



Behavioural Corporate Finance and its impact on IT sector decisions - An Indian perspective

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Preface

SDM Research Center for Management Studies (RCMS), since inception, has endeavored to promote research in the field of management education, in various ways. In this direction, in order to promote applied research, the Research Center has taken a unique initiative to encourage the faculty members to carry out various projects in the areas of management.

After completion of the projects, based on the peer review, reports are published with an ISBN number, by the Institute. The projects help the faculty members, and the students, who assist the faculty members for these projects, in various aspects, to gain practical knowledge, in the field of management.

The institute takes into account the time and resources required by the faculty members to carry out such projects, and, fully sponsors them to cover the various costs of the project work (for data collection, travel, etc).

From the academic viewpoint, these projects provide a unique opportunity to the faculty members and the students to get a first-hand experience, in investigating issues and concerns of targeted organizations or sectors, on a face to face basis, thereby, helping in knowledge creation and its transfer.

Mousumi Sengupta

Chairperson – SDM RCMS

Acknowledgement

I am deeply indebted to the early researchers who provided a track for the growing interest in the area of behavioral finance. I have tried an optimum possible effort with the assistance of my dear students of SDMIMD Mr.Manel Srikanth, Mr. Pavan and Mr.Parikshit to extract the psychological status of the decision makers of the IT sector. I am grateful to the managers who spent their little time to answer for the queries and provided their indeed support for making this report a complete one.

I also bow my truthful thanks to our Hon'ble Director Dr.N R Parasuraman for motivating me to work on this research report.

Thanks go to Dr. Mousumi Sengupta, Chairperson, SDM RCMS as well and to all my friends and family members who were supporting me while working on the report and assisted me either directly or indirectly prepare this report. This report being the complete extraction of practical and on-field happenings, there was a lot of support from the strategic level personalities from the firms. I also submit my thanks to all those officials.

I look forward to receiving suggestions for improving the future modifications and further developments in this research arena.

Kannadas S

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Executive summary

The study is focused mainly on the psychological influences which make a greater impact on the crucial financial decision making processes by the top level employees who are in the capacity of making decisions. The decision making processes are different from the person who own the organisation and the one who is employed for that position. The top level employee /decision makers who are in the capacity of taking a major financing, investing and dividend decisions which at times decide the fate of the organisation in the long run and progress of the organisation in the short run are not only thinking about the development of the organisation but also the power and position which they occupy.

The top level decision makers we often refer as strategic decision makers are not free from their psychological influences and personal biases. This study focuses on their personal /psychological biases/influences which dominate at times while taking making decisions. In this study it is an effort to extract the thought processes and the behavioral aspects of a decision maker in IT (information technology) sector. As the samples are corporate personalities, the sample size is constricted to 100 but the samples are spread across the four south Indian states i.e. Karnataka, Andhra Pradesh, Telangana and Tamil Nadu. This study is developed with the extraction of ideas from the earlier literatures and the objectives are set to avail the information and describe the scenario of psychological impact and their results in taking decisions.

A Qualitative questionnaire is framed and the decision makers from the IT industry are interviewed. Based on the responses, Percentage Analysis is applied to create a tabulated projection from the frequency distribution and denote the collected data for better considerate. This study is an initial step towards better understanding of reasons which include psychological /emotional aspects behind every financial decision. There is a vast scope for further study by applying statistical tools for comparison and hypothetical analysis in future. This study acts a base for future research work of the author. There is a reason for choosing IT industry for the study i.e. IT industry is most vulnerable on day to day basis with faster growth and spontaneous vicissitudes. So the decision making in such an industry plays a crucial role. Based on the percentage analysis the suitable recommendations are provided to have a control over the psychological errs and emotional gushes while taking the financial decisions. Traditional finance focuses on rationality of the decision maker, behavioral finance focuses on the irrationality of the corporate financial decision makers and highlights that the rationality is not universal but bounded. This study provides a nominal contribution in this direction.

Section I : Introduction

Behavioral finance

“An important subfield of finance. Behavioral finances use insights from the field of psychology and applies them to the actions of individuals in trading and other financial applications”-NASDAQ

Behavioral finance is a field of finance that proposes psychology-based theories to explain stock market anomalies such as severe rises or falls in stock price. Within behavioral finance, it is assumed the information structure and the characteristics of market participants systematically influence individuals’ investment decisions as well as market outcomes. (Investopedia, 2017)

The efficient market hypothesis proposes that at any given time in a liquid market, prices reflect all available information. There have been many studies, however, that document long-term historical phenomena in securities markets that contradict the efficient market hypothesis and cannot be captured plausibly in models based on perfect investor rationality. Behavioral finance attempts to fill this void by combining scientific insights into cognitive reasoning with conventional economic and financial theory. More specifically, behavioral finance studies different psychological biases that humans possess. These biases, or mental shortcuts, while having their place and purpose in nature, lead to irrational investment decisions. This understanding, at a collective level, gives a clearer explanation of why bubbles and panics occur. Also, investors and portfolio managers have a vested interest in understanding behavioral finance, not only to capitalize on stock and bond market fluctuations but also to be more aware of their own decision-making process.

History of behavioral finance (Finworx, 2017)

Behavioral finance has informal origins dating back to Selden’s 1912 *Psychology of the Stock Market*, as well as Fessinger’s 1956 study of cognitive dissonance and Pratt’s 1964 discussion on risk aversion and the utility function. However, the official start of behavioral finance is arguably 1979, which marks the release of Daniel Kahneman and Amos Tversky’s *Prospect Theory: A Study of Decision Making Under Risk*. They find that rather than calculating the universe of potential outcomes and selecting the optimal one, investors calculate outcomes against a subjective reference point, such as the purchase price

of a stock. Moreover, investors are loss adverse, which means they are willing to take on more risk in the face of losses, but become more afraid of risk when it comes to protecting their gains.

What’s notable about this first behavioral finance paper is the authors’ willingness to ask the question, “Is all what it seems?” with regards to traditional finance, as investment decisions in real life can drastically differ from their theoretical counterparts. More importantly, the paper posits that the notion of the rational man, or the “rational expectations wealth maximizer,” the bedrock upon which traditional finance is based, doesn’t actually exist. If traditional finance answers the question, “How should rational decision makers act in the face of risk?”, then behavioral finance answers the question, “How do real, actual humans act in the face of risk?”

Kahneman and Tversky were shortly thereafter joined by a third so-called founding father, Richard Thaler. In 1980, Thaler published a paper about investors’ propensity towards mental accounting, a phenomenon wherein they tended to view their money as being in separate and disparate pools depending on function (retirement fund, vs. emergency fund vs. college fund, etc.). Together, Thaler, Kahneman, and Tversky began a robust body of literature on how people make financial decisions, using psychology to bring the gap between real life and classic economic theory.

The work of the three “founding fathers” is frequently referred to as the “biases literature,” the study of all the behavioral biases that trip up average and professional investors alike. However, their work is just the tip of the behavioral finance iceberg.

Behavioural finance holds out the prospect of a better understanding of financial market behaviour and scope for investors to make better investment decisions based on an understanding of the potential pitfalls.

Over the past fifty years established finance theory has assumed that investors have little difficulty making financial decisions and are well-informed, careful and consistent. The traditional theory holds that investors are not confused by how information is presented to them and not swayed by their emotions. But clearly reality does not match these assumptions. Behavioural finance has been growing over the last twenty years specifically because of the observation that investors rarely behave according to the assumptions made in traditional finance theory.

Behavioural researchers have taken the view that finance theory should take account of observed human behaviour. They use research from psychology to develop an understanding of financial decision making and create the discipline of behavioural finance.

Behavioral finance is a new approach to financial markets that has emerged, at least in part, in response to the difficulties faced by the traditional paradigm. In broad terms, it argues that some financial phenomena can be better understood using models in which some agents are not fully rational. More specifically, it analyzes what happens when we relax one, or both, of the two tenets that underlie individual rationality. In some behavioral finance models, agents fail to update their beliefs correctly. In other models, agents apply Bayes' law properly but make choices that are normatively questionable, in that they are incompatible with SEU. (Thaler, 2003)

In the traditional framework where agents are rational and there are no frictions, a security's price equals its "fundamental value". This is the discounted sum of expected future cash flows, where in forming expectations, investors correctly process all available information, and where the discount rate is consistent with a normatively acceptable preference specification. The hypothesis that actual prices reflect fundamental values is the Efficient Markets Hypothesis (EMH). Put simply, under this hypothesis, "prices are right", in that they are set by agents who understand Bayes' law and have sensible preferences. In an efficient market, there is "no free lunch": no investment strategy can earn excess risk-adjusted average returns, or average returns greater than are warranted for its risk. Behavioral finance argues that some features of asset prices are most plausibly interpreted as deviations from fundamental value, and that these deviations are brought about by the presence of traders who are not fully rational. A long-standing objection to this view that goes back to Friedman is that rational traders will quickly undo any dislocations caused by irrational traders.

Suppose that the fundamental value of a share of Ford is \$20. Imagine that a group of irrational traders becomes excessively pessimistic about Ford's future prospects and through its selling, pushes the price to \$15. Defenders of the EMH argue that rational traders, sensing an attractive opportunity, will buy the security at its bargain price and at the same time, hedge their bet by shorting a "substitute" security, such as General Motors, that has similar cash flows to

Ford in future states of the world. The buying pressure on Ford shares will then bring their price back to fundamental value. Friedman's line of argument is initially compelling, but it has not survived careful theoretical scrutiny. In essence, it is based on two assertions. First, as soon as there is a deviation from fundamental value - in short, a mispricing - an attractive investment opportunity is created. Second, rational traders will immediately snap up the opportunity, thereby correcting the mispricing. Behavioral finance does not take issue with the second step in this argument: when attractive investment opportunities come to light, it is hard to believe that they are not quickly exploited. Rather, it disputes the first step

It is interesting to think about common finance terminology in this light. While irrational traders are often known as "noise traders", rational traders are typically referred to as "arbitrageurs". Strictly speaking, an arbitrage is an investment strategy that offers riskless profits at no cost. Presumably, the rational traders in Friedman's fable became known as arbitrageurs because of the belief that a mispriced asset immediately creates an opportunity for riskless profits. Behavioral finance argues that this is not true: the strategies that Friedman would have his rational traders adopt are not necessarily arbitrages; quite often, they are very risky

Behavioral Corporate Finance (Malcolm Baker, 2012)

Behavioral corporate finance aims to explain the financial contracts and the real investment behavior that emerge from the interaction of managers and investors. A complete explanation of financing and investment patterns therefore requires a correct understanding of the beliefs and preferences of these two sets of agents. The majority of research in corporate finance makes broad assumptions that these beliefs and preferences are fully rational.

Agents are supposed to develop unbiased forecasts about future events and use these to make decisions that best serve their own interests. As a practical matter, this means that managers can take for granted that capital markets are efficient, with prices rationally reflecting public information about fundamental values. Likewise, investors can take for granted that managers will act in their selfinterest, rationally responding to incentives shaped by compensation contracts, the market for corporate control, and other governance mechanisms.

Research in behavioral corporate finance replaces the traditional rationality assumptions with behavioral foundations that are more evidencedriven. The field is no longer a purely academic pursuit, as behavioral corporate finance is increasingly the basis of discussions in mainstream textbooks.

Behavioural finance studies the psychology of financial decision-making. Most people know that emotions affect investment decisions. People in the industry commonly talk about the role greed and fear play in driving stock markets. Behavioural finance extends this analysis to the role of biases in decision making, such as the use of simple rules of thumb for making complex investment decisions. In other words, behavioural finance takes the insights of psychological research and applies them to financial decision making. (Utkus, n.d.)

Behavioral corporate finance, and behavioral finance more broadly, received a boost from the spectacular rise and fall of Internet stocks between the mid1990s and 2000. It is hard to explain this period, both at the level of market aggregates and individual stocks and other securities, without appealing to some degree of investor and managerial irrationality.

Managers and corporate directors need to recognize two key behavioral impediments that obstruct the process of value maximization, one internal to the firm and the other external. The author calls the first obstruction behavioral costs. Behavioral costs, like agency costs, tend to prevent value creation. Behavioral costs are the costs associated with errors that people make because of cognitive imperfections and emotional influences. The second obstruction stems from behavioral errors on the part of analysts and investors. These errors can create gaps between fundamental values and market prices. When they do, managers may find themselves conflicted, unsure of how to factor the errors of analysts and investors into their own decisions. (Shefrin, 2001)

Proponents of value based management emphasize that with properly designed incentives, managers will maximize the value of the firms for which they work. As such, either they treat behavioral costs as simply another form of agency costs, or they deny the relevance of cognitive errors. In contrast, proponents of behavioral finance argue that behavioral costs are typically large, and cannot be addressed though incentives alone. This is not to say that incentives are immaterial. On the contrary, incentives are of critical importance. The point, however, is that there are

limits to incentives. If employees have a distorted view of what is in their own self-interest, or if they have a mistaken view of what actions they need to take in order to maximize their self-interest, then incentive compatibility, although necessary for value maximization, will not be sufficient.

Concurrent Evidences

Humans are not robots. Emotion and other illogical factors often influence our decisions. For example, you might know someone who invests in Facebook just because everyone he knows uses it. Or you might know someone who refuses to sell anything because he gets sentimental.

Behavioral finance is a field that combines cognitive and behavioral psychology with finance and helps explain the irrational choices people make. But how can behavioral finance help you make money or save money

To elucidate the same, we need to look at a few real world implications to make a better sense of it

Save for Retirement (Nerd Wallet, 2013)

In recent years, many policy makers have sought to use behavioral economics to influence workers' retirement savings. In Nudge, a book by Cass Sunstein and Richard Thaler, a leading behavioral finance professor, the two recommend that companies institute autopilot 401 (k) savings plans. Autopilot savings counteract reluctant savers who are prone to inertia by automatically enrolling them. Plans where participants need to opt-in have 68% rates of participation after 36 months of employment whereas plans where participants are automatically enrolled and need to opt-out to leave, have a 98% rate of participation.

Besides increasing the number of participants, behavioral finance principles can be applied to increase the amount saved. Thaler and Shlomo Bernartzi, a UCLA economics professor, developed a savings plan called Save for Tomorrow where participants committed to saving portions of their future income increases for retirement. When experimenting with the Save for Tomorrow plan, Thaler and Bernartzi found that within half a year, those who had previously had trouble saving, were saving three percent of their paychecks. After three and a half years, they were saving nearly 14 percent of their paychecks. In 2006, the Save for Tomorrow plan was incorporated into the Pension Protection

Act, a law that clarifies legal issues regarding automatic income reduction and helps specify appropriate default investments.

Fuller and Thaler Growth Fund (Nerd Wallet, 2013)

The Fuller and Thaler Growth Fund hopes to locate assets that are mispriced because of market under reaction. The Growth Fund focuses on companies in mature industries or who have financial difficulties. When evaluating companies, they use a three-step process. First, similar to standard investment firms, they evaluate companies using quantitative methods. Second, they determine whether a company's earnings increases are temporary or permanent. Third, if the companies have surprise earnings increases, they use behavioral analysis to see the market is underreacting. Since the companies have a history of financial difficulties or are in mature industries, the market suffer from anchoring biases or over confidence and believe the earnings to be a fluke.

Sentiment Analysis (Nerd Wallet, 2013)

One tool fund managers use to capitalize on investor irrationality is market sentiment analysis. Instead of using quantitative methods of evaluating the market, companies such as MarketPsych and Lexalytics mine the news and social media to evaluate trends in the market. Fund managers can then use the information to help determine market attitudes towards certain companies and use this information to locate mispriced assets.

