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Individual's Psychology and Investment Decision Dynamics: A Systematic Literature Review

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Introduction

Investment decision-making has been traditionally explained through the classical financial theories, which assume that, individuals are rational and they always seek to maximise the expected returns, based on complete information. However, increasing evidence from the behavioural finance further suggests that investment decisions are often influenced by the psychological, emotional and cognitive factors (Abideen *et al.* 2023). These factors further lead the individuals to deviate from the rational behaviour. Different factors, namely, overconfidence, loss aversion, herding behaviour, risk perception and emotional responses have significantly shaped the way individuals could evaluate the investment opportunities, while respond to the market uncertainties. These psychological influences have become increasingly relevant in the dynamic financial environment at present, which is characterised by the rapid technological advancements, increased the access to the financial information, digital trading platforms, while heightened the market volatility.

It can be seen that, over the past two decades, research on the investor psychology has further expanded considerably across different nations, markets and investment contexts (Bai, 2023). Despite this expanding body of literature, existing studies remain fragmented, hence, focusing on specific psychological biases or specific investor groups without providing a comprehensive synthesis of the way, these factors could collectively influence the dynamics of investment decisions. Thus, the key objective of this study is to integrate the present knowledge, identify the prevailing themes, highlight the methodological trends and uncover the research gaps. It aims to critically examine the existing literature on the individual's psychology and different investment decision dynamics, hence, offering a comprehensive understanding of the psychological determinants of investment behaviour (Saivasan & Lokhande2022). Along with this, this study proposes the future research directions for the researchers, policymakers and practitioners in the context of behavioural finance.

Problem Statement

The growing field of behavioural finance has established that investment decisions of individuals influenced not only by economic and financial factors, but also by a range of psychological, cognitive and emotional determinants (Al-Zakwani, 2026). There are different studies which have analysed the behavioural biases, such as, overconfidence, herding, loss aversion, anchoring and risk perception. However, the existing literature has been dispersed across numerous theoretical perspectives, geographical contexts, categories of investors and research methodologies. This fragmentation has made it more difficult to obtain a comprehensive understanding of the way; psychological factors have collectively shaped the dynamics of the investment decisions. Furthermore, this rapid evolution of the financial markets through digital trending platforms, social media, fintech innovations and artificial intelligence have introduced new behavioural dimensions which have not been systematically synthesised (Bacchoo & Mishra, 2025). Consequently, there is a requirement for systematically reviewing different literature which could critically integrate the existing evidence, identify the dominant themes, while evaluate methodological trends and highlights the inconsistencies and research gaps to guide any future investigations.

Research Objectives

- To systematically synthesise the existing literature regarding the influence of individual's psychology on investment decision dynamics
- To critically examine the key psychological factors, theoretical frameworks and methodological approaches, adopted in previous research study
- To identify the research gaps along with proposal of future research directions for understanding the investor psychology during investment decision-making

Review Methodology

This study adopts a "Systematic Literature Review (SLR)" approach though which, one can systematically identify, screen, evaluate and synthesise the existing research regarding individual psychology and investment decisions dynamics. This review follows the PRISMA framework, to ensure a transparent and structured process across four stages, which have been listed below (prisma-statement.org, 2026).

Identification

A comprehensive literature search was conducted by using three key academic databases, namely, Scopus, Google Scholar, Web of Science and others. Appropriate combinations of keywords, consisting of "investor psychology", "investment decisions", "investment behaviour", "behavioural finance", "psychological biases" and "individual investor". The initial search identified 23 records.

Screening

Following this identification stage, it can be seen that, duplicate records have been removed, resulting in 15 unique records. These studies have been subsequently screened based on their titles and abstracts. A total of 5 articles have been excluded because they were off-topic, non-empirical and 25 articles for not published in English. Consequently, 105 articles have been progressed to the full-text assessment stage.

Eligibility

The full texts of the 150 articles, which are potentially relevant have been assessed against the predetermined eligibility criteria. Studies have been excluded when they were conference abstracts, where the accessible full text were lacked, hence, didn't sufficiently focus on the behavioural finance or were published before 2022. Following this assessment, only 23 articles have met the requirements for the qualitative or thematic analysis.

