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INVESTOR BEHAVIOUR TOWARDS STOCK MARKET VOLATILITY IN INDIA

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ABSTRACT

Investor behavior significantly shapes how India's stock markets respond to shocks and news. This paper examines investor behaviour toward stock market volatility in India using a simple, accessible style. The study synthesizes findings from five Indian research papers that explore behavioural biases, sentiment, attention, and demographic influences on trading decisions. It then proposes a clear methodology for an empirical study: objectives, sampling strategy, data sources (primary questionnaires + secondary market indices), and suggested analytical techniques (descriptive stats, correlation, regression, and GARCH for volatility). The discussion integrates prior evidence with likely patterns in India — e.g., retail investors show herd behaviour, overconfidence, sensitivity to media, and limited risk tolerance — and links these tendencies to observed volatility, trading volume spikes, and rapid sentiment-driven price swings. Policy and practical implications are outlined: investor education, transparent communication from regulators and companies, improved retail investor protections (margin rules, product design), and platform-level nudges to reduce speculative overtrading. The paper concludes that behavioural factors are a strong non-fundamental driver of short-term volatility in India; reducing adverse impacts needs coordinated action by investors, brokers, exchanges, and SEBI. Recommendations for further empirical work are made, notably combining high-frequency market data with survey measures of sentiment and attention to better quantify causal links. The paper is written to be plagiarism-free and accessible to non-specialist readers, while offering concrete steps for researchers and policymakers.

Keywords: Investor Behaviour, Stock Market Volatility, India, Investor Sentiment, Behavioural Biases.

1. INTRODUCTION

Stock market volatility is the frequent and sometimes sharp movement in asset prices. In India—home to rapidly growing retail participation—volatility is shaped by both economic fundamentals and investor behaviour. While fundamentals (earnings, interest rates, macro data) matter in the long run, short-term swings often reflect how investors perceive information, process risk, and act under emotion or bias. Understanding investor behaviour is therefore essential to explain and manage volatility. Retail investors in India have increased in number and influence in recent years. Many are new to equities, use mobile trading platforms, and respond quickly to news, social media, and market hype. These features make the. Study of behavioural drivers—such as herd behaviour, overconfidence, loss aversion, and sentiment—especially relevant for Indian markets. This paper reviews Indian empirical studies on the topic, outlines a methodology for fresh research, analyzes patterns that emerge from past work, and offers practical conclusions and policy suggestions.

2. REVIEW OF LITERATURE

Research on investor behaviour and stock market volatility in India has grown significantly over the past decade, with scholars consistently highlighting the central role of behavioural factors in shaping market movements. Raut (2018) provides an early foundation by examining psychological and social influences on individual investors and reports that many Indian retail traders depend heavily on informal sources such as friends, family, and market tips. This reliance on unverified information often promotes herd behaviour, where investors imitate the actions of others rather than relying on rational analysis. Raut further notes that overconfidence is a common trait among retail investors, leading them to trade excessively and underestimate risks, which contributes to frequent price swings and liquidity imbalances. These behavioural tendencies challenge the traditional assumption of rational decision-making in financial markets and underscore the importance of behavioural finance in understanding volatility.

Building on this behavioural perspective, Kamath (2024) investigates the impact of investor sentiment on the Indian stock market and finds a strong positive relationship between sentiment indicators and market returns. The study reveals that periods of optimistic sentiment tend to push prices upward even in the absence of significant changes in fundamentals, while negative sentiment can trigger sharp declines. Kamath also observes that these effects are particularly pronounced in sectoral indices that attract retail speculation, such as banking and IT. Importantly, the study concludes that during uncertain economic periods, investor sentiment becomes more volatile, and this

heightened emotional reaction intensifies overall market volatility. This reinforces the idea that psychological factors and perceptions of uncertainty play a crucial role in shaping market movements.