Expert Analysis (Nerd Wallet, 2013)

Katsuhiko Okada, Kwansei Gakuin University Institute of Business and Accounting and CEO of Magne-Max Capital Management, uses behavioral finance principles to make investment decisions:

"Our fund aims to capture Japanese Investor psychology through text-mining the media sentiment in the market. We obtain massive textual data from the news media as well as social media such as Message boards and Twitter. In order to decompose the Japanese text into to an analyzable format, we use technologies developed in the area of Informatics, specifically Natural Language Processing (NLP) area. We then create a dictionary of words defining sentiment. At the moment, we have 6000 words and phrases in the dictionary that determine the sentiment of the investors to each one of the listed stocks in the Tokyo Stock Exchange. We call it "Sentiment Index."

We monitor corporate events and market events simultaneously and use the Sentiment index to filter out the stocks that we should go long or short. This sentiment filtering works in favor of the sharp ratio. It reduces the volatility of our NAV by substantial margin.

"Our hedge fund is composed of three practitioners and three tenured professors with three different disciplines: Finance, Informatics and Computer Science. In order to successfully apply behavioral finance to money management, an interdisciplinary system development is a must. Also, one has to have a flexible and adaptive decision making system because the history rarely repeats itself in the market."

Greg B. Davies, Head of Behavioral and Quantitative Investment Philosophy at Barclays, believes that behavioral finance will help spawn future innovations in finance:

"It is a mistake to think that learning more about behavioral (and classical) finance will on its own enable us to make better decisions in times of stress. We need structure and rules to help us govern our innate response to the immediate environment and context.

"In terms of innovations, there are a number of things that can help in the future. They are largely about making it easier for investors to govern their decisions over time – decision support tools. For example, there will increasingly be products designed to provide built in emotional insurance – they will help investors to both access the markets and simultaneously reduce anxiety along the journey.

"Investors will use technology to track decisions, identify individual proclivities and biases, and then provide assistance to improve decision making over time. We already use sophisticated psychometric profiling to establish individual's financial personality, and then use this to tailor portfolios that provide the greatest return, for the lowest emotional discomfort.

"We're developing tools to help investors build an Investor Constitution they can use to govern their investment decisions, thus rendering many of these abstract notions more concrete and usable."

Mike Ervolini, the CEO of Cabot Research, says fund managers benefit greatly from behavioral finance feedback tools:

“Cabot Research is the only behavioral finance consulting firm in the entire globe that helps equity portfolio managers. We’ve built analytics from the ground up just to help equity portfolio managers become more self-aware and improve. We allow them to use their own histories and we analyze their profits in such a way where they learn key things like how much of your profits come from buying or selling.

85% of the time a manager engages in a type of behavior that is costing the portfolio over 1% a year. And in 40% of the situations, the behavior is costing the portfolio over 2.5% a year. Traditional analytics can’t correct for these detrimental behaviors. In the future we will see fund managers increasingly relying on behavioral finance feedback.”

Victor Ricciardi, Goucher College Professor of Finance, believes that financial advisors with knowledge of behavioral finance can help investors make better decisions about retirement savings:

“I think seeing a financial advisor should be like seeing a doctor. You go every year to evaluate your investments and to correct for behavioral tendencies. Behavioral finance isn’t a replacement for standard finance—it’s complements our knowledge of how markets work. Behavioral finance can help people better understand their financial decisions and make better investment decisions. For example, many investors suffer from inattention bias. Financial advisors can help a client assess their level of risk tolerance and develop the proper asset allocation approach and then monitor their portfolio every year.”

BYU Professor Colbrin Wright believes that behavioral finance is best used to aid investors’ decision making and it is unclear whether or not funds using behavioral finance strategies are effective:

“Behavioral finance is still a very young field. It will be quite a while before we will truly know how to apply ideas from behavioral finance to investing. If you evaluate a lot of the funds that claim to have use behavioral finance strategies, it’s questionable whether or not they are successful. The successful funds end up using strategies that look very similar to value investing, which has been around for decades. For the academics that believe they can beat the market, they might be know-it-alls who have more than a little hubris.”

The financial crisis is more complex. The mispricing did not involve a new technology, but rather more

mundane mortgage finance made opaque through financial innovation and the creation of seemingly lowrisk derivatives. The buyers were not retail investors, but banks and money market mutual funds. Most importantly, the systemically important banks that created these securities had some of the largest exposures. It was as if Bank of America had held on to a large fraction of the Internet stocks that were underwritten in the late 1990s. There were equal parts traditional corporate finance frictions, like agency problems, signaling, and debt overhang, and behavioral distortions that led to both the credit bubble and the challenges of resetting bank balance sheets. The economic damage was further multiplied because banks themselves shouldered the losses (Malcolm Baker, 2012)

There is some evidence that some portion of the effect of stock prices on investment is a response to mispricing, but key questions remain. The actual magnitude of the effect of mispricing has not been pinned down. Even granting an empirical link between overpricing and investment, it is hard to determine the extent to which managers are rationally fanning the flames of overvaluation, as in catering, or are simply just as overoptimistic as their investors.

Behavioral finance in mergers and acquisitions (Malcolm Baker, 2012)

Shleifer and Vishny propose a markettiming model of acquisitions. They assume that acquirers are overvalued, and the motive for acquisitions is not to gain synergies, but to preserve some of their temporary overvaluation for longrun shareholders. Specifically, by acquiring lesservalued targets with overpriced stock (or, less interestingly, undervalued targets with cash), overvalued acquirers can cushion the fall for their shareholders by leaving them with more hard assets per share. Or, if the deal’s value proposition caters to a perceived synergy that causes the combined entity to be overvalued, as might have happened in the late 1960s conglomerates wave then the acquirer can still gain a longrun cushion effect, while offering a larger premium to the target.

An unresolved question in the ShleiferVishny framework is why managers would prefer a stockforstock merger to an equity issue if the market timing gains are similar. One explanation is that a merger more effectively hides the underlying market timing motive from investors, because the equity issue and investment decision are bundled.

Baker, Coval, and Stein consider another mechanism that can also help explain a generic preference for equity issues via merger. The first ingredient is that the acquiring firm faces a downward sloping demand curve for its shares. The second ingredient is that some investors follow the path of least resistance, passively accepting the acquirer's shares as consideration even when they would not have actively participated in an equity issue. With these two assumptions, the price impact of a stockfinanced merger can be much smaller than the price impact of an SEO. Empirically, inertia is a major feature in institutional and especially individual holdings data that is associated with smaller merger announcement effects.

Standard explanations for entering unrelated lines of business include agency problems or synergies, e.g., internal capital markets and tax shields. Likewise, moves toward greater focus are often interpreted as triumphs of governance.

Investor demand for conglomerates does appear to have reached a peak in 1968. Ravenscraft and Scherer find that the average return on 13 leading conglomerates was 385% from July 1965 to June 1968, while the S&P 425 gained only 34%. Diversifying acquisitions were being greeted with a positive announcement effect, while other acquisitions were penalized.

Klein finds a "diversification premium" of 36% from 1966 to 1968 in a sample of 36 conglomerates. Perhaps responding to these valuation incentives, conglomerate mergers accelerated in 1967 and peaked in 1968. Conglomerate valuations started to fall in mid-1968. Between July 1968 and June 1970, the sample followed by Ravenscraft and Scherer lost 68%, three times more than the S&P 425. Announcement effects also suggest a switch in investor appetites: diversification announcements were greeted with a flat reaction in the mid to late-1970s and a negative reaction by the 1980s.

Klein further finds that the diversification premium turned into a discount of 1% in 1969 to 1971 and 17% by 1972 to 1974, and a discount seems to have remained through the 1980s. Again, possibly in response to this shift in catering incentives, unrelated segments began to be divested, starting a long trend toward. Overall, while systematic evidence is lacking, the drivers of the diversification and subsequent refocus wave could be related to catering.

Behavioral finance in equity issues

The simple theoretical framework suggests that long-horizon managers may reduce the overall cost of capital paid by their ongoing investors by issuing overpriced securities and repurchasing underpriced securities.

Several lines of evidence suggest that overvaluation is a motive for equity issuance. Most simply, in the Graham and Harvey anonymous survey of CFOs of public corporations, two thirds state that "the amount by which our stock is undervalued or overvalued was an important or very important consideration" in issuing equity (p. 216). Several other questions in the survey also ask about the role of stock prices. Overall, stock prices are viewed as more important than nine out of ten factors considered in the decision to issue common equity, and the most important of five factors in the decision to issue convertible debt. Empirically, equity issuance is positively associated with plausible ex ante indicators of overvaluation. Pagano, Panetta, and Zingales examine the determinants of Italian private firms' decisions to undertake an IPO between 1982 and 1992, and find that the most important is the market-to-book ratio of seasoned firms in the same industry.

Lerner finds that IPO volume in the biotech sector is highly correlated with biotech stock indexes. Loughran, Ritter, and Rydqvist find that aggregate IPO volume and stock market valuations are highly correlated in most major stock markets around the world. Similarly, Marsh examines the choice between (seasoned) equity and long-term debt by UK quoted firms between 1959 and 1974, and finds that recent stock price appreciation tilts firms toward equity issuance.

In US data, Jung, Kim, and Stulz, Hovakimian, Opler, and Titman, and Erel, Julio, Kim, and Weisbach also find a strong relationship between stock prices and seasoned equity issuance. There are many non-mispricing reasons why equity issuance and market valuations should be positively correlated, of course. More specific evidence for equity market timing comes from the pattern that new issues earn low subsequent returns. In one of the earliest modern tests of market efficiency, Stigler tried to measure the effectiveness of the S.E.C. by comparing the ex post returns of new equity issues (lumping together both initial and seasoned) from 1923 to 1928 with those from 1949 to 1955. If the S.E.C. improved the pool of issuers, he reasoned, then the returns to

issuers in the latter period should be higher. But he found that issuers in both periods performed about equally poorly relative to a market index. Five years out, the average issuer in the preS.E.C. era lagged the market by 41%, while the average underperformance in the later period was 30%.

Much evidence suggests that investor sentiment varies over time in its strength and nature. For example, stock market bubbles can grow and pop within certain industries. Greenwood and Hanson exploit this observation. They find that net equity issuance by firms with different characteristics - size, share price, distress status, payout policy, industry, and profitability-helps to predict returns on portfolios defined on those characteristics. Their paper is also an interesting contribution to behavioral asset pricing and shows the value of a unified perspective. That is, the paper suggests how the misvaluation of firm characteristics at any given point in time, an otherwise difficult concept to measure, is betrayed by the financing activity and market timing motives of firms. We will see more results of this sort in the catering section.

If equity issues cluster when the market as a whole is overvalued, the net gains to equity market timing may be even larger than the underperformance studies suggest. Baker and Wurgler (2000) examine whether equity issuance, relative to total equity and debt issuance, predicts aggregate market returns between 1927 and 1999. They find that when the equity share was in its top historical quartile, the average valueweighted market return over the next year was negative 6%, or 15% below the average market return. Henderson, Jegadeesh, and Weisbach (2006) find a similar relationship in several international markets over the period 1990 to 2001. In 12 out of the 13 markets they examine, average market returns are higher after a belowmedian equity share year than after an abovemedian equity share year.

The equity market timing studies continue to be hotly debated. Some authors highlight the usual joint hypothesis problem, implicitly proposing that IPOs and SEOs deliver low returns because they are actually far less risky (and priced accordingly by investors). This notion strikes us as fanciful, but for more on this perspective, see Eckbo, Masulis, and Norli, and Eckbo and Norli. On a statistical point, Schultz highlights a smallsample "pseudo market timing" bias that can lead to exaggerated impressions of underperformance when abnormal performance is calculated in "event time." The empirical relevance of

this bias is unclear. Schultz (2003, 2004) argues that it may be significant, while Ang, Gu, and Hochberg, Dahlquist and de Jong and Viswanathan and Wei argue that it is minor.

Market timing can help resolve a puzzle of how or why issuers are able to raise outside equity when potential agency costs are high. In the traditional view of Jensen and Meckling, existing owners bear future agency costs up front when they raise new equity, potentially rendering outside equity prohibitively costly. This assumes of course that outside investors are rationally computing these costs. Chernenko, Greenwood, and Foley find that Japanese firms with the highest agency costs appear to raise capital when perceptions of agency costs are low. After listing, their subsequent performance is very poor, as if investors periodically ignored potential agency problems.

Viewed as a whole, the evidence indicates that market timing and attempted market timing play a considerable role in equity issuance decisions. We are constantly reminded that seasoned equity issuance that is not associated with mergers is still an infrequent event.

Behavioral finance and debt issue

A few papers have examined debt market timing - raising debt when its cost is unusually low. Survey evidence offers support for market timing being a factor in debt issuance decisions. Graham and Harvey find that interest rates are the most cited factor in debt policy decisions: CFOs issue debt when they feel "rates are particularly low." Expectations about the yield curve also appear to influence the maturity of new debt. Shortterm debt is preferred "when short term rates are low compared to longterm rates" and when "waiting for longterm market interest rates to decline." While the former statement would be consistent with the preference for a low interest rates to pump up earnings, the latter clearly indicates a skepticism in the textbook expectations hypothesis, which posits that the cost of debt is equal across maturities. At the same time, CFOs do not confess to exploiting their private information about credit quality, instead highlighting general debt market conditions

On the empirical side, Marsh in his sample of UK firms, finds that the choice between debt and equity does appear to be swayed by the level of interest rates. Guedes and Opler examine and largely confirm the survey responses regarding the effect of the yield

curve. In a sample of 7,369 US debt issues between 1982 and 1993, they find that maturity is strongly negatively related to the term spread (the difference between long and shortterm bond yields), which fluctuated considerably during this period. Is there any evidence that debt market timing is successful? In aggregate data, Baker, Greenwood, and Wurgler examine the effect of debt market conditions on the maturity of debt issues and, perhaps more interestingly, connect the maturity of new issues to subsequent bond market returns. Specifically, in US Flow of Funds data between 1953 and 2000, the aggregate share of longterm debt issues in total long and shortterm debt issues is negatively related to the term spread, just as Guedes and Opler find with firmlevel data. Further, because the term spread is positively related to future excess bond returns—i.e. the difference in the returns of longterm and shortterm bonds, or the realized relative cost of long and shortterm debt—so is the longterm share in debt issues. Perhaps simply by using a naïve rule of thumb, “issue shortterm debt when shortterm rates are low compared to longterm rates,” managers may have timed their debt maturity decisions so as to reduce their overall cost of debt. Of course, such a conclusion is subject to the usual riskadjustment caveats.

Behavioral finance and finance intermediation (Malcolm Baker, 2012)

Our focus is mostly on the financing decisions of firms, but financial intermediaries often play a critical role between firms and the ultimate investors. To the extent that capital market inefficiencies affect corporate finance, an interesting question is how intermediaries affect issuance and investment patterns and whether they play a stabilizing or destabilizing role. The role of financial intermediaries in behavioral corporate finance is an interesting question in its own right that deserves more research attention

Banks are not dissimilar to firms in that they have the same market timing motives to sell overvalued securities and buy back securities that are undervalued. Motivated by the crisis, Shleifer and Vishny model how financial intermediaries can take advantage of investor sentiment in this way through securitized lending—creating and selling overpriced assets. This creates a channel for banks to transmit sentimentdriven mispricing into real effects. In their model, banks retain a fraction of their loans. After a haircut, the value of these loans determines how much

they can borrow shortterm. When loan values are high, borrowing to make more of them and expand the balance sheet and finance more real investment is so profitable that it is worth the risk of having to liquidate their holdings if and when prices fall below fundamentals. As Charles Prince, the CEO of Citigroup, famously said in July 2007, “When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you’ve got to get up and dance. We’re still dancing.” As a result, far from being in a position to buy underpriced loans and stabilize the market, or finance new investment, banks can deepen a crisis.

