A PEEP INTO THE BEHAVIOUR OF UNIT TRUST FUND INVESTOR

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Abstract

Investing in unit trust fund has now become a norm for many Malaysians. It is use as a supplementary to their EPF saving for their golden age. In investing unit trust fund, choice of fund is utmost important. The funds must suite the financial objective of the investors and the use of unit trust consultants is very normal. This paper is prepared with the objective to understand the behaviour of the investors in their choice of fund. Three hundred and thirty three respondents took part in the survey. This study analyses the behaviour of the investors, which affect the investors during their choice of fund. It identifies the most fundamental behaviour during the process in selection of fund. The two behaviours considered for this study are herding and overconfidence. The results show that herding was prominent and there was symptom of overconfidence.

Introduction

Unit Trust Fund is becoming vehicles of securities investment most favoured by the public worldwide. Whereas, this trend is more pronounce in the developed securities market of the United States of America and Europe, unit trust fund is increasingly gaining the public attention in the developing economies as well. Unit Trust Fund may be regarded as one of the best avenues for investment available, particularly to small retail investors on account of lower transaction costs, diversification, liquidity and the benefits of the expertise of the fund manager. Although they are not shield from the market risk, the ability to diversify provides assurance to the public.("Federation of Investment Managers Malaysia," 2014)

The purpose of this study is to investigate the fundamental behaviour of investors investing in unit trust fund in Peninsular Malaysia. The two behaviours consider are herding and overconfidence.

Herd Behaviour

As declared by De Bondt (1995), the proof of herding is the weakest point of classical financial theories. De Bondt (1995) said that if Efficient Market Hypotheses holds, it would be mean that there is small trading volume since rational investor would force out the noise investor out of the market. Shleifer (1990) said that noise traders are irrational and ill informed. Yet Keynes (1936) argue that, it is rational to follow others if we feel that others are better informed and had a better judgment. Mallouk (2014) concurred that humans are hardwire to move in herds, to follow the crowd, and to find safety in consensus. If the market is going down and the media commentators and our co-investors are yelling, "head for the exits," our herding instinct, together with the powerful force of fear, is to do the same. If the market is bullish, rallying and everyone is saying full steam ahead, our herding instinct, coupled with the alluring force of greed, entices us to join the crowd. Lindlhe (2012),said that in deciding which restaurant to eat or which school to attend, frequently we are influenced by the crowd and this conclude that people are influenced by others in their decision making. This is applicable in financial market. Investors will follow the advice of the expert and the direction of the market and generally refer to as herd behaviour. Lindhe (2012) in her study said that there are types of herding:

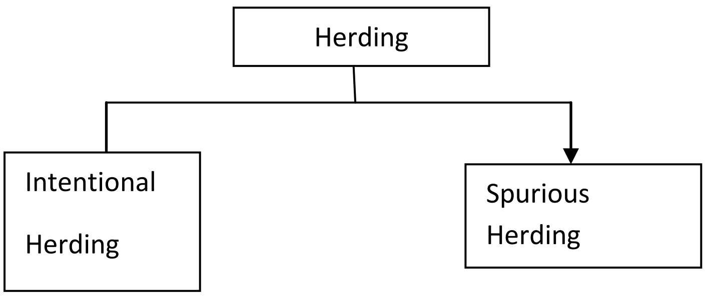

Figure 1 Types of herding according to Lindhe (2012)

Intention herding is the result of the aim by investor to follow the actions of other's. Herding can be intentional if investors imitate others. This is agreed by Keynes (1936) and may lead to inefficient market.When a group of investor have a set of similar information and face the same decision, spurious herding occurs. They will make similar decision and the outcome is efficient. To distinguish between the two is important in theory but in practice is rather difficult. According to Sharma (2001) there are many factors that influenced an investment decision.