Inclusion and Synthesis

Along with this qualitative synthesis, 75 studies have been considered as appropriate ones for review, resulting in a final evidence base of 23 articles. The identified literature has been evaluated according to the publication trends, geographical context, theoretical foundations, psychological factors, methodological approaches as well as some major findings. A thematic synthesis has employed to identify some dominant themes, emerging trends, contradictions and research gaps, concerning the relationship between the individual psychology and investment decision dynamics. This systematic process further strengthens the reliability and comprehensiveness of the findings of the review.

Theoretical Foundations

The study of individual psychology and investment decisions dynamics is primarily grounded in "Behavioural Finance Theory", which has challenged the assumption of fully rational investors, proposed by traditional financial theories (Goyal *et al.* 2026). There are several theoretical perspectives, which provide a foundation for understanding the way psychological factors, influencing the investment behaviour.

Prospect Theory: This theory is developed by Kahneman and Tversky, who have explained that individuals could evaluate the potential gains and losses, relative to a reference point instead of solely considering their final wealth.

The concepts of loss aversion, risk sensitivity and framing effects could explain the reasons, investors might make some inconsistent decisions under uncertainty (Regenwetter, Robinson & Wang, 2022).

Heuristic Theory: This theory highlights the way individuals could use simplified mental strategies, while processing the complex financial information. Different types of biases, such as, representativeness, availability and anchoring could influence the perception of the investors, their expectations as well as choices (Ahmed & Rura, 2024).

Bounded Rationality Theory: This theory suggests that, investors have limited information-processing capabilities, time and cognitive resources. Consequently, it might depend on some simplified decision rules instead of conducting the complete rational analysis.

Social Influence Theory: It further explains the behaviours, such as, herding behaviour, where individuals could follow the actions or opinions of other investors, specifically during the periods of market uncertainty (Oliveira *et al.* 2025).

Hence, based on the above discussion, it can be stated that, these theoretical perspectives have demonstrated that investment decisions have been shaped by the interaction of cognitive biases, emotions, risk perceptions, information processing and social influences (Ekarani & Artini, 2025). In this way, it provides an integrated foundation for examining the complex dynamics of individual investment behaviour.

Thematic Literature Review

The discussion on individual psychology and investment decision dynamics have further demonstrated that investment behaviour couldn't be explained solely through traditional financial assumptions of rationality, risk-return optimisation and complete information. Instead of this, investment decisions have emerged from the interaction of cognitive biases, emotional responses, risk perceptions, social influences as well as individual characteristics.

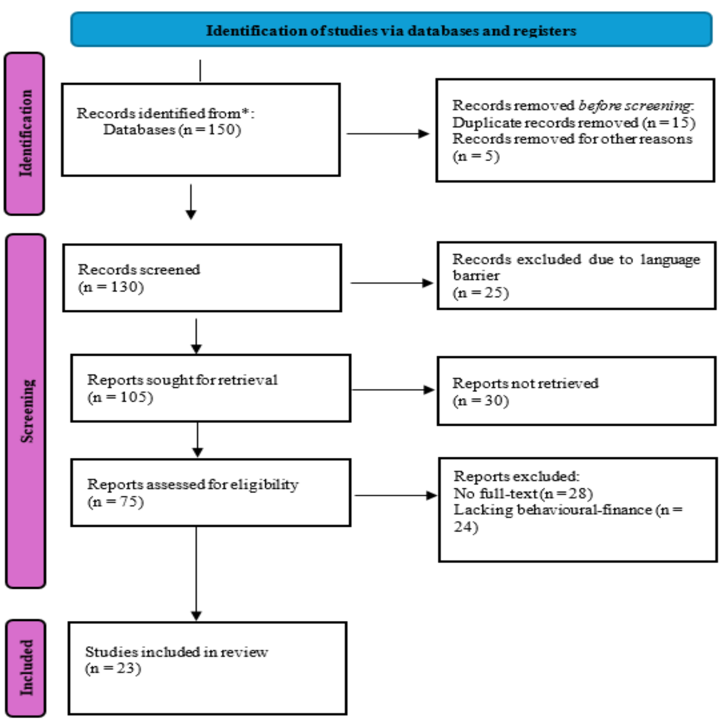

Figure 1: Database Registerer
(Source: prisma-statement.org, 2026)