The recent financial crisis has many different elements, from the decisions of individual borrowers to the ultimate purchasers of mortgage backed securities, and the involvement of numerous intermediaries, including mortgage brokers, mortgage banks, investment banks and other underwriters of mortgagebacked and other collateralized debt obligations (CDOs), ratings agencies, bond insurers, and the governmentsponsored entities, Fannie Mae and Freddie Mac. It is no surprise that there is not a tidy behavioral, or rational, explanation to its causes or its ultimate real consequences. Barberis makes significant progress in this direction. We do not have room to fully survey the burgeoning literature on the crisis here.

A behavioral view of the crisis starts with the observation that less than fully rational demand was the underpinning of twin bubbles in real estate and the debt contracts underlying real estate and other similar assets. There are a variety of explanations. For example, investors and ratings agencies neglected a rare but not zero probability bad state and overvalued quasiAAA securities in Gennaioli, Shleifer, and Vishny. Real estate and credit instruments were difficult to short, so differences of opinion may have led to overvaluation.

A defining feature of the financial crisis was that systemically important banks retained a significant exposure to all types of mortgage securities. There are a number of explanations. One is that they simply carried inventory of mortgages and were left with these securities on their balance sheets at the start of the financial crisis. Unlike Internet IPOs, CDOs required time and bank capital to assemble. A second explanation is that they intentionally took risks with limited bank capital, intentionally gambling on a positive outcome in the mortgage markets. This moral hazard view has shaped the debate in financial

reform. A challenge to this view is that the leadership of Bear Stearns and Lehman Brothers who were in a position to change leverage had a lot at stake, and indeed lost much of their wealth in 2008. A third explanation is that there were agency problems within the firm and the structured finance groups with the most information about these markets did not share with management. A final explanation is that they were convinced by their own marketing or, relatedly, they were focused on shortterm performance and the high prices of mortgage securities that changed hands prior to the crisis. This belongs to the section on less than fully rational managers. Whether this was overconfidence, cognitive dissonance, or a larger sociological phenomenon is hard to pin down.

Behavioral finance and dividend decisions (Malcolm Baker, 2012)

The catering idea has been applied to dividend policy. Long provides some early motivation for this application. He finds that shareholders of Citizens Utilities put different prices on its cash dividend share class than its stock dividend share class, even though the value of the shares' payouts are equal by charter. In addition, this relative price fluctuates. The unique experiment suggests that investors may view cash dividends per se as a salient characteristic, and in turn raises the possibility of a catering motive for paying them.

Aker and Wurgler test a catering theory of dividends in aggregate US data between 1963 and 2000. They find that firms initiate dividends when the shares of existing payers are trading at a premium to those of nonpayers, and dividends are omitted when payers are at a discount. To measure the relative price of payers and nonpayers, they use an ex ante measure of mispricing they call the "dividend premium," which is just the difference between the average market-to-book ratios of payers and nonpayers. They also use ex post returns, and find that when the rate of dividend initiation increases, the future stock returns of payers (as a portfolio) are lower than those of nonpayers. This is consistent with the idea that firms initiate dividends when existing payers are relatively overpriced.

Time-varying catering incentives shed much light on the "disappearance" of dividends. Fama and French (2001) document that the percentage of Compustat firms that pay dividends declines from 67% in 1978 to 21% in 1999, and that only a part of this is due to the

compositional shift towards small, unprofitable, growth firms which are generally less likely to pay dividends. Baker and Wurgler document that the dividend premium switched sign from positive to negative in 1978 and has remained negative through 1999, suggesting that dividends may have been disappearing in part because of the consistently lower valuations put on payers over this period. An analysis of earlier 1963-77 data also lends support to this idea. Dividends "appeared," "disappeared," and then "reappeared" in this period, and each shift roughly lines up with a flip in the sign of the dividend premium. In UK data, Ferris, Sen, and Yui find that dividends have been disappearing during the late 1990s, and that a dividend premium variable formed using UK stocks lines up with this pattern. Supposing that dividend supply does respond to catering incentives, why does investor demand for payers vary over time in the first place? One possibility is that "dividend clienteles" vary over time, for example with tax code changes. However, in US data, the dividend premium is unrelated to the tax disadvantage of dividend income, as is the rate of dividend initiation. Shefrin and Statman develop explanations for why investors prefer dividends based on self-control problems, prospect theory, mental accounting, and regret aversion. Perhaps these elements vary over time. Baker and Wurgler argue that the dividend premium reflects sentiment for "risky" nonpaying growth firms versus "safe" dividend payers, since it falls in growth stock bubbles and rises in crashes; Fuller and Goldstein show explicitly that payers outperform in market downturns. Anecdotal evidence suggests that some investors flock to the perceived safety of dividends in gloomy periods, and bid up payers' prices, at least in relative terms, in the process.

There are limitations to a catering theory of dividends. For one, it is a descriptive theory of whether firms pay dividends at all, not how much—in US data, at least, the dividend premium does not explain aggregate fluctuations in the level of dividends. DeAngelo, DeAngelo, and Skinner report that the aggregate dollar value of dividends has increased in real terms, as dividends have become concentrated in a smaller fraction of traded firms. Also, the theory works better for explaining initiations than omissions, and it has little to say about the strong persistence in dividend policy. Catering, like agency or asymmetric information or taxes, is best viewed as one element in an overall theory of dividend policy. As we will see later, it is not even the only approach to dividends that behavioral corporate finance offers.

Section II : Review of literature

(Fromlet, 2001) Exhibit that the psychology and irrational behavior do matter on financial markets. This is an important conclusion per se, but it is even more important to draw practical conclusions. Are there any lessons to be learned? Without doubt, there are conclusions from analysis of behavioral factors that can help investors to avoid mistakes. (The Table 1 gives an easily understandable summary of some of the conclusions.) Avoiding mistakes is what the researcher would like to call defensive behavioral finance applications. Tests have been made in order to find out what investors actually do versus what they ought to do if they were acting rationally. Experience from decision traps, biases, over- and under-reactions, risk acceptance, and so on, can be used as strategic tools in asset management, even in an offensive application. In the United States there is an increasing number of academics that are concentrating their efforts on behavioral finance, both when it comes to research and education.

(Heaton, 2002) Debate two dominant features First, optimistic managers believe that capital markets undervalue their firm's risky and may pass up positive net present value projects that must be financed externally. Optimistic managers overvalue their own corporate projects and may wish to invest in net present value projects even when they are loyal to shareholders. These results imply under investment-overinvestment tradeoff related to free cash flow, without asymmetric information or (rational) agency cost theories. The model suggests that the effects of free cash flow are ambiguous. Optimistic managers will sometimes decline positive NPV projects if those projects require outside financing. Free cash flow in an amount required to fund positive net present value projects can socially costly under-investment. In a world with optimistic managers, therefore, it is that mechanisms that force the firm to pay out all cash flow and acquire external finance necessarily good mechanism.

(Price, 2003) CEOs could make things easier for themselves if, before embarking on complex performance-improvement programs, they resolute the extent of the change required to achieve the business outcomes they seek. It can be broadly mentioned that they can choose among three levels of change. On the most straightforward level, companies act directly to achieve outcomes, without having to change the way people work; one example would be divesting noncore assets to focus on the core

business. On the next level of complexity, employees may need to adjust their practices or to adopt new ones in line with their *existing* mind-sets in order to reach, say, a new bottom-line target. An already "lean" company might, for instance, encourage its staff to look for new ways to reduce waste, or a company committed to innovation might form relationships with academics to increase the flow of ideas into the organization and hence the flow of new products into the market.

(Nofsinger, 2008) The behavioral finance paradigm for explaining how agents behave and how their behavior might affect financial markets looks like it is here to stay. Although conducting research on behavioral finance poses many challenges and hurdles, the authors in this special issue have (to a high degree) successfully addressed those challenges. The scholar suspect that even more of those challenges and hurdles will be overcome in future research. Our overall goal with this special issue was to help bring behavioral finance theories to Asian financial markets. The Asian financial markets represent a fruitful testing ground for behavioral finance researchers: the papers in this special issue represent solid proof of this assertion. The scholar hope that readers will enjoy and benefit from the contents of these studies as much as the scholar enjoyed and benefited from putting this issue together. And, of course, the scholar hope these papers help spur the next generation of behavioral finance research.

(Accountants, 2008) Entrepreneurial spirit and business judgement (that human ability to weigh intangibles and ambiguity) will always be important in decision making. But the risks of personal bias, repeating past mistakes, acting on guesses or following hunches unnecessarily, can be limited if a culture of evidence based decision making is fostered. Providing evidence in the form of organisational financial and management information has long been the basis for Chief finance officers' role in the decision making process. Supporting the strategic planning process and providing the metrics and analysis to support evidence based decision making are important. But these will no longer suffice. The CIMA Forum believes that CFOs have a much bigger contribution to make. The emphasis in recent years has been on organisational financial controls, risk management and providing transparency in reporting. But the trend in organisational financial decision makings expansion continues towards management skills and supporting decision making.

(Hackbarth, 2009) In this nascent literature in financial economics considers corporate managers' personality traits. The primary objective of this article is to study the interaction between financing and investment decisions from a behavioral perspective, i.e., in the presence of managerial optimism and overconfidence. The researcher develops a contingent claims approach that integrates a simple real options model into an earnings-based capital structure environment. Analytic expressions for arbitrary beliefs, with rational beliefs as a special case, are derived from the model in which managers' financing and real option exercise decisions are endogenously linked to each other by optimality conditions. Focusing on this behavioral perspective, the researcher find managerial biases can play a positive role because of two balancing economic effects. First, biased managers choose higher debt levels than rational managers, exacerbating underinvestment. Second, biased managers invest earlier than rational managers, attenuating underinvestment. The latter dominates the former effect for mild biases and hence the benefits of mild biases exceed their costs. Debt overhang agency costs decline and investor welfare improves. The bottom-line of this study is, however, the more general, agency-theoretic observation that mildly biased managers can ameliorate bondholder–shareholder conflicts (e.g., debt overhang, asset substitution, or asset stripping). Intuitively, managerial biases can act as commitment devices for implementing second-best strategies of a levered firm that are closer to first-best real option exercise strategies.

(Sibony, 2010) In case of a large business decision your company made recently: a major acquisition, a large capital expenditure, a key technological choice, or a new-product launch. Three things went into it. The decision almost certainly involved some fact gathering and analysis. It relied on the insights and judgment of a number of executives (a number sometimes as small as one). And it was reached after a process sometimes very formal, sometimes completely informal turned the data and judgment into a decision. The research indicates that, contrary to what one might assume, good analysis in the hands of managers who have good judgment won't naturally yield good decisions. The third ingredient is the process which is also crucial. The researcher discovered this by asking managers to report on both the nature of an important decision and the process through which it was reached. In all, it is studied 1,048 major decisions made over the past five years,

including long term/short term project investments in new products, M&A decisions, and large capital expenditures.

(Haiss, 2010) Incentive structures faced by bank managers are central to mitigate herding, as myopic and asymmetric reward structures in many banks were among the key drivers of the excess of the most recent financial boom (Butler, 2008). Regulators should give consideration to the impact of regulation on the incentives of compensation schemes within banks and the extent to which they induce prudential behavior. Incentive structures also need to become a supervisory issue. The banks themselves also need to sort out features of reward systems that provide triggers towards herding and procyclicality, e.g., incentives that are not in the long run in the interests of the banks themselves.

(Yazdipour R. , 2011) Three central decisions in entrepreneurship and entrepreneurial finance - entry/seed funding, industrial financing/long term/short term project investment, and growth/exit - are deliberated and this study is made for applying the behavioral corporate finance theories and concepts to better understand the involved decision processes, and consequently, to help improve the decision making process for both entrepreneurs and venture capitalists. The behavioral corporate finance approach is important because the traditional corporate finance has remained silent on the first issue, and the Agency Theory (organisational financial contracting), which is effectively the only theory that is applicable to issues in entrepreneurial finance, has produced mixed empirical results. Although the focus is on individual decision making with tremendous psychological influence and under highly uncertain entrepreneurial environments, the suggested risk framework and the related discussions can be extended to decision making in other uncertain environments.

(Baker, 2012) The behavioral corporate finance literature has matured to the point where one can now sketch out a handful of canonical theoretical frameworks and use them to organize many dozens of empirical studies. The review of this evidence indicates that behavioral approaches offer a useful complement to the other corporate finance paradigms. They deliver intuitive and sometimes quite compelling explanations for important industrial financing and investing patterns, including some that are difficult to reconcile with existing theory.

(Marchand, 2012) An efficient market is one where the market is an unbiased estimate of the true value of the long term/short term project investment. It is the degree to which stock prices reflect all available and relevant information. Market efficiency was introduced by Fama (1970), whose theory efficient market hypothesis (EHM) stated that is not possible for an investor to outperform the market because all available information is already built into stock prices. In a rational world corporate investors make organisational financial decision to maximize their risk-return tradeoff. They have all the information they need on estimated return and risk and they make their choices according to this information. In traditional theories of finance long term/short term project investment decisions are based on the assumption that corporate investors act in a rational manner. This means that they behave rationally so they earn returns for the money they put in stock markets. To become successful in the stock market it is essential for corporate investors to have rational behavior patterns. Rational behavior is also required to be organisational financial successful and to overcome tendencies. The conclusion can be drawn that corporate investors not always act in a ration manner due to the cognitive and psychological errors they have to deal with. They are influence by behavioral factors that are important in organisational financial markets because they influence the corporate investors who make the organisational financial decisions. Busenitz and Barney (1998) state that if the environment is uncertain and complex, biases and heuristics can be an effective and efficient aim to decision making. Under these circumstances a more comprehensive and careful decision making is not possible. Biases and heuristics present an effective way to estimate the appropriate decisions.

(Kannadhasan, 2015) Decision-making is a complex activity. Decisions can never be made in a vacuum by relying on the personal resources and complex models, which do not take into deliberation the situation. Analysis of the variables of the problem in which it occurs is mediated by the cognitive psychology of the manager. A situation based on decision making activity encompasses not only the specific problem faced by the individual but also extends to the environment. Decision-making can be defined as the process of choosing a particular alternative from a number of alternatives. It is an activity that follows after proper evaluation of all the

substitutions. They need to update themselves in multidimensional fields so that they can accomplish the desired results/ goals in the competitive business environment. This needs better insight, and understanding of human nature in the existing global perspective, plus development of fine skills and ability to get best out of long term/short term project investments. In addition, corporate investors' have to develop positive vision, foresight, perseverance and drive. Every investor differs from others in all aspects due to various factors like demographic factors which includes socio-economic background, educational attainment level, age, race and sex. The most crucial challenge faced by the corporate investors is in the area of long term/short term project investment decisions. An optimum long term/short term project investment decision plays an active role and is a significant contemplation. In designing the long term/short term project investment portfolio, the corporate investors should consider their organisational financial goals, risk tolerance level, and other constraints. In addition to that, they have to predict the output mean- variance optimization. This process is better suited for institutional corporate investors; it often fails for individuals, who are susceptible to behavioural biases. In the present scenario, behavioural finance is becoming an integral part of the decision-making process, because it heavily influences corporate investors' performance. They can improve their performance by distinguishing the biases and errors of judgement to which all of us are prone. Understanding the behavioural finance will help the corporate investors to select a better long term/short term project investment instrument and they can avoid repeating the expensive errors in future. The apposite issues of this analytical study are how to minimize or eliminate the psychological biases in long term/short term project investment decision process.