Famous article by Banerjee (1992) define herding as what is everyone is doing although own information suggests otherwise but it can be apply in many situations and form. Rizzi (2008)on the other hand define herding as mimicking the behaviour of others. Caparrelli (2004) and Lakonishok (1992) agreed that if investors show herding behaviour, they invest what other invest and sell whichever they are selling. The decision they made did not follow and known rules of trading securities. Dom (2003) defined herd behaviour as trading in the same direction simultaneously in relation to the same asset by a group of investors. Decamps and Lovo (2002**)** stated that the criteria for herding is that investors follow the decision of others by changing its own decision. Michelle (2007) in his study suggested that social influence has effect on financial choices and that the inclination to herd is not homogenous but vary across personality types and age. This was agreed by Baddeley (2012) who said that herding is the product of individual difference and non-economic factors such as personality trait, gender and age. Chiang (2010) found that in the field of Behavioral Finance, correlation in trades is due to the interaction of traders. In his study, he found that in most financial market, a large group of traders has stop thinking rationally and start following others. Thus, according to Devenow (1996), herd is a "correlated behaviour models between individual".

The reason for this unison action was explain by Bikhchandani & Sharma (2000) as they said that the similar behaviour was due to similar information with the objective of maximising profit. Bikhchandani & Sharma (2000) argued that an individual herd if she or he would have made choice without knowing other investors' choice, but does not make that choice when she finds that others have decided. However, Hirshleifer (2001)pointed out that herd behaviour was due to information cascades and convergence of behaviour and it is a situation where investor chooses to discard his own private information. Furthermore according to Tan (2008) due to herding, it creates profitable transaction and capable of driving price away from the fundamental value.

Reasons to Herd

Generally according to Ackert & Deaves (2010), people are subject to the forces of herd. However, many like to dismiss that they are lean to herding as very few would agree that they are not force to herd and only the young and inexperienced herd (Ackert & Deaves, 2010). Another reason to herd according to Ackert & Deaves (2010) is due to the expensive information acquisition; different people owned different information and it is costlyto value which option is worth. According to Bikhchandani & Sharma (2000), what drives investor away from the decision they made after observing others are due to the following reasons: Anxiety of others will make higher profits. This reason will make them think twice to decide on their own. Keynes (1936) said that herding was the strategy to investors as they may share the risk and return preference and information that creates trading in unison (Falkenstein, 1996). Bikhchandani, Hirshleifer and Welch (1992); and Scharfstein (1990) support the argument as they found that investors prefer to share the blame and follow the crowd. The famous phrase "*is better for reputation to fail conventionally than to succeed unconventionally"*.

Another reason to herd is 'time' factor (Bikhchandani, Hirshleifer and Welch,1998). Time is precious in the decision of choosing a fundas more time used in relaying the information, the more costly it will be. Thus following others will reduce time to decision making. Furthermore, Leonardo Bursztyn (2013) discovered that the people choice is often link with choices around them. According to Leonardo Bursztyn (2013), the peer effect had been widely studied; what is our peer buys or possess will affect our choice. This is known as social learning or social utility. All this can shed are some light on the mechanism underlying herding behaviour in decision making in finance industry.

Overconfidence

Financial world success is depends on confidence of the investors towards the market (Galbraith,1975), however overconfident may lead to wrong judgment and financial decision. De Bondt (1995) research finding argued that overconfidence was related to overrate the chance of accuracy of their information, their capabilities and their success. Thus, Oskamp (1965) and Skala (2008), who is a psychologist supported the idea of De Bondt (1995) and their clinical judgment found that overconfidence was defined as surplus of confidence over accuracy. Oskamp (1965) proved that confidence in judgment and accuracy of his judgment is a wide big gap. When one always estimates one's own ability to perform a given task is called overconfidence (Sepala, 2009). It's explained that people inclined to overrate their own abilities and level of knowledge. It comes in many forms, such as better than average, optimism bias and setting too narrow confidence limits.

The tendency of people to say their skill is higher than average is called better-than-average effect. Merkle &Roger (2011)develop a new study to differentiate between two possible reasons for the effect, namely rational information processing and overconfidence. The participants were required to evaluate their relative position by stating their complete belief distribution. They discovered that people hold beliefs about their abilities in different domains and irrational in processing information. Both on an average and on an individual level, they show substantial over placement. They concluded that overconfidence is not obvious overconfidence but rather the effect of a psychological bias.

