

THE ANALYSIS OF APPETITE TO SPECULATE FOR THE BROKERS IN ROMANIAN CAPITAL MARKET

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Abstract

It is known that the personality of each individual has multiple facets in relation to the behavior found in everyday life and to investors on the stock exchange. This paper focuses on the study and analysis of the psychological profiles of brokers from the Romanian capital market as well as the way in which they react in both normal and extreme situations. Investment decision and in particular the decision to invest in securities listed on the stock exchange, in many cases is based on fundamental analysis or technical analysis. This is evidenced by numerous bibliographical sources specific to this field. In practice, however, intervenes a number of subjective factors affecting in a way somehow the unexpected behavior of investment brokers, or their investment decision. I propose therefore an analysis on behavior of investment brokers in the Romanian capital market as regards their inclination toward speculation and how this influences the investment decision.

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Key words: *investment decision, investor's personality, inclination toward speculation.*

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Introduction

In the specialty literature can be identified several theories that addresses the manner of investment decision making, on the financial markets. Perhaps the most relevant and most well-known of these is the efficient market theory, formulated by Eugene Fama, since 1965. Ever since then, Fama said: "an efficient market is one on which there are a large

number of rational agents who maximizes profits, are engaged in a constant competition and trying to predict the future course of action, for which the current information is available almost for free to all participants. On an efficient market, competition between the many intelligent participants leads to a situation where, at any time, the prices already reflect the effects of past and forthcoming information. In other words, on an efficient market, the current price of the action will be at all times a good estimator of its fundamental value" (Fama, 1965). Later, however in 1970 he completed the theory of efficient market, thus: "an efficient market is a market on which prices reflect perfectly and permanently available information" (Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 1970). Therefore, the efficient market theory is based on the assumption that decisions of market participants are rational. This is due in particular to the fact that much of the market participants are using at the same time most of the information available at any given time in the market. According to this theory, the hypothesis of the formation of speculative bubbles in the market could be excluded, since these are the most obvious forms of inefficiency of the market.

What happened in the last 7 years of international financial markets demonstrate however, that the behavior of investment brokers can play a very important role in the development of financial markets. The subject related to the behavior of investment brokers in the capital markets has always received the attention of investors, the media and the general public. Investment decision making by the brokers respective trading strategies used by them, were always the attention to all market participants, although brokers most often use a common logical.

And from this point of view we can say that investments in financial instruments are an attraction to investors as long as from them can be obtained yields above those that can be obtained from bonuses for deposits (Stoica, 2006). Another important aspect in this case is the fact that the derivative financial markets, we have to deal with practical issues of marketable financial instruments without limits.

Therefore, although the theory of efficient market tells us that on an efficient market are always acting rational investors with distaste for risk, and the prices of financial instruments include market information available at any given time, at least from the experience of the crisis in 2008-2010, we can no longer believe that things are like that. The first and simplest explanation in support of this idea lies in the fact that the market is not perfect. With regard to the behavior of brokers, and here can be found a wide variety of specialties, including: their objectives can often be different, the risk accepted by each is different, and the volatility of the market accepted may vary from one broker to another, the time horizon of their

investment is also different, and the differences that can be identified, can continue.

Methodology and data

In this paper I propose conducting an analysis with regard to the behavior of investment brokers in the Romanian capital market. I pursued this matter related to their inclination toward speculation and how this influences their investment decision. In order to achieve the objectives set out in this paper, I have tried to point out the few lines of brokers profile from the Romanian capital market, using for that purpose a questionnaire with 34 questions addressed to them. The questionnaire was distributed to all staff members of financial investment services authorized to operate on the capital market in Romania, both on the Bucharest Stock Exchange and on Monetary and Financial Exchange Sibiu, in February-March 2012. Response rate among them has been quite low. The analysis was performed using a number of 31 questionnaires completed. The questions of the questionnaire also made reference to their preferences in terms of investments; the investments made, the time horizon of their investment, but also to items related to temperament, fears, temper and investment personality.