(Nagarajan, 2015) The study was aimed at looking into the behavioural aspects decision making of software project management in in-house software development centres in India. It was considered to investigate the relationship between sector type and major organisational factor as perceived by the in-house software project head and the collective behavioural perception of in-house software project heads on organisational financial and human resource management, project management practices and supportive skills and environment where in-house

development happens. The study was based on survey explorative design by using a structured questionnaire which was pre-tested with 35 in-house software project heads. It was also found out that there is a relationship between psychological influence and organizational factor as perceived by the in-house software project head. In-house development centre heads need to be concerned with the behavioural aspects of developer community in their organisation, and beginning to consider these variables in their management practices will surely help to turn out successful projects both quantitatively and qualitatively. It is time to prove through further research and experiments that the behavioural aspects of software project management in the in-house development centres in India still need to catch up with the practices to match the global standards as set by major software development companies both in India.

(Ejimabo, 2015) It is explored that the influence of decision making in organizational leadership and management activities that impact creativity, growth and effectiveness, success, and goal accomplishments in current organizations. The qualitative pattern was used in order to gain in-depth knowledge and considerate of the issues and challenges influencing effectiveness, and success among organizational leadership and managements in business practices. The author being committed and determined to discovering a pattern of meaning through experience, systemic thinking, assessment, and creative analysis used the Kurt Lewin leadership philosophical underpinning approaches of leadership namely: autocratic, democratic, and laissez-faire methods of leadership decision making processes in the context of this study, with the aim of discovering the main factors rather than specific variables and outcomes affecting decision making among business leaders. Roughly, four hundred past and current business executives and managements partaken in this study. Data was collected through structured interviews and surveys. The results that emerged from the study indicated that there is a great need for change and improvement in decision making among organizational executives while accommodating technology, diversity, globalization, investment and dividend policy, teamwork and effectiveness.

(Misra, 2016) Neuro-scientific research has now crowned the modern research era throughout

the globe. Here is an attempt to focus on Cognitive Neuro science, of which Decision Making Style (DMS) is chosen as one of the imp aspect of it that affects our behavioral manifestation. Almost all activities, achievements, objectives, success and failure of our life is dependent on our decision making process. The multiple system of decision making lead to have a look to the reasons about why people differ in their decision making style. With this idea the study aims at analyzing the implicit and explicit analysis of emotional and cognitive parts of Neuro-decision making among the potential executives in their summer training programme, of corporate engineer, to create awareness among the employees on the neuro scientific management of decision making, and its effects in the work place situations. Further out of several other components of DMS, like, Directive, intuitive, Behavioral, Spontaneous(Automatic), sensitive, Sequential, logical, Global, personable, Sensing, thinking, feeling, reasoning, emotional, etc., the Sequential, logical, Global, personable points were analyzed as the effective components of DMS. An attempt has been made in this paper to build brain-based Neuro scientific models, capable of predicting decision making behaviors of the executives in organizational (HRM) sectors.

(Lobão, 2016) The aim of this book is to demonstrate how the personal traits of managers affect the decisions made in the firm, especially organisational financial decisions. The psychological qualities of individuals holding management positions have a decisive effect on, for instance, their industrial financing and capital budgeting decisions or their dividend policy. It will also become clear that the psychological profile of each manager will provide an explanation for the organisational financial decisions made beyond the scope of the company and its business sector. There is already a significant number of theoretical and empirical works that show the clear effect of psychological variables on corporate investors' decisions in organisational financial markets. This book proposes to expand the scope of that analysis to include the study of those effects on business managers. Introducing psychological factors in the study of organisations and in the theory of the firm is a current challenge that must be met. The author ought to focus more on the way managers think and behave in order to improve how businesses are run.

Section III : Research methodology

Statement of the problem

In the arena of growing corporate complexities rational decision makers are found to be available but it is mere bounded rationality. The available information and beliefs make them to take decisions based on the critical analysis of the scenario but in reality the psychology play a key role in taking decisions knowingly or unknowingly. At times there are success in decision making as the past experience and the provided information are sustainably true and practical. But many a time the decisions culminate in erratic results. There are many psychological aspects and beliefs play a key role in decision making which need to be found and analyzed.

Objectives of the study

- To know the crucial corporate behavioral factors influencing the financial decisions in the IT concerns.
- To find out the major emotional as well as herding behavior which influence the end results IT concern decision makers
- To recommend the suitable precautionary measures and solutions to overcome the negative end results of wrong financial decisions which are influenced by the inappropriate corporate decision making approach.

Issues for the study

- Psychological factors affecting the corporate financial decision makers in IT sector
- Impact of Personal benefits and organizational interests towards the decision makers in IT sector
- Result of influenced financial decisions, while reaching the organizational goals

Research questions

- Is there any impact of individual corporate behaviour on decisions taken by them?
- What is the role of corporate behaviour during major decisions?

- What type of impact will be created by the psychological factors and organizational interest bases?

Research design

Descriptive research design

Descriptive research is a method designed to portray the participants in an accurate manner. There are three ways to avail the data i.e. observations, viewing and recording the samples. The method of case study is to have an in-depth study of an individual or a group of individuals. The method of conducting survey with a structured questionnaire does provide the required information to describe the scenario and the culmination of the scenario.

Here the samples are interviewed with the questionnaire and the data is availed for a detailed description and the data is tabulated in such a way to make it ready for a quick grasp of the existing development.

Data collection method

Depth interview through questionnaire with decision making in IT sector level

It's important to start with a good literature search and in depth interviews are most appropriate for situations in which you want to ask open-ended questions that elicit depth of information from relatively few people (as opposed to surveys, which tend to be more quantitative and are conducted with larger numbers of people).

Depth interviews provide the structure to ensure that these conversations are both well-organized and well-suited to your purpose. While time-consuming and labor-intensive, in-depth interviews can provide rich data to inform Extension programming.

Sample size: 100

Huge sample sizes generally lead to increased precision when estimating unknown parameters. In some situations, the increase in accuracy for larger sample sizes is minimal, or even non-existent. This can result from the presence of systematic errors or strong dependence in the data, or if the data follow a heavy-tailed distribution.

Sample sizes are judged based on the quality of the resulting estimates. Alternatively, sample size may be assessed based on the power of a hypothesis test.

Moreover the previous researches have chosen around 50 to 75 samples (found out through literature review) for similar studies and accomplished the research successfully.

Type of sampling applied: Simple random sampling

A simple random sample is meant to be an unbiased representation of a group. An unbiased random selection of individuals is important so that if a large number of samples were drawn, the average sample would accurately represent the population. However, this does not guarantee that a particular sample is a perfect depiction of the population. Simple random sampling merely allows one to draw externally valid conclusions about the entire population based on the sample. Each individual is chosen randomly and exclusively by chance, such that each individual has the same probability of being chosen at any stage during the sampling process.

Advantages are that it is free of classification error, and it requires minimum advance knowledge of the population other than the frame. Its simplicity also makes it relatively easy to interpret data collected in this manner. For these reasons, simple random sampling best suits circumstances where not much information is available about the population and data collection can be efficiently conducted on randomly distributed items, or where the cost of sampling is small enough to make efficiency less important than simplicity.

Tools applied for analysis

- Statistical interpretation aids charts and graphs- for quick understanding of the circumstance
- Percentage analysis - to describe the scenario and is applied to create a contingency table from the frequency distribution and represent the collected data for better understanding.

Location for the study

South Indian states (Karnataka, Tamilnadu, Andhra Pradesh, Telangana and Kerala)

Section IV : Theoretical and Practical background of the study

Role of behavioral finance in Corporate decision making

The Executives when they think of firms financing and investment decisions are often guided by an image of an efficiency in the markets. But many a times the markets are not as efficient as they believe and sometimes the executives themselves are not rational and the decision which they take will be biased. This is where the new academic of research the Behavioral Corporate finance plays the role. It would force a researcher to reexamine the traditional ways of compensation strategies and conventional ideas. Behavioral Corporate finance is a sub discipline of behavioral finance integrates the human psychology and economics into the study of judgment of a human mind and the biases it makes under various uncertainty conditions.

Behavioral corporate finance argues that in many senses, corporations are natural arbitrageurs. The researchers have proved that it is much easier for a CFO to issue more shares when a company is overvalued than it is for a hedge fund to short the shares which are overvalued. The consequences which the CFO will face if the shares are not overvalued are modest compared to that of the manager of hedge fund. The research says that the job security advantage that the CFO has over the manager of the hedge fund will affect the type of decision taken.

The behavioral corporate finance has started looking at the financing and investing decisions of the executives within the firm. If the executives are overoptimistic and overconfident thus affecting the decision about capital structure. So is there way to push them towards optimal behavioral is the question answered by the researching on Corporate Behavioral finance. The researchers have said that there is CEO effect on decisions with respect to capital structure. CEO effect means decisions taken based on his/her personal style rather than based on set criteria that has been determined by the firm. Financially aggressive CEOs leverage more and hold less cash on the balance sheet and grow their firms through acquisitions. Conservative leaders have more cash on the balance sheet and grow more through internal investments. These different styles of capital management have real effects on corporate

performance. Behavioral finance research indicates that traditional ideas of corporate governance may be too simplistic. Theories from behavioral finance are at the forefront of explaining differences in corporate financial policies and capital structures. Most important, however, behavioral corporate finance has reintroduced humanity - in all its complexity and subtlety - into corporate finance, where indeed it belongs. (www.strategy-business.com, 2004)

There are 3 types of problems that require decision making on part of the entrepreneurs and investors. They are

- Entry/Seed Funding Decisions
- Financing/Investment Decisions
- Growth/Exit Decisions

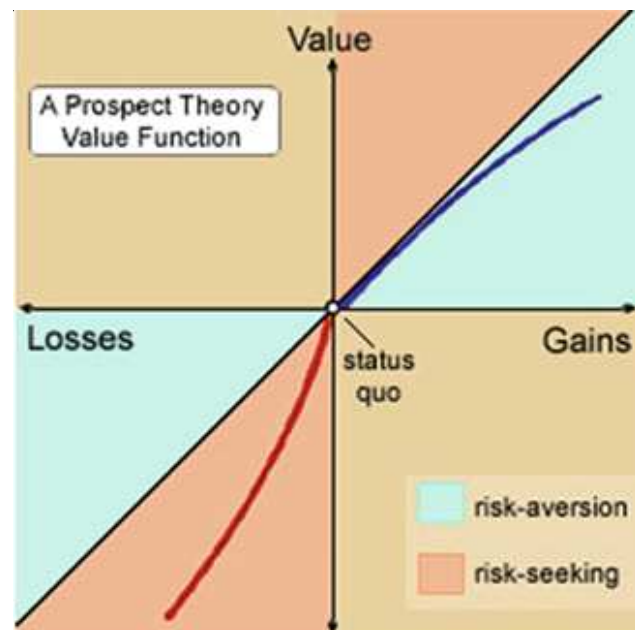
In the first problem of Entry/Seed Funding Decisions focus here is on the application of behavioral finance and economics theories to entry/seed funding decisions – jointly defined as launch decisions. Such joint decisions involve two separate but related decisions by both an entrepreneur and a Venture capitalist. The reason for discussing and analyzing the two decisions together is a practical necessity. That is, the decision to enter a business by an entrepreneur alone does not mean much; unless, she can convince a VC to fund her start-up. With this in mind, there are two central questions that both entrepreneurs and VCs face in a launch decision. (Yazdipour R. , 2011)

The second section is based on the belief that if we can better understand the types of risks and uncertainties that are involved in and around the entrepreneurial finance problems the decision taken with respect to the financing and investments will be low in biases. It is also argued that the manager when we take decision with respect to this stream will be more focused on his past experiences and learnings rather than the present feasibility of the outcome.

The stage of growth and exist decisions when the manager has to take one of the important decisions of his career whether he has exit from the business which the company is currently operating in or whether to growth the company in that business. Here as a manager your personal creditability and ability will come under the scanner where existing the business means that the manager is incapable to lead his team. If he is a rational thinker a puts the company first, he would surely think wisely and do

what is good for the company. The manager who has a higher risk appetite would surely take higher risk and deal more complex situations.

So we can see how mindset of an individual will affect the decisions he or she will take. This might have an adverse impact on the future prospects of the company, any blunders or mistakes would once for all kill the company forever and any masterstrokes from the manager may have a positive impact on the company's growth for year' to come. It all depends on whether the decision making in a company is entirely depended on one CFO or multiple ones as the decision to invest or to invest will be depended on that CFO alone and not the company. In these circumstances the Behavioral finance theory has a major role to play.



Managers are "optimistic" when they systematically overestimate the probability of good firm performance and underestimate the probability of bad firm performance. This assumption finds support in a large psychological literature demonstrating that people are, in general, too optimistic. That literature presents two pervasive findings (e.g., Weinstein 1980) that make optimism an interesting subject of study for corporate finance researchers.

First, people are more optimistic about outcomes that they believe they can control. Consistent with this first experimental finding, survey evidence indicates that managers underplay inherent uncertainty, believing that they have large amounts of control over the firm's performance. Second, people are more optimistic about outcomes to which they are highly committed. Consistent with the second experimental finding,

managers generally appear committed to the firm's success probably because their wealth, professional reputation, and employability partially depend on it (e.g., Gilson 1989). The approach taken here departs from the standard assumption of managerial rationality in corporate finance.

Behavioral approaches are now common in asset pricing, of course, but little work in corporate finance has dropped the assumption that managers are fully rational. This is somewhat surprising considering that the common objections to behavioral economics have less vitality in corporate finance than in asset pricing. The "arbitrage" objection (rational agents will exploit irrational agents) is weaker, because there are larger arbitrage bounds protecting managerial irrationality than protecting security market mispricing. The most obvious "arbitrage" of managerial irrationality—the corporate takeover—incurs high transactions costs, and the specialized investors who pursue takeovers bear much idiosyncratic risk.

Arbitrage strategies short of a corporate takeover are difficult to implement, because managerial decisions usually concern assets (including human assets) that trade in markets without short sale mechanisms or other derivative assets that make arbitrage possible. The "learning" objection (irrational agents will learn from experience to be rational) is also weaker, because important corporate financial decisions about capital structure and investment policy are more infrequent than trading decisions, with longer-delayed outcomes and noisier feedback. Learning from experience is less likely in such circumstance.

We assume the manager is optimistic about the value of the firm's assets and investment opportunities. He balances two conflicting goals. The first is to maximize *perceived* fundamental value. To capture this, we augment fundamental value with an optimism parameter γ , $(1+\gamma) f(K) - K$

where f is increasing and concave in new investment K . Note that here, the manager is optimistic about both the assets in place (f can include a constant term) and new opportunities. Once again, if traditional market imperfections cause the Modigliani and Miller (1958) theorem to fail, financing may enter f alongside investment. The manager's second concern is to minimize the *perceived* cost of capital. We assume here that the manager acts on behalf of existing investors, because of his own stake in the firm and fiduciary duty. This leads to a similar setup to the market timing objective in Section 2.2, except that an optimistic manager never believes there is a good time

to issue equity. In particular, since the capital market is efficient and values the firm at its true fundamental value of fK , the manager believes that the firm is undervalued by γf , and thus in selling a fraction of the firm e he perceives that existing, longrun shareholders will lose.