As explained by Skala (2008), overconfidence is a human trait. It is always there in the investment community. According to Skala (2008), the goal setting of unrealistic target is due to human tendency trait which is overconfidence. Muthukrishna et al. (2014), on the other hand argue that overconfidence, is often conceptualize in many ways and it is usually difficult to interpret. Hence, Healy (2008) provides a useful set of definitions for different overconfidence concepts; (1) '*overestimation'* which is "the belief that you are better than you really are compared to an objective standard (e.g. believing you can consistently perform a flawless parallel park, when in reality you get it right three times out of ten)"; (2) *Self-attribution bias* refers to the inclination to overestimate the degree to which people are responsible for their own success; (3) *Over placement* is the belief that you are better than most people (e.g. most drivers believe they are better than average, so statistically at least some of these drivers must have over placement); and (4) *Over precision* is having more confidence in your beliefs than is justified (e.g. being 90% certain that you're a better driver than average when you don't have enough data to ascribe that level of certainty). According to Hastorf (1970) and Barberis & Thaler (2003), when people are successful, he claim that it was due to his own hard work and nothing related to external force. Livico (2004) and Benabou (2004)on the other hand discovered that people are always reminisce by their failure, however they will keep on overrating their own skill and abilities and never blame themselves for their failure although they acknowledge that *they do not know what they do not know.*

Daniel (1998) has modelled overconfidence in to two states: *Static confidence* and *dynamic confidence*. Static confidence is the confidence that investors initially exhibit when the overestimate their private signals. They overreact to these signals causing price deviation from the rational level. However, with the arrival of public information, the deviated price, are partially corrected. Dynamic confidence is induce by self-attribution bias, arises when public signal confirms that private signal generated by investor. This hypothesis was tested by Chuang (2006) empirically using US data and the discovery was parallel to Daniel (1998).

Reasons for Overconfidence

Psychological reasons for overconfidence lie in cognitive and motivational factors. (G, 1997). Cognitive factors include biases alleviated by accelerated and accurate feedback, counter argumentation or careful consideration of the problem. The motivational factors on the other hand exposes the strong believe in one's self-efficacy. *Confirmation bias* is one of the reason that contribute to overconfidence as found in Skala's study (2008).Confirmation bias is an example of cognitive and motivational factors as according to Skala (2008), in his study, he found that the excessive usage of confirming evidence and forgetting the contradictory arguments occurred among the respondents. However, Gigerenzer, Hoffrage, & Kleinbölting (1991) did not agree with Skala's (2008). They argue that overconfidence is the result of faulty procedure and their relationship to the environment.

Another reasons according to Merkle & Weber (2011) that leads to overconfidence of the investors are *psychological bias.* Psychological bias is the tendency for investors to make decisions or take action in an illogical way. Psychological bias is the contradictory to common sense or measured judgment. Psychological bias is the decision base on gut feeling and heuristic judgment. Markus (1991) therefore found that there is a positive relationship between individualism and overconfidence. Study by Markus (1991) found that investors think very positively about themselves and focus only on their own attributes in making decision. He also suggested that people in distinctive culture are likely to be more overconfident about the precision of their information over people in collective culture. Deaves (2011) on the other hand discovered that market forecaster was egregiously overconfident. Deaves (2011) argues that the more experienced the forecasters are, the more overconfident they will be as they 'learned to be overconfident' due to the extra information that they have. This argument was supported by Gervais (2001) as he also found that successful traders lead to increase overconfidence.

Research Methodology

The current study is descriptive in nature where it described the behaviour of the unit trust investors decision making process. Survey via questionnaire distribution was utilized on thesample of 333retail unit trust investors in Malaysia. Convenient sampling was used as identifying population of retail unit trust investors is difficult to obtain. Four states took part in this study.

Structured questionnaires with bi-lingual are distribute to the respondents to collect responses as primary data. Likert scale of 1 to 5 was use. Most of the questions are adapted from previous study. It was discover that the questionnaire met all criteria set before hand and a reliability test using Cronbach Apha was conducted and it was in the accepted range between 0.70 and 0.77.