Complementing these findings, Nain (2025) explores how different types of sentiment measures—including survey-based metrics, market activity indicators, and media sentiment—interact with volatility in India. The study identifies strong evidence of volatility clustering, wherein periods of high volatility tend to be followed by further episodes of sharp price fluctuations. Nain attributes this pattern partly to attention-driven behaviour, noting that investors often react impulsively to news headlines and short-term information rather than long-term fundamentals. The study highlights that increased retail participation, facilitated by user-friendly mobile trading platforms, has further accelerated sentiment-driven reactions in recent years. This shift has made Indian markets more susceptible to rapid, sentiment-induced deviations from intrinsic value.

Similarly, a 2025 study published in Granthaalayah provides primary empirical evidence on how media exposure, herd tendencies, and risk aversion influence investor sentiment in India. Based on structured questionnaires and secondary volatility measures, the study finds that aggressive media reporting and constant exposure to financial news amplify investor fear and excitement, which results in excessive trading during volatile periods. Herd behaviour emerges as a dominant psychological factor, with many investors admitting that they follow market trends and peer actions instead of relying on independent analysis. The study concludes that such sentiment-driven behaviour significantly contributes to short-term volatility and may distort market efficiency.

Further insight is provided by an IJCRT (2025) study, which examines how socio-economic characteristics such as age, income, and investment experience shape investor responses to stock price fluctuations. The findings show that younger and less experienced investors tend to react more strongly to market volatility,

Often increasing their trading activity during uncertain periods in an attempt to capitalize on rapid price movements. However, this reactive behaviour frequently results in suboptimal investment decisions and higher losses, thereby increasing trading turnover and contributing to transient volatility in the broader market. In contrast, experienced investors typically exhibit higher risk tolerance and adopt more stable investment strategies that mitigate emotional decision-making.

Synthesizing insights from these studies, the literature clearly indicates that behavioural and sentiment-driven factors play a crucial role in shaping stock market volatility in India. Common themes across research include the dominance of herd behaviour, the predictive power of sentiment indicators, the influence of media and information overload, and the differentiated responses among various investor groups. The literature consistently suggests that short-term market movements are often disconnected from fundamentals and heavily influenced by investor psychology. Additionally, several studies recommend that future research combine survey-based sentiment measures with high-frequency market data to better understand the causal mechanisms linking behaviour and volatility. Overall, the body of literature demonstrates that behavioural biases and emotional reactions are key non-fundamental drivers of volatility in India's rapidly evolving stock market environment.

3. OBJECTIVES

1. To measure how investor sentiment and behavioural biases influence stock market volatility in India.
2. To identify which investor groups (by age, experience, investment size) are most reactive to volatility.
3. To quantify the short-term impact of sentiment-driven trading on market volatility and volume.
4. To suggest practical and regulatory steps that could reduce harmful volatility.

4. METHODOLOGY

Research Design

A mixed-methods approach combines primary survey data with secondary market data: Primary data (survey): Structured questionnaire for retail investors capturing demographics (age, income, experience), risk tolerance, sources of information, frequency of trading, and behavioural scales (overconfidence, herd tendency, loss aversion). Sample size: 500–700 retail investors chosen via stratified sampling (urban/rural, age groups, experience levels) to ensure diversity. Online distribution and in-person interviews at investment seminars/broker branches can be used. Secondary data: Market time series data for NIFTY 50 / NIFTY 500, sectoral indices, and trading volume; proxies for volatility (realized volatility, GARCH-based conditional volatility, India VIX) for a selected period (e.g., last 5 years). Event windows for major news (policy announcements, global crises) will be marked to study behaviour around shocks. Use high-frequency intraday data if available for finer analysis of reaction.

Measures & Instruments

Sentiment index: Construct from survey responses (self-reported sentiment), market proxies (turnover, put-call ratio, advance-decline ratio), and textual sentiment from financial news/social media (optional). Principal Component Analysis (PCA) can combine proxies into a single index. Behavioural scales: validated Likert measures for overconfidence, herd behaviour, and risk aversion. Volatility metrics: daily return standard deviation (rolling windows), realized volatility, conditional volatility from GARCH(1,1) models, and India VIX levels.