The first condition is about investment policy. Instead of setting the marginal value created from investment equal to the true cost of capital, normalized to be one here, managers overinvest, to the point where the marginal value creation is less than one. The more optimistic (γ) is the manager and the less equity (e) he is forced to raise in financing investment, the greater the problem. To the extent that the manager has to raise capital by issuing equity, the cost of capital is scaled up by the same factor as the manager's over-optimism scales up the marginal product of capital, so raising equity offsets the distortion in investment caused by overoptimism. (Behavioral Corporate Finance: A Survey, 2005)

Investment policy. If there is no optimal capital structure, so that f_e is equal to zero, the manager will not issue equity, setting e to zero, and there is no interaction among financing, internal funds, and investment. In this case, the optimistic manager will clearly overinvest: fK is less than unity. In Heaton (2002) and Malmendier and Tate (2005), there is an optimal capital structure, or more precisely an upper bound on debt. If the manager needs equity to invest (here, f_e greater than zero), the degree of overinvestment falls. Needing equity is akin to having little cash or cash flow available for investment.

Thus in this setup, investment can be strongly related to current cash flow and profits, controlling for investment opportunities. This leads to a behavioral foundation for the Jensen (1986) agency costs of free cash flow. But instead of receiving private benefits of control, managers are simply optimistic and overinvest from current resources as a result. Leverage reduces the degree of overinvestment by increasing f_e , thereby increasing equity issues e and reducing K . (Behavioral Corporate Finance: A Survey, 2005)

Financial policy. An optimistic manager never sells equity unless he has to. If there is an upper bound on leverage (f_e greater than zero, here), optimism predicts a pecking order of financing decisions: The manager relies on internal capital and debt and uses outside equity only as a last resort. Again, other imperfections may mitigate the aversion to equity. If the manager is risk averse with an undiversified

position in the firm's equity, for example, he may wish to issue equity even though it is below what he thinks it to be worth.

Managerial overconfidence can have different effects on capital structure than optimism, Hackbarth (2009) argues. If overconfidence is modeled as underestimating the risk of earnings, managers may view their debt as undervalued and too expensive as a source of capital. The convexity of equity, on the other hand, leads managers to view their equity as overvalued. This reverses the pecking order that obtains under optimism. Suffice to say that theoretical predictions about the effect of optimism and overconfidence on capital structure are somewhat sensitive to the modeling framework.

Other corporate decisions. It is not as easy to incorporate other decisions into this Framework. Consider dividend policy. If the manager is more optimistic about future cash flow and assets in place than outside investors, he might view a dividend payment as more sustainable. On the other hand, if he views future investment opportunities, and hence funding requirements, as greater, he might be reluctant to initiate or increase dividends and retain internal funds instead. This analysis requires a more dynamic model of investment and cash flow and a decomposition of firm value into assets in place and growth opportunities.

It is obvious from casual observation that top managers "matter," in that they have the power to make decisions that affect investment and financing policy and firm value. There is also systematic evidence. Bertrand and Schoar (2003) find that individual managers have investment and financing styles and preferences, possibly inherent and possibly based on beliefs shaped by beliefs that they bring from previous to new employers. For example, CEOs that use bigger mortgages for their own home purchases also use more leverage in their firms (Cronqvist, Makhija, and Yonker (2011)), although part of this effect can be attributed to endogenous firmmanager matching. (Behavioral Corporate Finance: A Survey, 2005)

If there is no optimal capital structure, so that f is equal to zero, the manager will not issue equity, setting e to zero, and there is no interaction among financing, internal funds, and investment. In this case, the optimistic manager will clearly overinvest: f_k is less than unity. (Advances in Behavioral Finance, 2005)

Mergers and acquisitions

In the case of Merger and Acquisitions the past theories have suggested that the successful acquirers may be optimistic and overconfident in their own valuation of deal synergies, and fail to properly account for the winner's curse. Roll interprets the evidence on merger announcement effects, surveyed by Jensen and Ruback (1983), as well as the lack of evidence of fundamental value creation through mergers, as consistent with this theory. Malmendier and Tate (2004) develop this argument and use their optionsbased proxy for CEO optimism to test it. They find patterns consistent with optimism and overconfidence. First, optimistic CEOs complete more mergers, especially diversifying mergers, typically suggested as being of dubious value.

Second, optimism has its biggest effect among the least equity dependent firms-when managers do not have to weigh the merger against an equity issue that they, as optimists, would perceive as undervalued. Third, investors are more skeptical about bid announcements when they are made by optimistic CEOs. Schneider and Spalt (2010) find similar results, including that offer prices are higher, but acquirer announcement returns are lower, when the target has (had) skewed returns. The announcement returns evidence is consistent with the theme of irrational managers operating in efficient markets. Managerial biases research has taken a Freudian turn with Aktas, de Bodt, Bollaert, and Roll's (2010) study of CEO narcissism. They measure narcissism, a trait related to but distinct from overconfidence, as the ratio of first person singular pronouns to total first person pronouns used in CEOs' transcribed speeches. Thuslydefined narcissist CEOs are more likely to be acquirers, and more likely to have initiated their transactions.

This is interpreted as consistent with the high stakes activity required to maintain the narcissistic ego. Targets run by narcissists, meanwhile, secure higher bid premia. Aktas et al. speculate that this arises because narcissistic CEOs demand extra compensation for the loss of ego associated with losing control. If managerial biases affect decisions because governance is limited, crosssectional variation in governance may be useful for identifying the effect. Yermack (1996) finds that firms with smaller boards of directors have higher firm value; Kolasinski and Li (2010) find that small boards dominated by independent directors reduce the impact of CEO overconfidence on acquisition frequency. They use

negative future returns on CEO purchases as ex post evidence of ex ante overconfidence.

Thus behavioral finance plays a vital role in cooperate decision making process. Psychology of an individual or the decision making body while taking corporate decisions will be influenced by so many factors that we have discussed above. The personal feelings, emotions, attitude plays a role in every decision taken by the corporate. Time and again many studies have already proved the influence of psychological behavior that would affect any decision taken by the person who is in the senior most position. The studies have also shown us the consequence of those outcome or what negative impact it has had on the company were decision was taken based on feelings and not on detailed analysis of the situation.

Impact of corporate decision making

Behavioral finance as both positive and negative Impact on the decision taken by the manager. Positive is when he trusts his instinct and takes the decision which will be proved completely right. It will be terrible wrong when the manager or the person who is in charge of taking corporate decision gives up his mind for feelings, emotions etc. The decision taken by him would prove very costly leading to denting the reputation of the company and the consequences may be long term. His also shows the inability of the manager to take fair decisions for the overall development of the organization.

Let's take the example of a CFO, CEO or a manager who has to take decision regarding the capital structure of the company. In that case several personality traits composing the global personality dimension of CEOs have a significant influence on certain capital structure related choices. Specifically:

- a) CEOs with high self-esteem favor decisions lowering the long-term liabilities-to-equity ratio and issuing new equity that do not lead to financial obligations like debt;
- b) CEOs that are highly extravert find exploiting possible advantages of each source of finance (i.e the debt tax shield) more important than avoiding possible corresponding negative consequences (i.e. debt financial distress). In contrast, CEOs who are intolerant to ambiguity consider avoiding possible negative consequences more important than exploiting possible advantages. Extraverted CEOs tend to issue new

equity whenever the debt-to-equity ratio is lower relative to the sector's ratio;

- c) CEOs who are open to new experiences avoid traditional, available, funding sources. They consider as more important the exploitation of possible advantages rather than avoiding possible negative consequences and they tend to issue new equity whenever the stock price is relatively high;
- d) The more conscientious a CEO is, the more he thinks that the stock market generally evaluates the firm at lower levels than its real value; and finally,
- e) CEOs high in sensation seeking tend to issue new equity, whenever the debt-to equity ratio is relatively high compared to the sector's ratio while the more emotionally stable a manager is, the less he prefers issuing debenture.

These results also lead us to conclude that personality traits are closely related to specific value maximization impediments, viewed by the behavioral finance perspective, such as aversion to ambiguity, illusion of knowledge, anchoring and the availability heuristic. The decision for a certain financing mixture of publicly listed firm is driven by CEOs consciousness, need for cognition and openness to experience. CEOs' self-esteem and need for cognition drive their decisions to issue new equity relatively often. (What Drives Capital Structure Decisions?)

Heuristic Decision Process (Behavioral Corporate Finance: A Survey, 2005)

The decision process by which the investors find things out for themselves, usually by trial and error, lead to the development of rules of thumb. In other words, it refers to rules of thumb which humans use to made decisions in complex, uncertain environments. The reality, the investor's decision making process are not strictly rational one. Thought the investors have collected the relevant information and objectively evaluated, in which the mental and emotional factors are involved. It is very difficult to separate. Sometimes it may be good, but many times it may result in poorer decision outcomes. It includes:

1. Representativeness: The investors' recent success; tend to continue into the future also. The tendency of decisions of the investors to make based on past experiences is known as stereotype. Debont concluded that analyses are biased in the direction of recent success or failure in their earnings forecasts, the characteristic of stereotype decisions.

2. Overconfidence: There are several dimensions to confidence. It can give more courage, and is often viewed as a key to success. Although confidence is often encouraged and celebrated, it is not the only factor to success. The investors who are cautious and analytical can achieve success and others have to withdraw. Yet, confidence, especially self-confidence, is often viewed as a positive trait. Sometimes, the investors overestimate their predictive skills or assuming more knowledge than they have. Many times it leads excessive trading.

3. Anchoring: It describes the common human tendency to rely too heavily, or ‘anchor’ on one trait or piece of information when making decisions. When presented with new information, the investors tend to be slow to change or the value scale is fixed or anchored by recent observations. They are expecting the trend of earning is to remain with historical trend, which may lead to possible under reactions to trend changes.

4. Gamblers fallacy: It arises when the investors in appropriately predict that trend will reverse. It may result in anticipation of good or poor end.

5. Availability bias: The investors place undue weight for making decisions on the most available information. This happens quite commonly. It leads less return and sometimes poor results also. (Behavioral Corporate Finance: A Survey, 2005)

6. Prospect theory

This theory is developed by Kahneman and Tversky⁹. The second groups of illusions which may impact the decision process are grouped in prospect theory. He discussed several states of mind which may influence an investor’s decision making process. The key concepts which he discussed are as follows:

1. Loss aversion: Loss aversion is an important psychological concept which receives increasing attention in economic analysis. The investor is a risk-seeker when faced with the prospect of losses, but is risk-averse when faced with the prospects of enjoying gains. This phenomenon is called loss a version¹⁰. Ulrich Schmidta, and Horst Zankb¹¹ discussed the loss aversion theory with risk aversion and he accepted the Kahneman and Tversky views.

2. Regret Aversion: It arises from the investors’ desire to avoid pain of regret arising from a poor investment

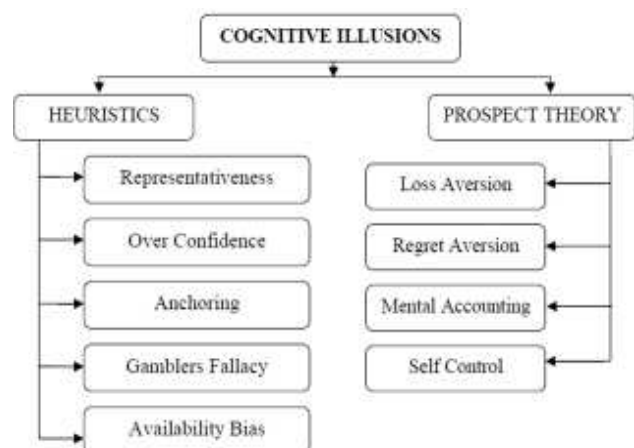
decision. This aversion encourages investors to hold poorly performing shares as avoiding their sale also avoids the recognition of the associated loss and bad investment decision. Regret aversion creates a tax inefficient investment strategy because investors can reduce their taxable income by realizing capital losses.

3. Mental Accounting: Mental accounting is the set of cognitive operations used by the investors to organise, evaluate and keep track of investment activities. Three components of mental accounting receive the most attention. This first captures how outcomes are perceived and experienced, and how decisions are made and subsequently evaluated. A second component of mental accounting involves the assignment of activities to specific accounts. Both the sources and uses of funds are labelled in real as well as in mental accounting systems.

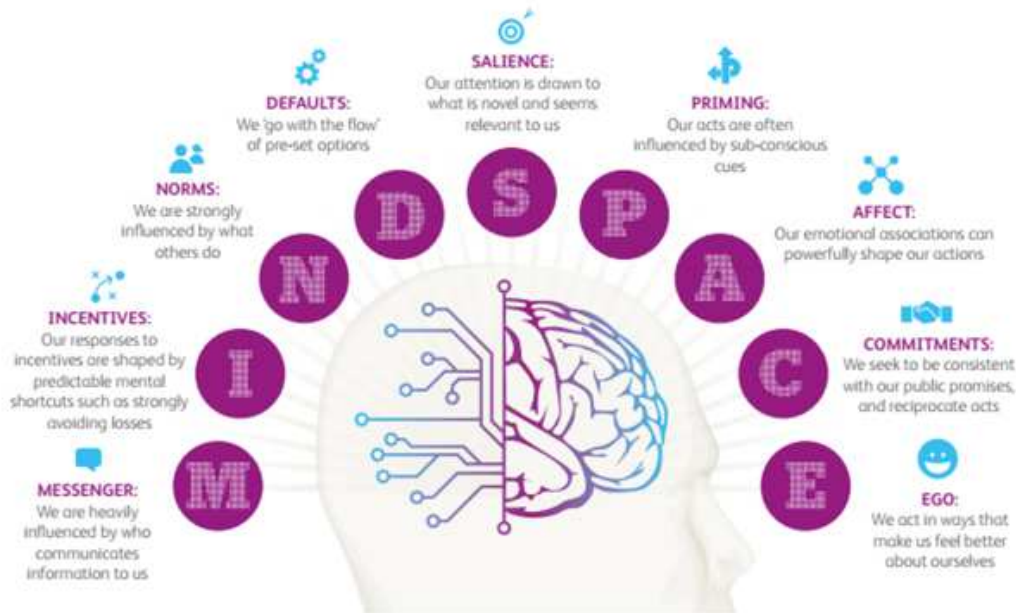
The third component of mental accounting concerns the frequency with which accounts are evaluated and ‘choice bracketing’. Accounts can be balanced daily, weekly, yearly, and so on, and can be defined narrowly or broadly. Each of the components of mental accounting violates the economic principle of fungibility. As a result, mental accounting influences choice, that is, it matters.

4. Self-Control: It requires for all the investors to avoid the losses and protect the investments. As noted by Thaler and shefrin¹³ investors are subject to temptation and they look for tools to improve self-control. By mentally separating their financial resources into capital and ‘available for expenditure’ pools, investors can control their urge to over consume. (Behavioral Finance and Its Impact on Investing, 2017)

Classification of cognitive illusion



The MINDSPACE framework for behaviour change assembles the nine most robust effects that influence our behaviour



Overall, these findings expand and confirm past research regarding the impact of managerial traits on capital structure decisions. Analytical work is in progress for constructing and examining the impact of a global personality index on certain capital structure decisions as well as the identification of segments among CEOs who possess similar personality traits.

Knowledge of the impact of a global personality profile on CEOs' capital structure decisions may be useful to financial policy makers to better evaluate efforts by CEO subgroups who may strive to influence governance policies and investment strategies and hence, address the importance of several agency-related problems. By acquiring such crucial information, conflicting situations that undermine publicly listed firms' success in the financial markets may be prevented and continuous enhancement of shareholders' value may be achieved.

