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AN ENSEMBLE OF INVESTMENT ADVENTURES: THE MYRIAD HUES OF PERSONAL FINANCIAL DECISIONS

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ABSTRACT

The study investigates how financial literacy influences the investment strategies of executives in two leading SME sector companies in Sri Lanka. Adopting a qualitative research approach, the study explores the role of financial attitudes, social norms, and perceived behavioral controls in investment decision-making based on the Theory of Planned Behavior and the Modern Portfolio Theory. Data were collected through in-depth interviews and analyzed thematically. The results suggested that an individual's investment decisions are influenced by interpersonal factors and that risk tolerance plays a crucial mediating role between financial literacy and investment choices. The findings can be useful for policymakers and financial institutions to enhance investment decentralization in Sri Lanka. However, the study acknowledges its limitations in terms of context-specific findings and potential biases from self-reported data. Future researchers are encouraged to conduct quantitative studies to validate and explore the relationships further.

Introduction

Behavioral finance has emerged as a field of research that investigates how psychology influences the decisions of investors, financial analysts, and financial markets. This area of study recognizes that investors are subject to biases, limited self-control, and irrational behavior (Patel et al., 2019). Various contemporary schools of thought, such as those focused on rational behavior (Loerwald & Stemmann, 2016), cognitive dissonance (Adil et al., 2022), prospect theory (Özen & Ersoy, 2019), and heuristics (Katarachia & Konstantinidis, 2014), have been inconsistent in explaining why investors behave unpredictably. In light of this, Patel et al. (2019) pointed out in their groundbreaking study that people rarely have sufficient knowledge, motivation, or time to make totally logical decisions. This makes it obvious that several behavioral characteristics, such as financial literacy, emotions, knowledge, skills, confidence, prejudice, etc., may influence individual or organizational investment decisions (Katarachia & Konstantinidis, 2014). As a result, this study recognizes the role that financial literacy plays in a range of personal investing choices.

An explanation of how money functions in contemporary society, including how people manage, invest, and exchange money with one another, is provided by financial literacy as a behavioral element. Investors must also possess the knowledge necessary to evaluate financial risks and opportunities, make wise decisions, know whom to contact for support, and take other actions necessary to improve their financial situations (Hilgert & Hogarth, 2003; Paraboni & da Costa, 2021). Financial institutions such as banks, depository institutions, pension authorities, and insurance companies provide services or tools referred to as financial goods (Aren & Nayman Hamamci, 2022). A few examples of formal financial products include savings accounts, checking accounts, credit and debit cards, insurance products, loans, mobile banking, mutual funds, pension plans, stocks, bonds, and mortgages; microfinance organizations have also been included in this category (Wong & Carducci, 1991). On the other side, the financial assistance offered by friends, family, neighborhood associations, and private individuals can be identified as informal financial products (Hilgert & Hogarth, 2003). In Sri Lanka, even though there are varieties of investment options, there is a notable lack of alternative investment products (Jayawardana, 2021) and many investors tend to opt for savings and fixed deposits over other financial options (Edirisinghe et al., 2015; Ranaweera &

Kawshala, 2022).

However, despite the fact that the Central Bank of Sri Lanka (2020) has provided new investment options in 2020, such as Real Estate Investment Trusts (REITs), new retirement plans, and equities and corporate bond derivatives, the aforementioned financial instruments are conspicuously absent in the nation. Because Sri Lanka's population is aging at a rapid rate, there should be a substantial demand for retirement programs, pension products, and insurance products. However, according to Jayawardana (2021), the majority of Sri Lankan investors opt for savings and fixed deposit products provided by banks and financial institutions. He found that alternative investment products have a poor penetration rate in the same study. For instance, only approximately 25,000 of the more than 750,000 Central Depository Accounts (CDS) trade actively, with the remainder being duplicate or dormant accounts. It is crucial to consider whether financial literacy influences these kinds of investing decisions while responding to Jayawardana's demand (2021).

Nevertheless, Sri Lanka is recognized as having a superior educational system and a higher percentage of literate people when compared to many other emerging countries. According to estimates from the Central Bank of Sri Lanka (2020), Sri Lanka has the highest adult literacy rate in South Asia at 92%. On the other hand, Sri Lanka had the highest proportion of financial literacy linked to its South Asian peers in the global financial literacy survey that was done on more than 150,000 adults in over 140 countries (Xiao & Porto, 2017). In the meantime, Sri Lanka has a low level of financial literacy and a significant gap between its literacy and financial literacy levels, according to Jain et al. (2022). As these authors explain, it is experimentally reasonable for the researcher to further assess whether financial literacy has any bearing on individual investment decisions and to look into the function that risk tolerance plays when people choose from a variety of investment portfolios.