Having regard to the moment of the application of the questionnaire (February-March 2012), the results of the analysis outlines especially aspects related to investment of the brokers ' behavior during the crisis, so their behavior on a decreasing trend of financial markets. It is known already that they are acting and reacting differently as regards the decision to invest, when financial markets are inscribed on an ascendant trend, from the time when the financial markets are on a downtrend.

I believe that in a market as it is the capital market of Romania, at the beginning of the road, the behavior of market participants is very important. In fact, the modernity of a market can be established by this aspect of the behavior of investment brokers, attitude, experience, personality and their qualifications.

Speculation in the stock exchange transactions

In transactions on the financial markets, respectively transactions in stock exchange markets, speculation is in simple words - taking a risk in order to achieve a win. Therefore, the claim involves the trading of financial instruments in order to achieve a net gain from the price difference. This can be done either by purchasing securities at a lower price and selling at a later time with the same financial instruments at a higher price or selling financial instruments initially at a great price and buying later the same financial instruments at a lower price. So, speculators are trying to profit from fluctuations in the market, turning them by assuming the risk, in

opportunities for them. Of course, the risk will be assumed in the case of an adverse price development in the market for the financial instruments in question, in which case the risk assumed it can turn into a loss for them.

Often, especially in the press in Romania, we can find information that speculators are the ones that create the risk of market; respectively they create the volatility for price of the various financial instruments. Surely they have a goal of obtaining profit, and through their actions they can distort somewhat market balance, creating excessive volatility. From my point of view, speculators are those who assume the risk in any market. Assuming this result ensures a high liquidity of the market and offers a more dynamic aspect to it. In any market, liquidity is a very important aspect to be taken into account when the decision is made to invest. Any participant wishes to identify easily the market counterparty. Another important role of speculators involves constantly identifying new opportunities to win, so we can say that they participate in the innovation and development of somehow in transactions on the stock exchange.

As a result of the questionnaire, I could draw a conclusion quite relevant, namely: in the Romanian capital market brokers manifest an inclination to speculation with regard to investment decision making.

Risk in the brokers vision

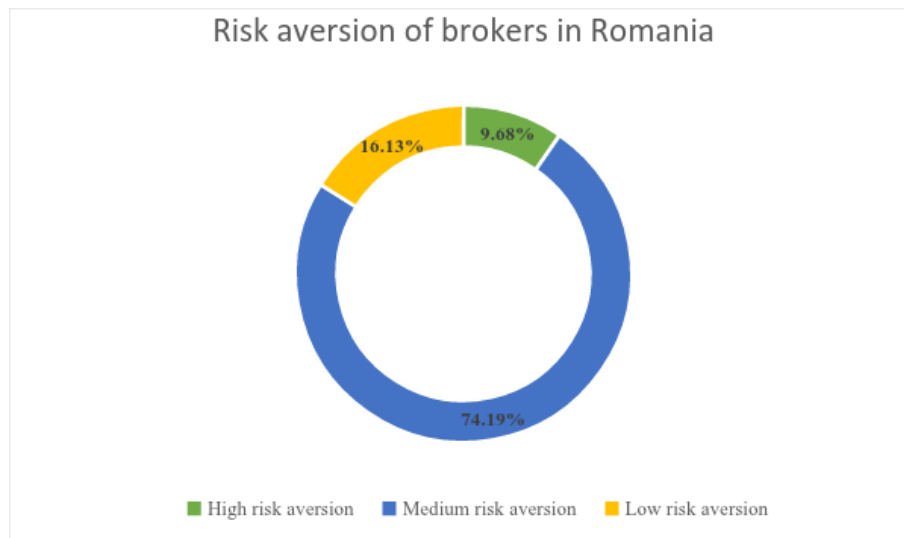
Not by chance we approached earlier appearance tied to speculators in the stock market. This due to the fact that the risk they assume it is a very important element that underpins investment decision making. When we talk about risk, automatically we think about the probability and possibility of its occurrence (Mionel, 2010, p. 203). Once these two dimensions included in the equation, we can say that the decision of investment becomes difficult to take but also to assume, and that the probability of occurrence and possible manifestation of a risk can be in many cases very difficult to quantify. Any broker quantifies the risk associated with a transaction on the stock exchange in accordance with a scale of risk assessment. Based on this assessment scales they will decide if an investment is risky or not for them and they could thus decide on taking the risk.