Some of the impacts of behavioral biases of an investor can lead to the following:

- Investors fail to design their portfolio of investment avenues systematically.
- Investors fail to diversify their portfolio.
- Investors generally overestimate their skills, attributing success to ability they don't possess and seeing order in information or data where it doesn't exist i.e., Investors are overconfident while making investment decisions

- Investors blindly follow the crowd (herd mentality) while making investment decisions which leads to wrong investment decisions
- Investors anchor on historical information.
- Investors think that good times are permanent. They feel that ones they earn a good profit from their investment avenue, the investment would give them good returns permanently
- Investors are greedy and they want to earn money quickly (Instant gratification) which also leads to wrong investment decisions.
- Investor's generally making short term investment decisions rather than long term investment decision. (<http://www.iracst.org>, 2105)

Implications for financial markets

The impact of behavioral finance is not only found in corporate financial decision making process but also when it comes to individual and corporate investments. Proponents of behavioral finance contend that heuristic-driven bias and framing effects cause market prices to deviate from fundamental values. It is argued that because these biases are an inherent part of all of our decision-making processes, they can systematically distort market behavior. For example, the representativeness heuristic could lead investors to become over optimistic about past winners and over pessimistic about past losers, causing share prices to deviate from their fundamental level.

Anchoring and over-confidence could lessen analysts' tendency to adjust earnings predictions when new information arises. In particular, the biases may result in -

- * Over or under reaction to price changes or news
- * Extrapolation of past trends into the future
- * Lack of attention to the fundamentals underlying a stock
- * Undue focus on popular stocks

If such patterns exist, there may be scope for investors to exploit the resulting pricing anomalies to capture superior, risk-adjusted returns. (www.coursehero.com, 2012)

Proponents of EMH, in fact, argue that smart money will exploit such anomalies and drive prices to their fundamental values. Other research, however, shows that rational investor trading is unable to completely offset the actions of irrational investors. This, as pointed out by Edward M Miller in 1977, is largely due to the inability of smart money to engage in short sales when the bulk of shares are held by irrational investors. Using data on the interest cost of borrowing and lending shares in the 1920s and 1930s, Jones and Lamont (2001) show that shares that were more expensive to short tended to be highly priced and had lower subsequent returns on average as predicted by Miller's theory.

Supporters of the traditional EMH theory (Fama, 1998), have firmly sought to refute behavioral finance. They note that if sufficient analysis is done on any data set of share prices, odd findings (such as a finding that share prices often rise or fall when a particular event occurs) will appear simply due to chance. They also argue that observed anomalies in market prices may not result from behavioral biases, but rather because of a misspecification of systematic risk. (www.coursehero.com, 2012)

For example, if a share is marketed by both rational and irrational share holders, it may have an added risk premium which will drive the share price in the 'wrong' direction as a result of a sudden, unwarranted change in their expectations for the share.

The study of behavioral finance is a valuable tool for financial advisors to better understand and implement recommendations for their clients. Understanding the behavioral pattern and psychology of a client can make the financial advisor more effective and strengthen the client-advisor relationship (Baker & Ricciardi, 2015; Pompian, 2012). Baker and Ricciardi (2015) found that understanding client factors such as personality traits, demographics, socioeconomic influences, and religion, and risk-taking history, cognitive and emotional biases could all affect a client's reasoning for financial and investing decisions.

Constructing the portfolio

One of the main jobs of a financial advisor is to help construct his client's portfolio. One common portfolio mistake most clients make is that they have too much of their retirement savings tied up in the stock of the company they work for without any superior information for why they should be so heavily invested in their company, resulting in a lack of diversification (Benartzi, 2001). Investors also rarely update their portfolios as conditions in the market change. There is a clear need for help in portfolio construction, and one way that an advisor can do that is through helping the client create goals within their portfolio. (Behavioral Finance and Its Impact on Investing, 2017)

The behavioral corporate finance literature has mellowed to the point where one can now draft out a handful of acknowledged theoretical frameworks and apply them to organize the gathered evidence of dozens of empirical studies. This survey suggests that the behavioral approaches to corporate finance offer a useful complement to the other archetypes in the field. They deliver intuitive and sometimes quite compelling explanations for important financing and investing patterns, including some that are difficult to merge with prevailing theory. (Behavioral Corporate Finance: A Survey, 2005)

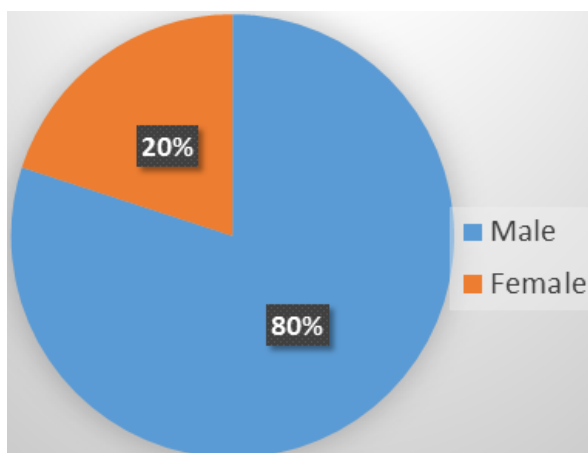
The decision making role has become crucial in the spontaneous changing corporate world. Especially, financial decisions are vital for the sustained survival in the long run. The financial decision makers' designation may vary from CFO to Chairman but the ultimate expectation from them is to perform for the growth of the organisation. There are three major areas of financial decision making namely Investment decisions, financing decisions and dividend decisions. There are two different types of decision makers in the corporate based on their approach towards the situation; rational decision makers and irrational decision makers. Irrespective of the types, their objective is to optimize or to determine an ultimate solution for an existing problem or an easy path to develop the organisation where they are employed. Even though there are plentiful formulae, methodologies and numerical analysis before taking a final financial decision, there is a prologue for all those i.e. human psychology or behavioral traits. Each and every individual at the decision making level in the corporate ought to be undergoing this stage irrespective of their age, gender, income, authority and ethnicity. Inevitably

there are both positive side and negative sides at this stage. If the psychological thoughts and behavioral traits are logical, it leads to optimistic approach while taking a decision. On the other hand, if the same are illogical, it paves way for overconfidence and culminates in erroneous decision making and hamper the expansion and growth in the long run.

Section V: Analysis and interpretation

Table 5.1 : Showing the gender of the respondents

Gender	Number of respondents	Percentage
Male	82	80%
Female	20	20
TOTAL	102	100%



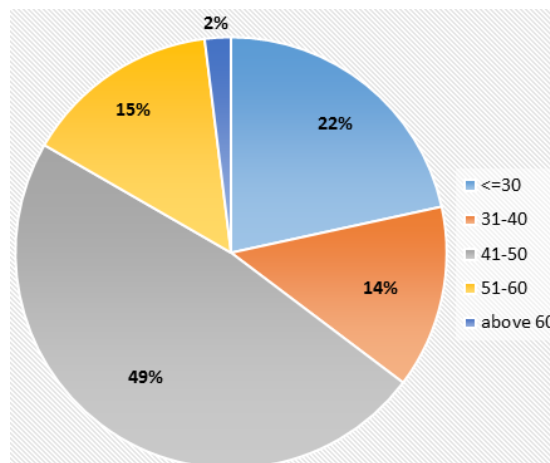
Graph 5.1 showing the gender of respondents

Interpretation

According to the survey conducted 80% of the respondents are males and the other 20% are females.

Table 5. 2 : Showing the age of the respondents

Age	Number of respondents	Percentage
<=30	22	22%
31-40	14	14%
41-50	49	48%
51-60	15	14%
Above 60	2	20%
TOTAL	102	100



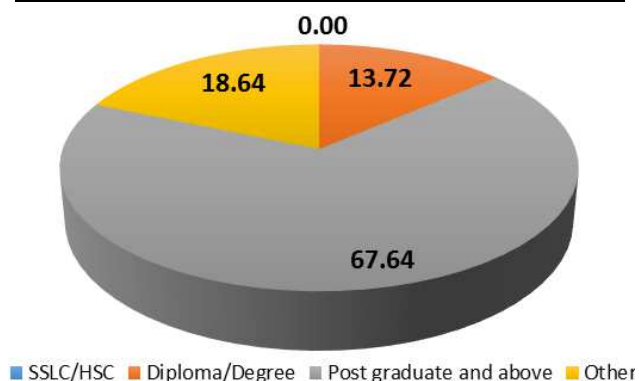
Graph 5. 2 : Showing age of respondents

Interpretation

According to the survey conducted, out of the 102 respondents 22% of the respondents were below 30 years of age, 14% were in the age group of 31-40, 48% are in the age group of 41-50, 14% are in the range of 51-60 and the others are above 60

Table 5.3 : Showing highest educational qualifications of respondents

Educational qualification	Number of respondents	Percentage
SSLC/HSC	0	0%
Diploma/Degree	14	13.72%
Post graduate & above	69	67.64%
Other	12	18.64%
TOTAL	49	100



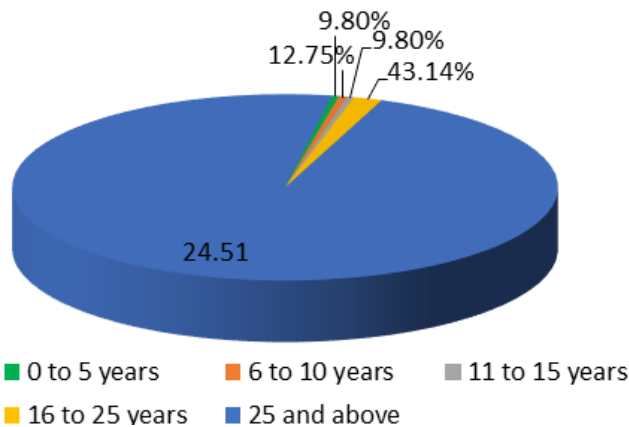
Graph 5.3 showing the educational qualification of respondents

Interpretation

From the survey conducted it can be found that 13.72% of the respondents have completed their degree/diploma whereas 67.6% of the respondents hold a postgraduate degree and 18.64% have other professional qualifications like CA, CMA etc

Table 5.4 : Showing the overall work experience of the respondents

Overall work experience	Number of respondents	Percentage
0-5	10	9.80%
6-10	13	12.75%
11-15	10	9.80%
16-25	44	43.14%
25 and above	25	24.51%
TOTAL	102	100%



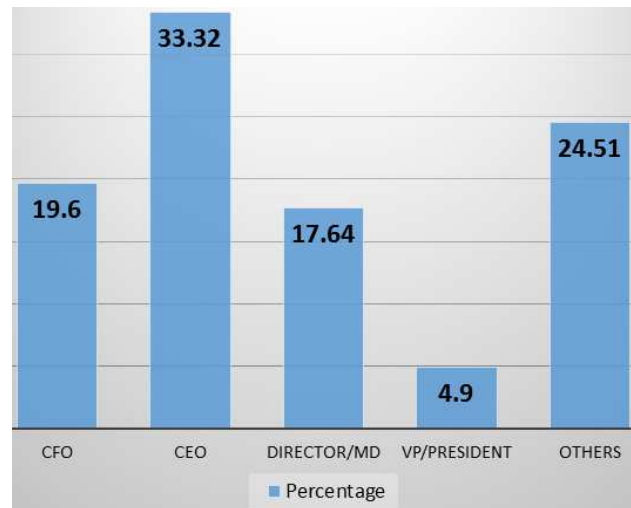
Graph 5.4 : Showing the overall work experience of the respondents

Interpretation

From the survey conducted we can observe that 9.80% of the respondents have an overall work experience of 0-5 years, 12.75 % have for a tenure of 6-10 years and another 9.80% have for a period of 11-15 years and 43.14% do so for 16-25 years which are in majority and 24.51% of respondents have work experience of more than 25 years.

Table 5.5 : Showing current designation of respondents

Designation	Number of respondents	Percentage
CEO	20	19.60%
CFO	34	33.33%
Director/Managing director	18	17.64%
Vice President/President	5	4.90%
Others	25	24.51%
TOTAL	102	100



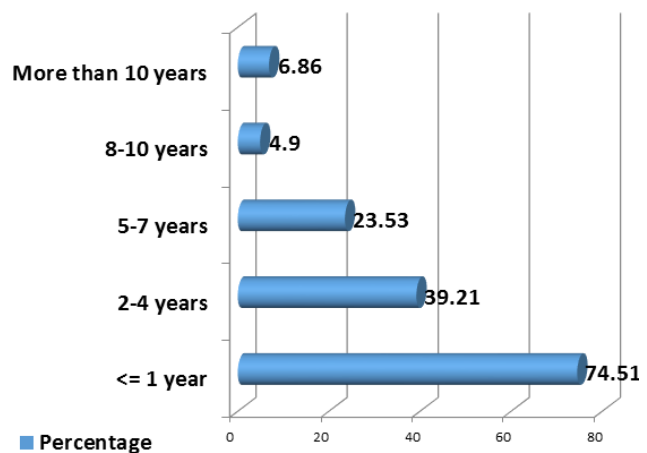
Graph 5.5 showing current designation of respondents

Interpretation

From the survey conducted it can be observed that 33% of the respondents were CFOs comprising of the majority and another 19.6% were CEOs whereas Directors and Managing directors were a meagre 4.9% and 24.51% can be categorised as falling into others category.

Table 5.6 : Showing tenure of respondents with current organisation

Tenure with current organisation	Number of respondents	Percentage
<=1 year	76	74.51%
2-4 years	40	39.21%
5-7 years	24	23.52%
8-10 years	5	4.90%
More than 10 years	7	6.86%
TOTAL	27	100%



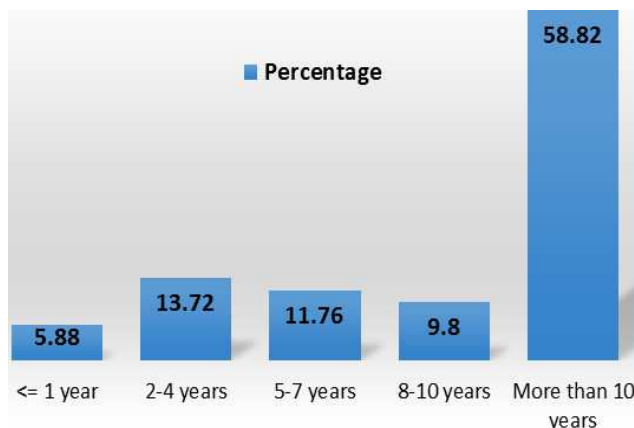
Graph 5.6 showing tenure of respondents with current organisation

Interpretation

From the survey conducted it can be noticed that a lot of respondents comprising of 74.51% of the respondents have stayed for less than a year whereas 39.21% of the respondents had their career with the current firm for more than 2-4 years, 23.52% of the respondents have their career for 5-7 years with the current organisation and 4.90% of the respondents do so when it comes to 8-10 years whereas a total of 6.86% of the respondents have stayed for more than 10 years with the current company

Table 5.7 : Showing corporate experience in the capacity of major decision making

Experience in decision making	Number of respondents	Percentage
<=1 year	6	5.88%
2-4 years	14	13.72%
5-7 years	12	11.76%
8-10 years	10	9.80%
More than 10 years	60	58.82%
TOTAL	27	100



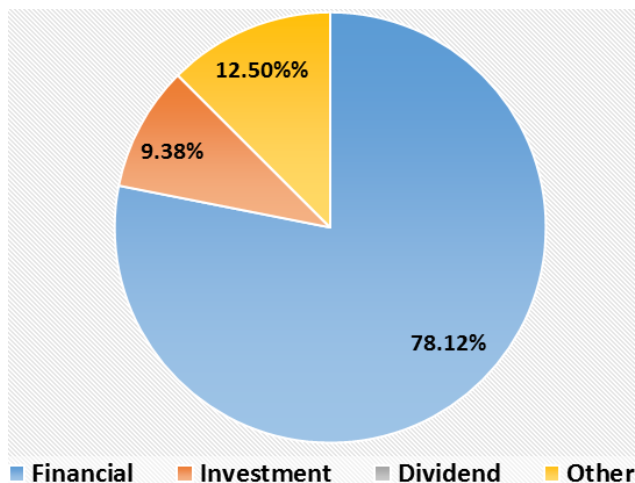
Graph 5.7 : Showing corporate experience in capacity of decision making