With this in mind, it is crucial to comprehend the cause of investors' growing propensity to choose savings and fixed deposits by noting the country's conspicuously noticeable lack of other financial products. The studies by Lusardi and Mitchell (2011), Paraboni and da Costa (2021), and Hilgert and Hogarth (2003) have explored external factors like technology, politics, inflation, and the country's economy on financial literacy and its influence on investment decisions. However, there is a need to refine the Theory of Planned Behavior (TPB) to better understand the relationship between financial literacy and investment behavior, considering the specific context of Sri Lanka.

Materials and Methods

Qualitative research creates connections between many ideas, disciplines, topics, and terminologies to explain complicated events. As per the nature and the context of the study the author will follow the interpretivism philosophy which advocates the researcher to comprehend how people differ in their capacity as social agents. Intending to explore the contribution of financial literacy on individual investment decisions, an inductive approach, which gives the researcher a thorough understanding of the phenomenon under investigation has been selected by the researcher (Adam et al., 2017). The flexibility of this approach will improve the quality of the research while encouraging the originality of the study (Skipton & Bail, 2014).

This study treats the problem in an inquiring manner to explore the real reality. The inquiring strategy direct researchers to easily comprehend and interpret people, groups, organizations in social, political, and related phenomena (Bhushan & Medury, 2014). The rationale behind selecting the SME industry for this study is that individuals within this sector are known for their proactive pursuit of investments, aiming to elevate their companies to new heights. SME (Small and Medium-sized Enterprise) owners and entrepreneurs are often driven by a strong desire for growth and development, which leads them to explore various investment opportunities to expand their businesses and achieve greater success. Understanding the investment behavior and decision-making processes of these individuals can provide valuable insights into how financial literacy and risk tolerance impact their choices, contributing to a more comprehensive understanding of investment dynamics within the SME industry.

A combination of purposive sampling and snowball sampling techniques was utilized to gather data in the study and the purposive sampling technique involved selecting the initial respondents, as supported by Ajzen (2002), Lusardi & Mitchell (2011), and Nasir & Khalid (2004). Subsequently, the snowball sampling method was applied to identify the balance of respondents in the SME industry who had existing investment plans. The main objective of using both purposive and snowball sampling techniques, in line with Atkinson & Messy (2011), Hilgert & Hogarth (2003), Özen & Ersoy (2019), and Satsios & Hadjidakis (2018), was to create a study sample that accurately aligned with the research goals. The research site chosen for this study was the Colombo district, the executive, judicial capital, and largest city of Sri Lanka by population.

Upon gaining access to the selected firms, 20 in-depth interviews (Appendix I) were conducted among executives whose service period was more than 5 years. In-depth interviews were carried out in person or online via Teams for the primary study. Once conducting the interviews 14th interview was the moment at which the study reached data saturation and, to confirm the data saturation threshold introduced by Braun and Clarke (2014), the researcher conducted an extra six (06) interviews. Audio recordings of all interviews were conducted in English with the consent of the participants. There was no hesitation or resistance from the respondents regarding the recording process. All recorded interviews are transcribed and saved as a supporting device for data management. The duration of the interviews ranged from 20 to 30 minutes. A structured interview guide (Appendix II) was utilized to ensure that the interview questions remained focused and consistent across all participants. The use of this guide helped maintain the coherence and relevance of the discussions. The researcher also took brief field notes during the interviews. It was essential for the researcher to strike a balance between taking notes and maintaining the trust and rapport established with the participants.

Thematic analysis, as described by Braun & Clarke (2013), served as the data analysis method in this study. The process involved coding the data to identify key features related to the research questions, "How does financial literacy contribute to individual investment decisions?" and "What is the role of risk tolerance in the relationship between financial literacy and individual investment decisions?". Three dimensions of financial literacy and their impact on investment decisions were uncovered, along with the role of risk tolerance in shaping individual choices. The findings in the next session, provide valuable insights into the complex interplay between these factors in the fascinating world of investment decision-making.

Propositions and Concept Indicator Model

The theory of planned behavior (TPB) has been widely applied and is thought to be one of the most influential models in a variety of study domains. The TPB has also emerged as a leading theory and has been used in numerous behavioral domains (Hallahan et al., 2014). Attitude toward behavior (in this case financial attitudes, FA), social norms (SN), and perceived behavioral control (PBC) together have an impact on the development of behavioral intention (Ajzen, 2002). Only a few works of research on financial decision-making, of Raut and Das (2017), Remund (2010), Lusardi and Mitchell (2011), and Wong and Carducci (1991) have used the TPB model as a lens to examine investors' intentions to trade online and discovered a favorable association between FA, SN, and PBC in investment decisions. By addressing this lacuna, the current study makes an effort to evaluate investment success in terms of variables including financial attitudes, subjective norms, and perceived behavioral control.