In literature we find the information according to which a broker will assume an additional risk as long as the returns it is greater than the one he can be obtain. Therefore, the notion of risk may be associated with the notion of potential win (Jacquillat & Solnik, 1997, p. 82).

It is important in this case, that each active broker to clearly establish the level of risk he can support for its transactions. In order to establish this level, he will consider first of all, his own attitude to risk and its own personality.

As shown in figure below, most brokers in the Romanian capital market exhibit a medium risk aversion (74,19% of them), 16,73% declare that they manifest an aversion to risk as low, and only a percent of 9,68% says that have a great aversion to risk. From the responses received from the brokers we found that each of them attaches a particular importance to the risk, however small it may be. From the responses I found that there is any broker for which the risk is not important in making an investment decision.

Figure 1. Risk aversion brokers Romanian capital market

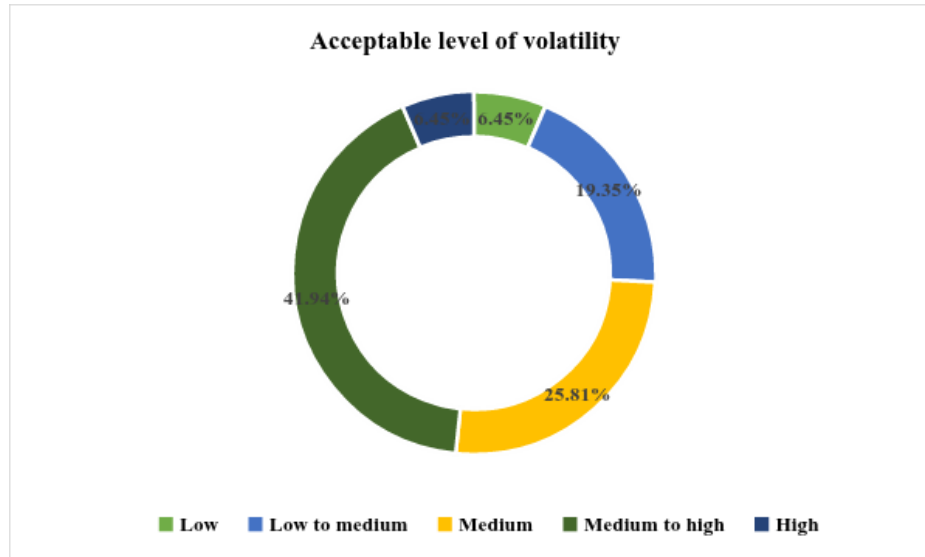


Source: own calculations

Brokers who declared that exhibit high risk aversion (9.68%) can be enrolled in the defensive category brokers, as Graham called them (Graham, 2010, p. 364). They frequently use methods of protection against risk and their investment preferences are represented by shares of growth. On the other side are brokers who say they exhibit low aversion to risk (16.13%) and their investment preferences are represented by financial instruments with high leverage. For the latter, the volatility of the market is nothing but the opportunity marking of earnings. Brokers with average aversion to risk (74.19%) have expectations according to general market developments.

Volatility in the broker's vision

Accepted volatility of financial markets must be analyzed in correlation with the level of risk accepted by brokers. Volatility level accepted by brokers in Romania can be highlighted using the following figure:

Figure 2. Volatility acceptable level to achieve the objectives

Source: own calculations

Following the results obtained as a result of the questionnaire, we found that 41.94% of brokers in Romania consider that a medium to high level of volatility in the market may be in line with their goals. A percentage of 25.81% of brokers believe that the average volatility in the market would be consistent with their investment objectives and 19.35% considered a low to medium level consistent with their objectives. