternatives. Investors are also assumed to be rational beings. Process of decision making in individuals is subject to various psychological changes, which therefore result in behavior. This paper seeks to investigate the influence of certain identified behavioral factors (or biases), namely; Heuristics bias and Prospect theory on the decision-making process of individual investors and financial professionals in the Egyptian Stock Exchange. Investors were categorized as knowledgeable, and unknowledgeable stock investors (knowledge here means how well investors have financial literacy, know and have studied stock investments in the Egyptian stock market and are experienced in dealings in it). For this paper, responses were collected from 156 financial professionals, managers of investment banks and investment companies and 251 unknowledgeable individual stock investors that invest in the Egyptian Stock Exchange via an adapted online-questionnaire that suited both classes of investors. The results show that prior to a decision making, individual investors and financial professionals in the Egyptian Stock Market undergo several cognitive and emotional illusions which may result in irrationality. Heuristics is one such variable which highly influences the decision making of investors and financial professionals directly and the assumptions of prospect theory are proved to be valid in the cases of both knowledgeable and unknowledgeable investors where they are indeed influenced by Loss aversion, Regret aversion and Mental Accounting when taking investment decisions

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