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Influence of Behavioral Finance on Decision Making in the Business World

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What is Behavioral Finance?

- Propose psychology-based theories to explain stock market anomalies
- Assume information structure influences individual’s investment decisions & outcomes
- Potential implications of psychological factors affecting investor behavior in financial markets

Key Concepts of Behavioral Finance

**REPRESENTATIVENESS**

- A heuristic process by which investors base expectations upon past experiences, applying stereotypes.
- “If this has happened, then that will happen”

**OVERCONFIDENCE**

- People tend to place too much confidence in their ability to predict.
- “I am so smart! I will never lose!”

**FAMILIARITY**

- Employers must always also be cognizant of their employees’ tendency to invest in securities with which they are familiar.
- “If I buy a stock, I will always buy a stock I am familiar with!”

**ANCHORING**

- Refers to the individual’s reluctance to accept a loss.
- “I hate lost!”

**LOSS AVERSION**

- Investors have a psychological need to have some sort of justification for their decisions.
- “I want to rely on something to justify my decisions!”

Aim

Aim 1: Summarize different types of behavioral finance, analyze the reasons and connotations behind each type of behavioral finance, and discuss the methods of how to avoid and overcome it.

Aim 2: Illustrate the influences and consequences with regard to the investor behaviors in the real business world.

Research Strategy

- Consulted related books, articles, and journals about behavioral finance
- Summarized key concepts and influences with regard to the investor behaviors in the real business world.

References