Cognitive Biases and Investment Decision-Making

Cognitive biases represent one of the most extensively examined dimensions of the investor psychology. Different biases, like, overconfidence, anchoring, representativeness, confirmation biases, conservatism and mental accounting have frequently influenced the way individuals could interpret the financial information, while make the investment choices (Dhungana *et al.* 2022). On the other side, overconfident investors tend to overestimate their knowledge and ability to predict the movements of the markets, which potentially resulting in excessive trading and insufficient diversification. Similarly, anchoring could cause investors to depend excessively on previously observed prices or information, while evaluating the new investment opportunities (Gabhane, Sharma & Mukherjee, 2023).

However, this discussion, doesn't indicate that all cognitive biases could operate uniformly. Their influences appear to depend on the investment experiences, financial literacy, market conditions and the complexity of the decisions (Noch & Rumasukun, 2024). Experiences investors might potentially develop the mechanisms for controlling certain biases, although experiences don't necessarily eliminate the behavioural tendencies (Sathya & Gayathiri, 2024). This suggests that psychological biases shouldn't be treated as isolated determinants, instead of, their effects need to be examined within the wider decision-making environment.

Emotional Factors and Investment Behaviours

Emotions constitute another significant determinant of investment decision dynamics. Different aspects, like, fear, greed, anxiety, regret, optimism and sentiment, could substantially influence the willingness of the investors to accept the risks and their responses to make fluctuations (Lakshmi *et al.* 2024). During the periods of uncertain market conditions and sharp declines, fear might encourage the investors to sell their assets prematurely. On the other side, excessive optimism during the rising markets might encourage the speculative investment. On the other side, a critical observation from the discussion is that emotional influences are often interconnected with the cognitive biases. For example, fear of losses could reinforce the loss aversion, whereas excessive optimism might strengthen the overconfidence of the people. Consequently, separating the cognitive and emotional influence might provide an incomplete explanation of investment behaviour (Verma *et al.* 2026). Moreover, emotional responses could differ according to the financial experiences of the investors, their personality, investment horizon as well as prevailing market conditions. This states a requirement for research which considers the combined instead of independent effects of cognition and emotion.

Risk Perception, Risk Tolerance and Investment Decisions

Risk perception and risk tolerance from a central link between the individual psychology and investment choices. Investors different considerably in their interpretation of the financial risks, even while exposed to the identical market information (Jain *et al.* 2023). It can be stated that, risk-averse individuals might prefer the safer instruments, such as, deposits and bonds, while investors with greater risk tolerance might demonstrate the stronger preferences for equities, mutual funds or other market-linked investments.

The discussion of several articles also indicates that demographic and socio-economic characteristics, consisting of age, income, occupation, education and investment experiences, might influence the risk attitudes (Almansour, Elkrghli & Almansour, 2023). However, findings concerning these relationships are not always consistent. For example, age might be associated with the greater risk aversion in some studies, while other research suggest that financial knowledge and investment experiences might be more influential than the chronological age. Therefore, demographic characteristics should not be considered as the deterministic predictors of the investment decisions (Herliana, Ratnawati & Djumahir, 2023). Rather, it might interact with the psychological characteristics and financial circumstances to shape the risk perceptions of the individuals.

Social Influence, Herding and Information Environment

Investment decisions are also influenced by the social and informational environment, surrounding the individuals. Herding behaviour occurs when investors follow the actions of other market participants, instead of depending exclusively on their own analysis (Widyari, Putri & Sari, 2024). Social networks, financial advisors, family members, peers, media reports, online investment communities and social media platforms could therefore influence investment preferences. The increasing digitalisation of financial markets has intensified that kind of phenomenon. At present time, investors have immediate access to the market opinions, online discussions, influencer content and real-time information (Wang & Nuangjamnong, 2022).

While increased information availability could improve the investment awareness, excessive exposure to unverified or emotionally charged information might encourage the impulsive decision-making, while reinforce the confirmation biases. Most importantly, the discussion further presents a dual perspective on social influence. Following the experienced investors or professional advice might improve the quality of the decisions, while blindly following the popular investment trends might contribute to the speculative behaviour (Viga, 2025). Thus, the quality, credibility and interpretation of information are critical to determine whether social influence supports or undermine the rational investment decisions.

Financial Literacy, Technology and Emerging Investment Behaviour

The discussion at present increasingly connects the investor psychology with financial literacy and technological transformation (Parsai & Chandok, 2025). It can be stated that, financial literacy could improve ability of individuals to evaluate the risks, understand investment products, while interpret financial information. However, financial knowledge alone might not eliminate the behavioural biases. A financially knowledgeable investors could still display the overconfidence, emotional reactions or herding tendencies. At the same time, digital platforms, mobile trading applications, Robo-advisory services, AI and fintech have transformed the investment environment. These technologies have reduced barriers to market participation and increased access to the financial information (Suresh, 2024). However, greater accessibility might also encourage the frequent trading and short-term decision-making. The ease of executing transactions could further reduce the psychological barriers associated with the investing, while potentially encourage the impulsive behaviour of the individuals. This emerging evidence therefore highlights a significant research issue, namely, technology doesn’t simply change the investment opportunities and it might also reshape the psychological mechanisms through which decisions have been made (Iram, Bilal & Ahmad, 2023). Existing research therefore remains relatively fragmented regarding the interaction between digital environments, investor psychology and behavioural biases, specifically among younger and first-time investors.

Overall, it can be stated that, this discussion in existing literature has established that investment decisions are multidimensional behavioural processes instead of purely rational financial calculations (Bihari *et al.* 2022). Cognitive biases, emotions, risk perceptions, social influences, financial literacy as well as technological environments could interact to shape individual investment behaviour. However, it should be noted that, much of this existing research examines the individual behavioural factors separately, hence, limiting the understanding of their combined influence. Along with this, considerable variation exists across different countries, investor categories, market conditions and research methodologies (Haidari, 2023). The dominance of cross-sectional quantitative research also has limited the understanding of the way; investor psychology could change throughout the time. Future research study should therefore adopt the integrated, longitudinal, cross-cultural and mixed-method approaches to examine the way; psychological and contextual factors collectively shape the investment decision dynamics (Kumar *et al.* 2023). This kind of approach could provide a more comprehensive understanding of the increasingly complex relationship between the individual psychology and investment behaviour.

Research Gaps

This systematic review has identified several important gaps in the existing literature regarding the individual psychology and investment decision dynamics. Firstly, existing research studies have frequently examined different psychological factors independently, for example, overconfidence, loss aversion, herding as well as risk perception, instead of examining their combined and interacting effects on the investment decisions (Jain *et al.* 2023). Secondly, this literature is dominated by cross-sectional quantitative studies, hence, has created limited understanding regarding the way, investor psychology and behavioural patterns could evolve throughout the time and across different market conditions. Thirdly, research findings have remained inconsistent across different contexts, such as, geographical, demographic and cultural, specifically regarding the influence of age, income, financial literacy and investment experiences. Fourthly, relatively limited research has integrated the emotional factors, cognitive biases, social influences and financial characteristics within a single conceptual framework (Kumar *et al.* 2023). Fifthly, it can be seen that, the rapid development of fintech, social media, mobile trading, artificial intelligence and digital investment platforms have created several new behavioural dynamics, which have remained comparatively underexplored. Lastly, emerging investors, specifically younger and first-time investors have received insufficient attention compared with the traditional retail investors. These gaps further have highlighted the requirements of longitudinal, cross-cultural, mixed-method and interdisciplinary research, which have examined the psychology of the investors as the dynamic one along with interconnected process, instead of as a collection of isolated behavioural factors (Che Hassan *et al.* 2023).

Future Research Direction

In the context of future research direction, it should be noted that, this study should examine numerous dynamics of the investor decisions as an integrated psychology process, instead of evaluating the cognitive, emotional and social biases independently (Hossain & Siddiqua, 2024). Firstly, empirical studies should investigate the combined effects of overconfidence, anchoring, loss aversion, regret, herding, FOMO as well as confirmation biases on risk perception, investment timing, frequency of the trading and choosing the portfolio. Secondly, future research needs to examine the financial literacy, demographic characteristics, market contexts and investor experiences as the moderating factors.