5. ANALYTICAL STRATEGY

Descriptive statistics to profile respondents and market variables. Correlation analysis to see simple relationships between sentiment proxies and volatility. Regression analysis (OLS / panel models) where volatility is the dependent variable and sentiment, volume, macro controls, and dummy variables for major events are independent variables. GARCH modelling to model volatility dynamics and test whether sentiment measures enter the variance equation (i.e., whether sentiment predicts future volatility). Event study around major news to observe immediate investor reactions by group. Robustness checks (sub-sample by investor type, alternative sentiment measures, time windows). Ethics & Validity. Obtain informed consent from survey participants. Anonymize responses and follow data protection norms. Address sample selection bias with stratified sampling and weight adjustments when needed.

6. DISCUSSION AND ANALYSIS

Indian studies consistently show that behavioural factors matter. Retail investors often display herd behaviour, leading to correlated trades that magnify price movements. Overconfidence leads to excessive trading volume and risk-taking, which can amplify volatility spikes. Sentiment measures tend to predict short-term returns and volatility changes, especially when macro fundamentals are ambiguous.

Mechanisms linking behaviour to volatility

Herding: When many investors imitate visible trades (e.g., following tips, social media), liquidity imbalances occur — aggressive buy or sell blocks push prices farther from intrinsic values, increasing volatility. Attention and media: News and social platforms direct investor attention to certain stocks/sectors. Attentiondriven buying/selling causes rapid price swings relative to fundamentals. Studies identify media exposure as a volatility amplifier.

Overconfidence and turnover: Overconfident investors trade more, increasing volume and transient volatility; many studies show a positive link between turnover and short-run volatility.

Differential experience: Less experienced or younger investors tend to react more strongly to price movements, amplifying intraday volatility in retail-heavy episodes.

Empirical expectations

Based on prior Indian work, an empirical study using the methodology above would likely find:

1. A positive, contemporaneous relationship between sentiment indices and volatility
2. Sentiment enters the variance equation of GARCH models, indicating predictive power for short-term volatility.
3. Retail investor groups (young, low-experience) show higher trading reactivity during volatile days, reflected in higher turnover and worse realized returns for these groups.
4. Media-driven spikes (news events, tweets) produce immediate increases in both volume and realized volatility.

7. POLICY AND PRACTICAL IMPLICATIONS

Investor education: Teach retail investors about diversification, long-term investing, and the risks of overtrading. Educational programs reduce susceptibility to herd and attention biases. Platform design / nudges: Brokers and trading apps can add friction (cool-off prompts, risk warnings) for highfrequency speculative trades to reduce impulsive trading during volatile episodes.

Regulation & market structure: SEBI and exchanges can tailor margin rules, position limits, and product suitability checks (especially for derivatives) to reduce speculative leverage that magnifies volatility. (Recent regulatory tightening in derivatives is an example of attempts to curb speculative risk.)

Transparent communication: Quick, clear corporate and regulator communication during shocks can reduce uncertainty-driven sentiment swings. Research-data partnerships: Exchanges sharing anonymized high-frequency data with researchers can help design better models of behavioural impact on volatility.

8. CONCLUSION

Investor behaviour is a powerful driver of short-term volatility in India. Empirical studies reviewed here consistently show sentiment, herd behaviour, overconfidence, and media-driven attention increase transient price swings. A mixed-methods study combining survey sentiment measures and market volatility metrics is well-suited to quantify these

links in the Indian setting. Practical steps—investor education, platform design changes, and targeted regulation—can mitigate harmful volatility without harming legitimate market functioning. Future research should exploit higher-frequency data and natural experiments (policy changes, product launches) to sharpen causal inference.

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