Data Analysis

Demographic Profile

Table 1 Response Rate

States	repondent
Penang	103
Kuala Lumpur	67
Kelantan	104
Terengganu	59
Total	**333**

Table 1 indicate that six hundred questionnaires distributed to the four states and only three hundred and thirty three is useable.

Table 2 Gender

Gender	Frequency	Percentage
Male	156	46.8
Female	177	53.2
Total	333	100.0

Table 2 shows the gender. 53 percent of the respondents were female, while the balances were male.

Table3: Respondents according to their occupation

Occupation	**Frequency**	**Percentages**
Public Sector (Professional)	154	46.2
Public Sector (Non-Professional)	47	14.1
Private Sector (Professional)	86	25.8
Private Sector (Non-Professional)	46	13.8
Total	**333**	**100.0**

Table 3 indicates that, most of the respondents came from the public sector that was from the professional level which contribute to 46.2 percent of the respondent and followed by professionals from the private sector which is 26 percent of the total respondent.

Research Findings

Does unit trust investos follow others (Hearding) in choosing Unit Trust Fund?

Table 5 shows the sources of advice and information that the investors sought in making their choice to invest in unit trust fund. The investors who rely on published sources or seminars in making decision are considered as inclined towards rational behavior as they make their own judgement from the information obtained. On the other hand, investors that relying on others' opinion such as other investors, consultant and friends are considered inclined towards herding behavior.

The result of the present study found that most of the respondents have relative high inclination towards herding with an aggregate mean of 3.51 as compared to only 3.40 for rational behavior. The successful investors decision (mean=3.62) followed by unit trust consultant (mean=3.61) is influential to be followed by the investors in choosing their unit trust fund. This indicating that they did follow the action and advice of unit trust consultants and co-investors who had succeed in investing unit trust fund. This clearly indicate that investor follow those who consider that can be trusted and successful as compared to believing in their own analysis and judgement.

Table 5: Source of Advice and Information

N= 333

Variables	**Mean**	**Std. Deviation**
Rational Behavior		
Seminar	3.37	1.04
Published Info.	3.56	0.96
Internet Review	3.35	1.02
Prospectus	3.32	1.05
Total Mean	**3.40**	
Herding Behaviour		
Well known Consultant	3.46	1.09
Market Sentiment	3.44	1.04
Successful investor	3.62	0.94
Co-investor	3.50	0.93
Friend & Relatives	3.47	1.00
Unit Trust Consultant	3.61	1.04
Total Mean	**3.51**	

Does 'Snake bite' effect influence unit trust investors' decision making?

Snake bite effect emerges when investors having experienced of huge losses and afraid to take risks and avoid investing in riskier securities. Table 5 shows the snake bite effect for investment of unit trust fund in the present study. It indicates that, after poor return was experienced by the investors, they would prefer to sell the fund (mean=4.25) followed by switching to another fund (mean=4.22) rather than keeping the fund (mean=4.08). They may afraid that the losses will persist. Snake Bite effect on the other hand lead the investors into learning more about the market sentiment and do the review via internet. Thus the findings of the present study found that the snake bite effect does influence unit trust decision making as they would rather sell the fund and switch to another fund. They seems to be more carefull in investing and analyze the market and do market review before decide to invest further.

Table 6 :Effects of Snake Bite Effects

N=333

	Mean	**Std. Deviation**
Keep the fund	4.08	0.83
Switch to another fund	4.22	0.65
Sell the fund	4.25	0.60
Market sentiment	3.93	0.63

Internet review	3.78	0.69
Friends and relatives.	3.64	0.77

Does illusion of Knowledge (overconfidence) influence Unit Trust Investors Decision Making?

Illusion of knowledge is sometimes also referring to 'Overoptimism and overconfidence'which tend to stem from the illusion of control and the illusion of knowledge.' (Montier, 2007). Thus, the illusion of knowledge is the tendency for people to believe that the accuracy of their forecasts increases with more information (Montier 2007).

Table 6 below shows the existence of illusion of knowledge among investors of unit trust fund in Malaysia. They believe that with extra information they have, it is easier for them to make decision and they are highly confident in their decision making. This clearly indicates that the more information they had the more confident they are. The effects of illusion of knowledge had made them to believe that the more information they had, the ease in selection of fund. Thus they are overconfident that they will select guaranteed profitable fund (mean=3.86); followed by winning fun (mean=3.83) as well as excellent ranking fund with mean of 3.76.