Interpretation

From the survey conducted it can be noticed that a lot of respondents comprising of 58.82% of the respondents have a corporate experience of more than 10 years and 13.72% of the respondents had their corporate experience for a period of 2-4 years, 11.76% of the respondents have an experience of around for 5-7 years and mere 5.88% of the respondents have experience in corporate decision making for less than a year

Table 5.8 : Showing the nature of decision the respondent has been involved in

Nature of decision	Number of respondents	Percentage
Financial	75	78.12%
Investment	9	9.38%
Dividend	0	0%
Other	12	12.5%
TOTAL	27	100%



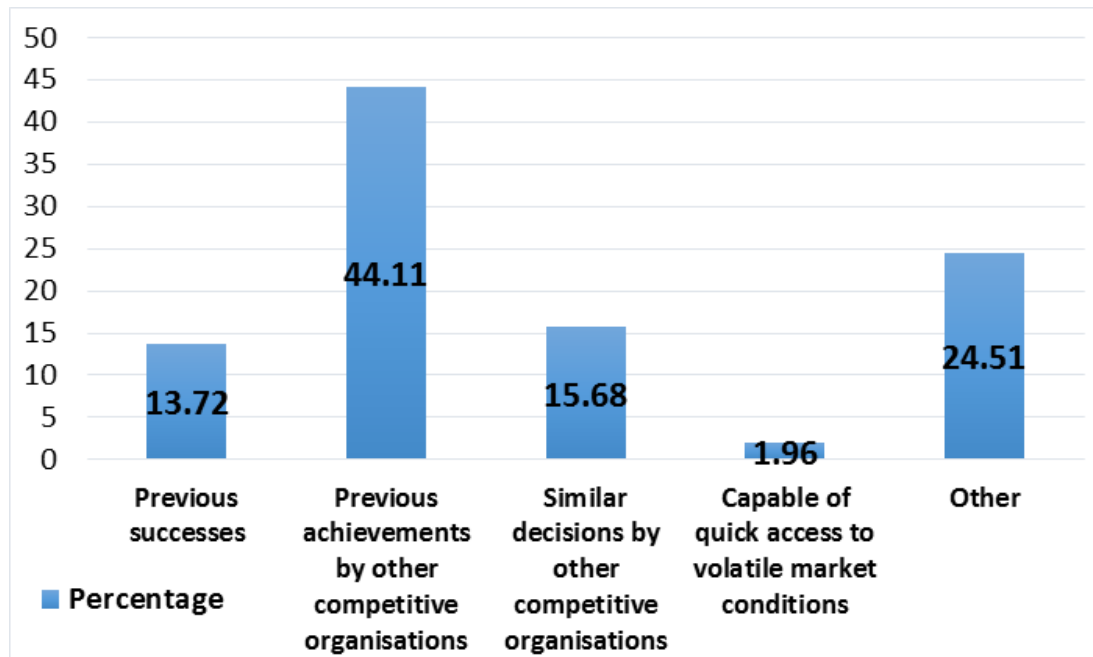
Graph 5.8 : Showing nature of decision the respondent has been involved in

Interpretation

From the survey conducted we can observe that 78.12% of the respondents have been involved in financial decision making whereas 9.38% are involved in investment decision making and 12.5% are classified as other category

Table 5.9 : Showing major reason for taking the particular decision quickly

Reason for taking decision quickly	Number of respondents	Percentage
Previous successes	14	13.72%
Previous achievements by other competitive organisations	45	44.11%
Similar decisions by other competitive organisations	16	15.68%
Capable of quick access to volatile market conditions	2	1.96%
Other	25	24.51%
TOTAL	102	100



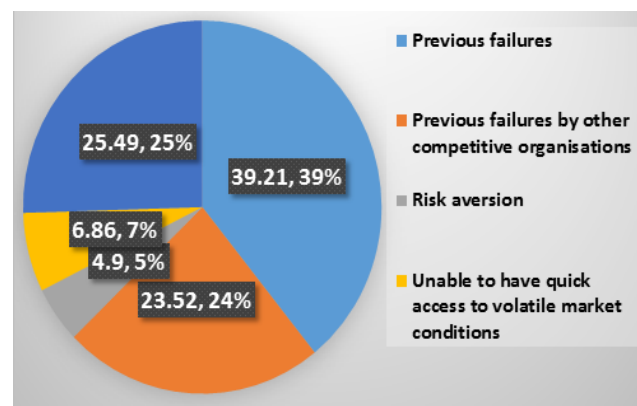
Graph 5.9 showing major reason for taking the particular decision quickly

Interpretation

From the survey conducted, it can be well inferred that 13.72% of the respondents took the decision quickly owing to previous successes, whereas 44.11% of the respondents did so because of previous achievements by other competitive organisations, meantime another 15.68% did so because of similar decisions by other competitive organisations and only 24.51% did so because of other factors

Table 5.10 : Showing major reasons for delay in decisions

Reason for delay in decisions	Number of respondents	Percentage
Previous failures	40	39.21%
Previous failures by other competitive organisations	24	23.52%
Risk aversion	5	4.90%
Unable to have quick access to volatile market conditions	7	6.86%
Other	26	25.49%
TOTAL	102	100%



Graph 5.10 showing major reasons for delay in decisions

Interpretation

From the study we can infer that 39.21% of the respondents cite previous failures for delay in decision whereas 23.52% believe it is due to previous failures by other competitive organisations and 4.9% cite risk aversion whereas 6.86% cite it was unable to have quick access to volatile market conditions.

Table 5.11 : Showing situations when respondents feel their decision is successful

When decision was successful	Number of respondents	Percentage
Reaching organisational objective	72	70.59%
Reaching the self-set objective	6	5.89%
Reaching the identical achievements of the market competitors	5	4.90%
Reaching the sustainable average of market achievements	13	12.74%
Other	6	5.89%
TOTAL	102	100



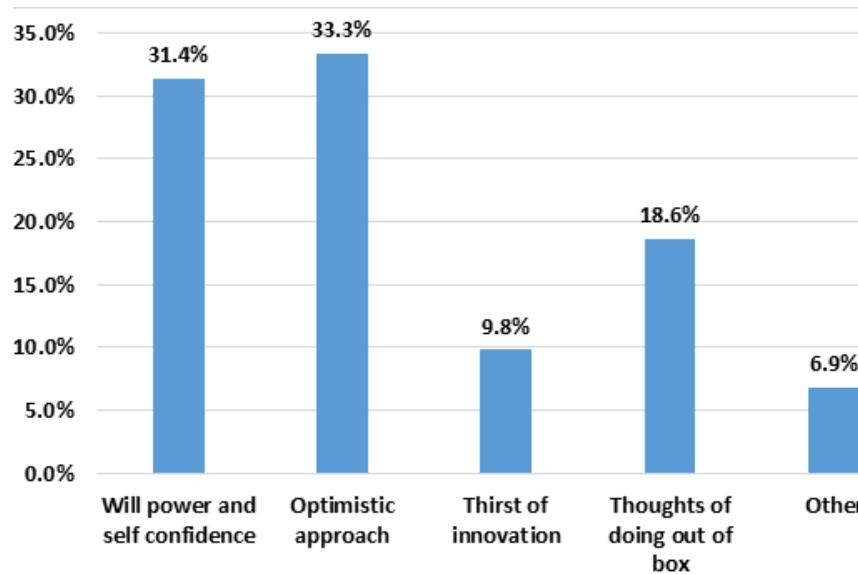
Graph 5.11 : Showing situations when respondents feel their decision is successful

Interpretation

From the study we can infer that 70.59% of the respondents feel their decisions were successful when they could reach organisational objectives whereas 5.89% of the respondents felt they were successful with their decisions when they could reach the self-set objective whereas 4.9% of the respondents felt so when reaching the identical achievements of the market competitors and 12.74% felt so when reaching the sustainable average of the market achievements and only 5.89% felt so by citing other reasons.

Table 5.12 : Showing the view on the psychological reason/s for the success of a decision, Please Rank if more than one.

Psychological reason	Number of respondents	Percentage
Will power and self confidence	32	31.4%
Optimistic approach	34	33.3%
Thirst of innovation	10	9.8%
Thoughts of doing out of box	19	18.6%
Other	7	6.9%



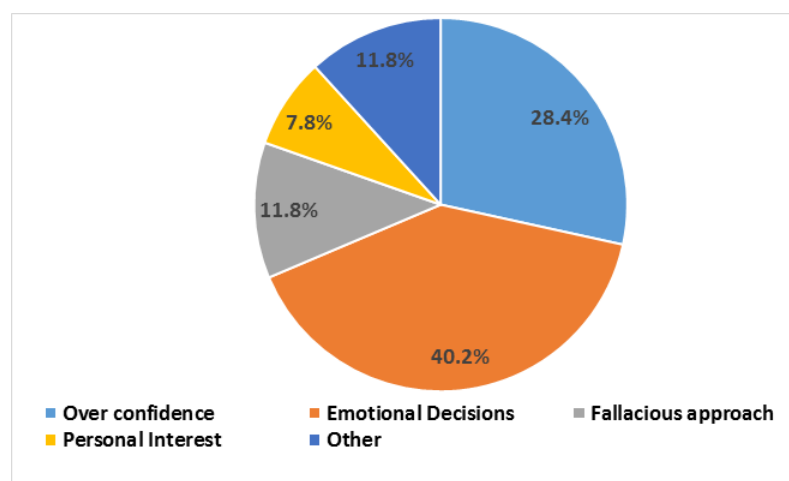
Graph 5.12 showing the views on the psychological reason/s for the success of a decision

Interpretation

When asked about the physiological reasons for a successful decision taken, we see a mixed response where close to 1/3rd feel the optimistic approach of the decision maker is the reason for the success and other 1/3rd feel the strong will power and confidence will lead to successful decision. Only a combined 28% of the respondents feel that the forward thinking and innovative approach of decision maker will lead to better decision.

Table 5.13 : Showing the view on the psychological reason/s for the failure of a decision, Please Rank if more than one.

Psychological reason	Number of respondents	Percentage
Over confidence	29	28.43%
Emotional Decisions	41	40.20%
Fallacious approach	12	11.76%
Personal Interest	8	7.84%
Other	12	11.76%



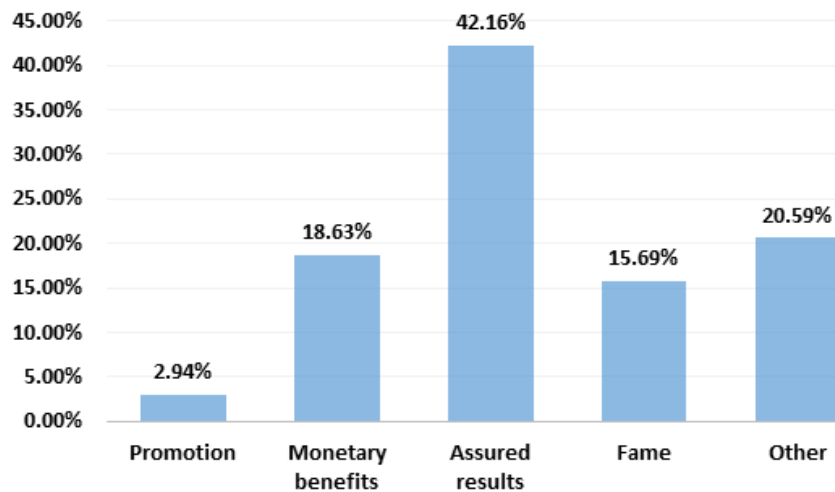
Graph 5.13 showing the psychological reason/s for the failure of a decision

Interpretation

When it comes to the reasons for the failure of a decision taken and psychological aspect affecting that close to 40% respondents say that emotional concerns while deciding something would surely lead to failure, surprisingly only 29% feel overconfidence is a reason. Personal interest of the decision maker and Fallacious approach gets a combined % of close to 20.

**Table 5.14 : Showing the factor which motives to take a decision?
Please Rank if more than one**

Factor which motives to take a decision	Number of respondents	Percentage
Promotion	3	2.94%
Monetary benefits	19	18.63%
Assured results	43	42.16%
Fame	16	15.69%
Other	21	20.59%



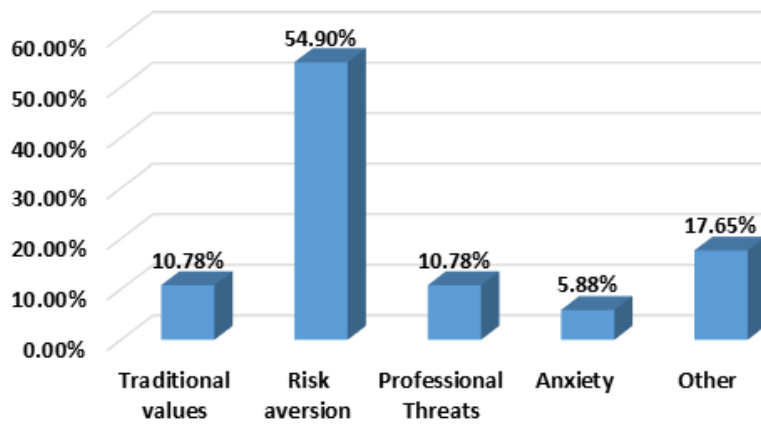
Graph 5.14 : Showing the factor which motives to take a decision

Interpretation

More than 43% people feel that the decision maker being confident of assured results will take a specific decision above all other factors. This also show how corporate world always drive for results and whatever they do they would be worried about the end product. Many other factors have been preferred by close to 20% respondents. Interestingly monetary benefits are not among the preferred choices with only 18% people responding to that. Fame and promotion are 16% and 3% respectively.

Table 5.15 : Showing the factor which influence to have a second thought on taking a particular decision? Please Rank if more than one

Factor which influence to have a second thought	Number of respondents	Percentage
Traditional values	11	10.78%
Risk aversion	56	54.90%
Professional Threats	11	10.78%
Anxiety	6	5.88%
Other	18	17.65%



Graph 5.15 : Showing the factor which influence to have a second thought on taking a particular decision

Interpretation

Risk aversion and concern for it is something that will bring confusion in the minds of the customer and ensure that they are not firm in their approach. Over 54% people have a second thought on the decisions because of the risk factor. It also shows that a decision maker doesn't consider the professional threats while taking an important decision which shows that the decision maker put company first and then his job. 11% give importance to traditional values and are ready to alter their decisions. Only 6% have second thought because of anxiety which is a good sign.

Table 5.16 : Showing the priority on taking a decision.