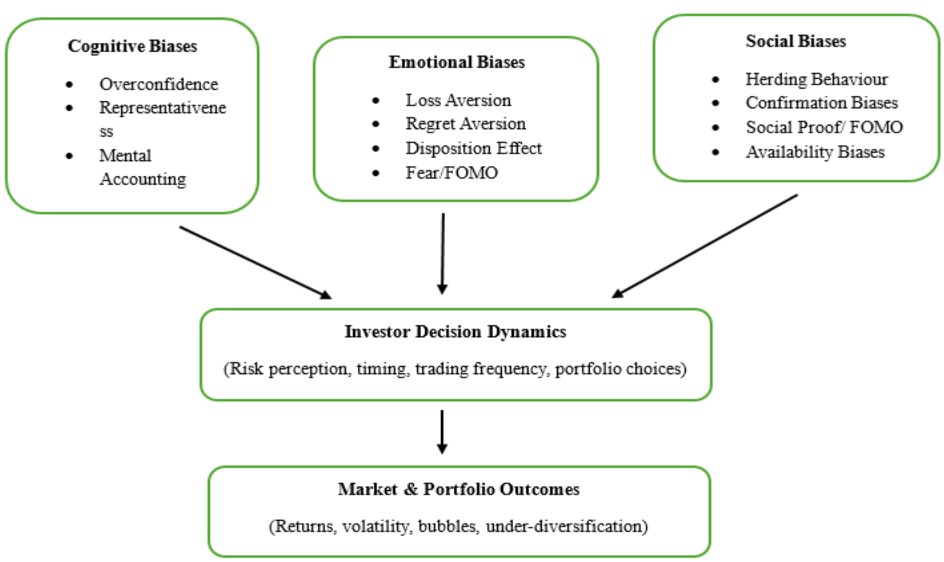

Figure 2: Proposed Conceptual Framework
(Source: Author's Creation)

In this way, the reasons can be determined regarding the psychological biases, producing the different investment outcomes across the individuals. Thirdly, longitudinal and experimental studies are required to capture the changes in the context of investor psychology during the market crises, bubbles and periods of high volatility. Along with this, future studies need to incorporate the digital investment platforms, social media, AI-based financial advice as well as online social proof through which, the emerging forms of the behavioural influence can be understood (Ngcamu *et al.* 2023). Finally, cross-cultural and comparative research across the developed and emerging markets can strengthen the generalisability of findings, while contribute to a more comprehensive behavioural finance framework, linking the psychology of the investors, decision dynamics and market as well as portfolio outcomes.

Conclusion

Based on the above discussion, it can be stated that, individual investment decisions have been shaped by a complex interaction of cognitive, emotional and social psychological factors, challenging the traditional assumption of purely rational decision-making. The reviewed literature further has demonstrated that cognitive biases, such as, overconfidence, anchoring, representativeness and mental accounting could influence the way, investors have processed the information, while evaluate the opportunities. Similarly, emotional biases, consisting of loss aversion, regret, fear and FOMO could affect the risk perception, investment timings and response to the uncertainty within the market. It should be noted that, social influences, such as, herding, confirmation biases, social proof as well as availability of the information could further reshape the individual investment behaviour.

On the other side, the proposed conceptual framework has integrated these different psychological dimensions with the decision dynamics of the investors, specifically with risk perception, trading frequency, timing of the investments as well as choices of the portfolio, which could subsequently influence the market and portfolio outcomes, such as, returns, volatility, bubbles as well as under-diversification. This review also indicates that financial literacy, demographics, experience of investors as well as market context, which might moderate these relationships. The research in future should therefore adopt the integrated, interdisciplinary and technology-oriented approaches to examine the evolving behaviour of the investors. Thus, it can be stated that, overall, it is important to understand the psychology of the investors, which provides some significant insights for improving the investment decisions, strengthening the financial literacy and developing more effective behaviour finance strategies for increasing complex financial markets.

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