Table 7: Effect of Illusion of Knowledge

Variables	**Mean**	**Std. Deviation**
Winning Fund	3.83	0.90
LowCostFund	3.45	0.91
Self Needed Fund	3.75	0.88
Guaranteed profitable Fund	3.86	0.92
Excellent Ranking Fund	3.76	0.91
Reputable Company's Fund	3.71	0.90

Does effect of Pass Success leads to investors' overconfident and influence unit trust investors decision making?

Pass success emerges when investors having experienced of huge gain. Pass success is the motivational factors to the investors to have strong belief in their self-efficacy and optimist with the future market. Pass Success will also lead to overconfident. Hence, table 7below shows the effect of the pass success to the self confident level of the unit trust investors in Malaysia. Pass success lead the investors to invest more in good reputation company (mean=4.07) and winning fund (mean=3.74) but less on lowest cost fund (mean=3.29). However, they will still relying on excellent fund manager (mean=3.73) for advice and information. This indicate that the Unit Trust Investors in Malaysia are conscious with their investment and does not show an overconfident behaviour in their decision making as they choose less risky fund to invest and still refer or seek advice of the fund manager.

Table 8 :Effect of Past Success

N=333

Variables	**Mean**	**Std. Deviation**
Winning fund	3.74	0.88
Lowest cost fund	3.29	0.93
Good Reputation Co.	4.07	0.87
Excellent Fund Manager	3.73	0.91
Highest Ranking Fund	3.80	0.91

Discussion

Descriptive analysis in the present study indicates that Unit Trust Investors in Malaysia do herd and follow others in making investment decision. They followed the unit trust consultant and successful co-investors. This is because unit trust consultant is said to be expert in their field. They provide advice and information to the potential investors, investors and provide services to them. Investors also followed the successful co-investors. This is due to the fact that they provide them with proven strategy, ideas and advice which guide them in the world of uncertainty. The findings of the present study therefore is consistence with the study done by Ackert & Deaves, (2010)as it indicate that Malaysian Unit Trust investors are not force to herd but many of the investor is inexperience and lack of investment knowledge, therefore they have to follow the expert advice before making decision. Furthermore, in Malaysian context, most of the unit trust investment is through Unit Trust Agent (UTC) and very few is through personal investment.

In terms of overconfident behavior, Unit Trust Investors in Malaysia could be considered calculative in their decision making as they are cautious with their decision to invest particularly in unit trust investment. For those who experienced huge losses or having ‘snake-bite effect’, they will never keep the losses fund as they will immediately sell it and switch to more profitable fund. This indicated that unit trust investors will force sale of any loss fund and will not wait for the fund to increase in price. This is the evidence of lack of confident level among the Malaysian unit trust investors.

Similarly for those who experience gain from previous investment or having ‘past success effect’ was also cautious in their investment decision making as they will only choose investment with good reputation company and winning fund. At the same time they still seeking opinion from the fund manager. This indicated that the Unit Trust Investors in Malaysia are conscious with their investment and does not show an overconfident behaviour in their decision making.

However, with extra information, investors tend to possess illusion of knowledge and they show that they were confidence in their decision making. They are able to look for high ranking fund and good reputation manager for their fund. Investors also influenced by illusion of knowledge. They believe that by having extra information, they can select better fund and make better decision.

Limitations and recommendation for future research

This present study only concerns with the fundamental behaviour of unit trust investors. It uses only descriptive statistic to understand only two behaviours of the investors in this survey in the four states of Malaysia. Based on the above findings, the researcher suggests that further research on this area should include more variables of behavioral finance to contribute more on understanding of the behavioural side of the investors. It will help the investors to understand themselves, as the main enemy in investment is the investor himself.

Conclusion

The researchers believe that this study has contributed to some extend to understand the behaviour of the investors in unit trust fund investment. The success of an investor lie largely on his behaviour, and to understand one is the only weapon to conquer it.

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