Priority	Number of respondents	Percentage
Employer satisfaction	27	26.47%
Moral values	41	40.20%
Other stake holders satisfaction	18	17.65%
Socio-economic values of the society	6	5.88%
Other	10	9.80%



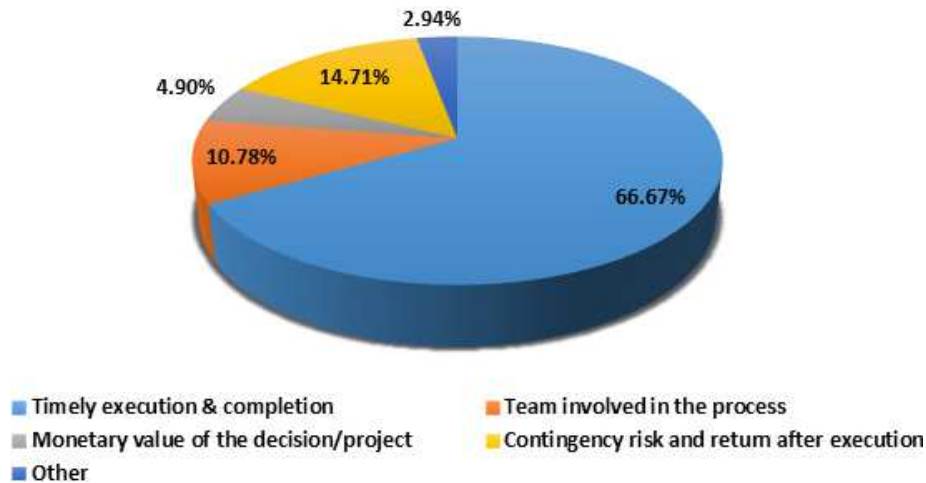
Graph 5.16 : Showing priority on taking a decision

Interpretation

When a corporate decision maker takes an important decision, contrary to the previous question he initially considers moral values and his thought process will be in that direction. Whatever idea or instance comes to his mind he will never compromise on the ethics he has learnt and has been thought. 40% of the respondents say so. A combined total of 45% of the respondents will think about the stakeholders of the company while taking such decisions and that is their main priority.

Table 5.17 : Showing the Major concern when decision is being executed

Major concern when decision is being executed	Number of respondents	Percentage
Timely execution & completion	68	66.67%
Team involved in the process	11	10.78%
Monetary value of the decision/project	5	4.90%
Contingency risk and return after execution	15	14.71%
Other	3	2.94%



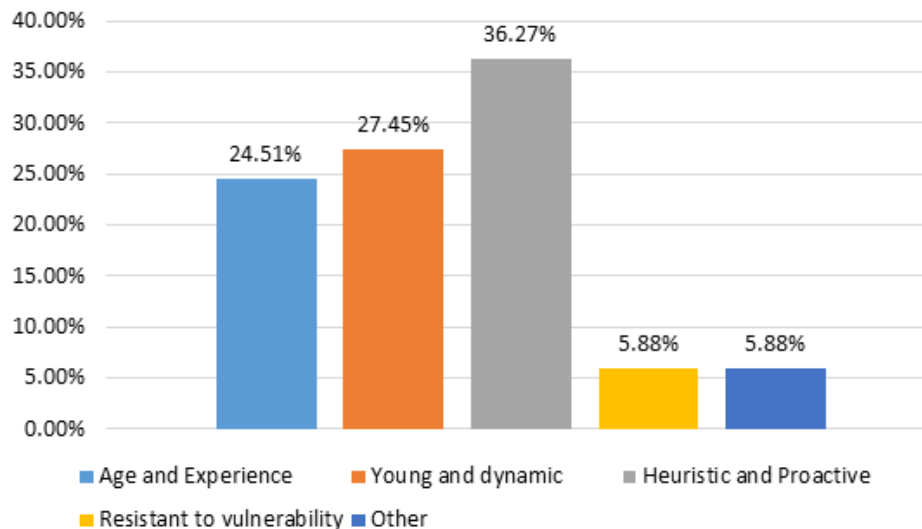
Graph 5.17 showing the major concern when decision is being executed

Interpretation

As in the expected lines 2/3rd of respondents are concerned about the timely execution and completion of the product after a key decision is taken with respect to it. 15% are also worried about the risk and return that the company gets after it is executed.

Table 5.18 : Showing the important aspect considered in subordinates while taking a decision based on their assistance.

Important aspect considered in subordinates	Number of respondents	Percentage
Age and Experience	25	24.51%
Young and dynamic	28	27.45%
Heuristic and Proactive	37	36.27%
Resistant to vulnerability	6	5.88%
Other	6	5.88%



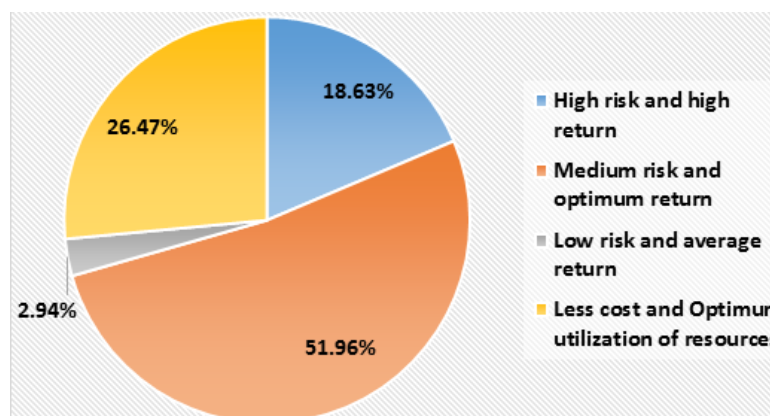
Graph 5.18 : Showing the important aspect considered in subordinates while taking a decision based on their assistance

Interpretation

It is to be noted that a decision maker doesn't just consider the experience or the dynamic thoughts of his subordinates but his proactive and preparedness for undertaking a task. In this research close to 37% decision makers will look for the proactive characteristics in his or her subordinates. Interestingly more than age and experience (24.51%), the youthfulness and dynamisms (27.45%) matters to the decision maker since he believe in creative thinking which the present generation is known for.

Table 5.19 : Showing the Major focus in the decision while executing it.

Major focus in your decision	Number of respondents	Percentage
High risk and high return	19	18.63%
Medium risk and optimum return	53	51.96%
Low risk and average return	3	2.94%
Less cost and Optimum utilization of resources	27	26.47%



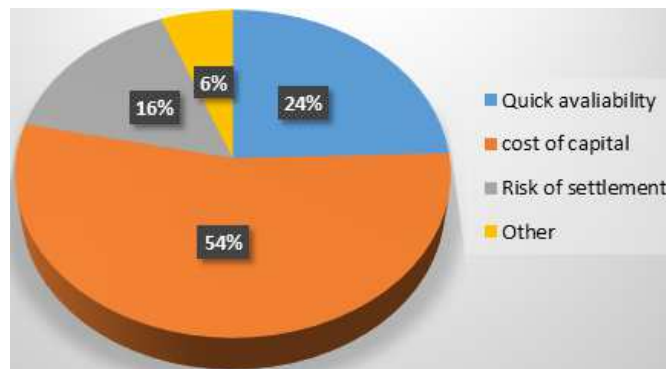
Graph 5.19 : Showing the major focus in decisions while executing it

Interpretation

More than 50% of the people are perfectly alright of taking a medium risk and compromising on higher returns for the company. They are very conservative but strive for optimum return. Only 19% of the respondents want to take high risks for getting higher return.

Table 5.20 : Showing the Top priority/major concern while taking financing decision

Top priority/major concern while taking financing decision	Number of respondents	Percentage
Quick availability	25	24.51%
cost of capital	55	53.92%
Risk of settlement	16	15.69%
Other	6	5.88%



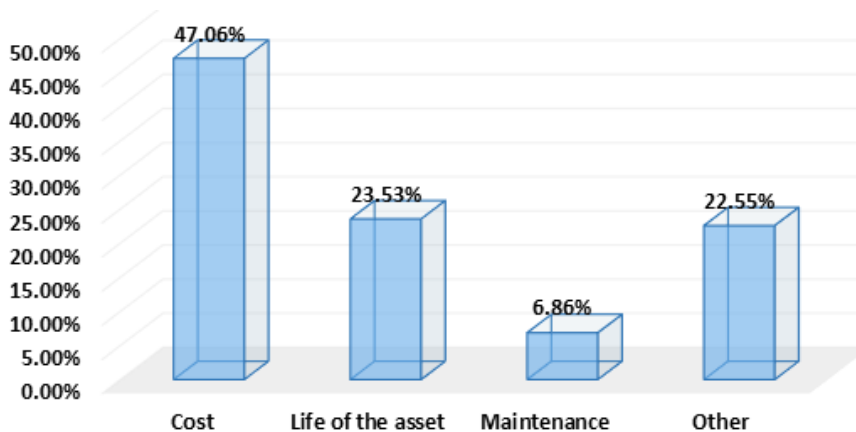
Graph 5.20 showing the top priority /major concern while taking financing decision

Interpretation

While taking a financing related decision for the corporate decision maker the cost of funds raised or borrowed, availability of it, risk deriving from that etc. becomes the cause of concern. As per our research 54% of the respondent feel that the cost of capital would be the major barrier for financing related decisions followed by availability of it which is at 24%. Risk only comes in at 3rd with 16%.

Table 5.21 : Showing the Top priority/major concern while taking investment decision

Top priority/major concern while taking investment decision	Number of respondents	Percentage
Cost	48	47.06%
Life of the asset	24	23.53%
Maintenance	7	6.86%
Other	23	22.55%



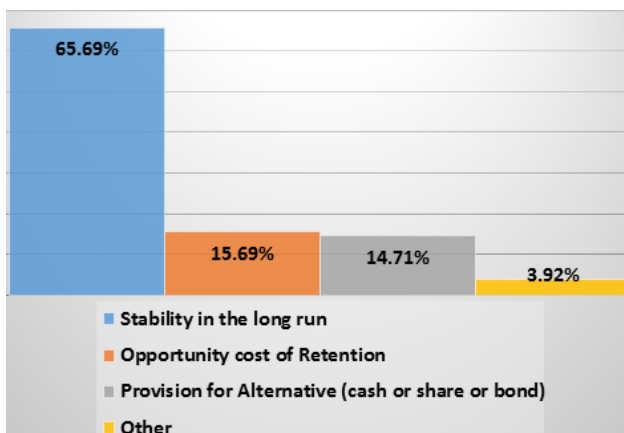
Graph 5.21 : Showing the top priority /major concern while taking investment decision

Interpretation

Same as like in finance decision making process, even in the context of investment decision the cost of the capital is the primary and major concern for a corporate entity and would affect the decision making of any sort. Close to 48% of the respondents feel so. Life of the asset is also important since we are investing on the asset and the utility for a longer duration would be kept in the decision makers mind. (24%)

Table 5.22 : Showing the Top priority/major concern while taking dividend decision

Top priority/major concern while taking dividend decision	Number of respondents	Percentage
Stability in the long run	67	65.69%
Opportunity cost of Retention	16	15.69%
Provision for Alternative (cash or share or bond)	15	14.71%
Other	4	3.92%



Graph 5.22 : Showing the top priority /major concern while taking dividend decision

Interpretation

Dividend is paid to the shareholder and for that stability of the company for a long period is very essential. Around 65% of the respondents second that thought too. It's interesting that only 15% of the respondent feel that the dividend decision would influence the shareholder to retain himself and continue with the firm for a longer tenure. It's clear that dividend decision would be influenced by the stability the company is expecting in the long run.

Section VI : Findings, suggestions and Recommendations

Findings

- The major findings in the study is that the majority financial decision makers are in the age group of 41-50.
- The highest qualification of the majority decision makers is post-graduation and above. There is no astonishment in that as the industry is IT industry the qualification does matters in the entry level itself.
- Majority of the decision makers are with 20-25 years of overall work experience.
- Out of the total sample one third of the sample are in the designation of CFOs and one fifth of the samples are CEOs. It clearly indicates that these two roles dominate in making crucial decisions.
- It is observed that the tenure in the current organisation is coming down with the sample frequency. 76% of the decision makers are in the same organisation just for 1 to 2 years
- Hardly 8% are there with more than 10 years. It can also be interpreted that the spontaneously changing industry is also a reason for faster employee turnover.
- Around 60% of the decision makers are in the capacity either in the same organisation or in different organisation for more than 10 years.
- Around 75% of the decision makers are mainly involved in financial decision than any other decision. When it is asked about the reason, the respondents' response was quite acceptable that the financial decision involves sourcing fund, for that the bosses need their support but investment decisions involves fund outflows so they are very cautious about it. The bosses risk averse in nature when it comes to huge investment so, generally they take such decisions by themselves of-course they consult with the CFOs and other strategic level personalities.
- When it comes to taking quicker decisions almost half of the respondents are looking at other organizations' earlier successes. It shows the herding fallacy and also anchoring effect while taking the decisions.

- When it comes to taking decisions too late, they are much bothered about their own failures earlier and then they are looking at others similar experiences.
- The financial decision makers feel that the goal is reached when the result meets the organizational objectives
- The financial decision makers are giving the reason of will power, self-confidence and optimistic approach for their success in their decisions.
- Two third respondents are specific about their emotional influence and over confidence are there major reason for their failures.
- When it comes to motivation for particular decision, two third are coming out with the reason of assured result and one third are frank about monetary benefit with that decision.
- Majority of the respondents are risk averse in nature. They are not able to accept the blaming and the defamations.
- The top priority on taking a decision is moral value at first and employer satisfaction at second.
- While executing a financial decision they are much more concerned about the timely execution and accomplishment than any other aspect.
- While involving the subordinates while executing a decision, they are more concerned about the proactive nature but follow heuristic approach.
- Surprisingly they are more focused on medium risk than high or low risk ventures.
- While taking a financial decision they are more concerned about the cost of capital.
- When it comes to investment decisions cost is the top priority as they are accountable to the bosses for such a huge investment (when the decision is vested with the salaried top level personalities), they are more worried about the fear of losing trustworthiness regarding their potentiality.
- When it comes to dividend decisions their major concern is sustainability in the long run as it is a question of their stability and fame.

Suggestions

- The suggestions are not permanent when it comes to IT industry especially. As the industry itself is vulnerable in nature. Still there are few suggestions to caution the decision makers to be aware off.
- The decision makers in the IT industry need to be proactive while analyzing the previous success and failures before taking a financial decisions based on that.
- There is a mammoth requirement of modifying the thought process while taking a decision that there is a possibility of misperception of over optimism may culminate into erratic outcomes.
- Controlling the emotions and avoiding rushing to conclude a scenario based on mere observation will definitely yield to avoid blunder outcomes.
- Mismatch of personal goals with organsational goal may result in over-cautious decisions which result in underutilization of resources and may end up in substandard results when compared to market average returns. The decision makers are hereby better suggested to find out the route cause for the mismatch and exert the ideas proactively

Conclusion

Modern behavioral corporate finance decision-making suggests that corporate financial decision makers do not always act realistically while making a decision. They deal with several perceptive and psychological errs as the IT industry being highly vulnerable in nature. These errors are called behavioral biases and are there in many conducts. The behavioral biases that occur in financial decision making prospect theory, overconfidence, unwanted risk aversion and herding behavior. These behavioral occurrences have been explained and studied by several research studies. And for all these portents there is prove that they influence financial decision making. The behavioral corporate finance state that people make decisions based on the potential value of losses and gains rather than the final result and thus will base decisions on apparent gains rather than apparent losses of-course earlier losses dominates. Overconfidence generates mispricing of factor pay offs and all securities whose cash flows are derived from the overestimate indicator precision. This confirms complications in the financial decision making processes.

Though the above examples of illusions are widely perceived, behavioural corporate finance

does not claim that all the corporate decision makers will suffer from the same illusion simultaneously. The predisposition of a decision maker to a particular illusion is likely to be a function of several variables. For example, there is suggestive evidence that the experience of the decision maker has an explanatory role in his regard with less experienced investors being prone to extrapolation while more experienced decision makers commit over confidence similarly, behavioural factors play a vital role in the decision making process. Hence the top level financial decision makers have to take necessary precautions to minimize or avoid delusions for manipulating their financial and investment decision making process.

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