The rationale for examining the relationships between financial attitudes, social norms, perceived behavioral control, financial knowledge, and individual investment decisions lie in understanding the underlying factors that influence individuals' decision-making processes in the realm of personal finance. By investigating these variables, researchers can gain insights into how motivations, societal influences, perceived control, and knowledge impact individuals' investment decisions. Previous studies (Ahmed et al., 2021; Özen & Ersoy, 2019; Sabir et al., 2021; Tahir et al., 2021) have established links between these variables and financial behavior, highlighting the significance of exploring these relationships to enhance our understanding of individuals' investment choices.

When it comes to financial planning, one of the most crucial factors in directing people toward a financially sound investment is their risk tolerance. A higher risk is linked to a higher chance of a larger return, whilst a lower risk is linked to a higher probability of a lower level of return. When an investor considers risk and returns when making investment decisions, the risk-return trade-off becomes effective. This fact has been supported by Gallery et al. (2011), Fachrudin and Fachrudin (2016), and Stolper and Walter (2017). According to research by Lusardi and Mitchell (2011), Raut (2020), and Remand (2010), financial literacy and risk tolerance have a significant positive relationship. Risk tolerance is used to assess the contribution to individual investment decisions, but there hasn't been any research done to establish its importance as an exogenous construct.

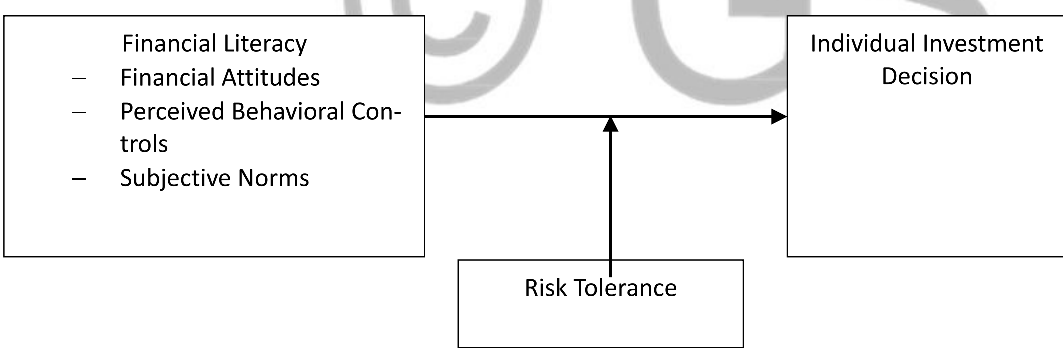

Figure 1: Concept Indicator Model
Source: Concept Indicator Model

Results and Discussion

Financial Literacy Yields Financial Attitude, Subjective Norms, and Perceived Behavioral Control

The study and interpretation of the data revealed two (02) categories, including "Are you a risk-taker or a risk-averse person? To clarify the function of risk tolerance, add the phrase "and Assess your Level of Risk Tolerance." The data analysis and the inclusion of risk factors have shown that most respondents take risks. They accept the truth in the adage "the higher the risk, the higher the return" and would want to take the risk inherent in the stock market. As a result, many risk-takers have made investments in erratic markets like the stock market. On the other hand, risk-averse people don't like taking chances, so they invest in low-risk products like savings accounts and fixed deposits.

The data from the poll showed that people's willingness to accept losses in unforeseen circumstances depended on their level of risk tolerance. Investors were accustomed to handling several investments as well as third-party authorizations for investments in order to remain stable during unpredictable times. The repetition of such operations raises people's tolerance levels and encourages them to invest more. As a result, choosing the best selections from investment portfolios requires a high level of financial knowledge from those making investments. Therefore, it may be inferred that those who are willing to take on a lot of risks are motivated to invest and that their choice of investments is influenced by their level of financial literacy. Investors with a higher level of financial literacy are more likely to invest in sophisticated financial products, which are typically linked with higher risk but also larger potential gains.

Risk Tolerance Contributes to the Relationship between Financial Literacy and Individual Investment Decisions.

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Conclusion

The goal of this research is to produce new knowledge that will be useful to investors when they select investments or build portfolios. Investors can choose the best course of action to reduce or avoid losses in the future when they have a thorough awareness of all the varied and intricate aspects that affect investment decision-making. When making investments, investors must take into account a number of complex factors, including financial attitudes, subjective norms, and perceived behavioral controls. According to the study's findings, one's ability to take on hazardous investments in order to manage their investments effectively and optimize returns may be enhanced by having a greater level of financial literacy. Greater financial knowledge and investing expertise will enhance risk tolerance, which will force investors to make riskier investment decisions that correspond to their higher level of risk tolerance. The study hereby invites future researchers to conduct quantitative studies to validate the findings of this qualitative research and examine the relationships between financial literacy, risk tolerance, and investment decision-making among executives in manufacturing companies in Sri Lanka. However, it is important to note here that this qualitative research is limited by its context-specific findings and potential biases arising from self-reported data.

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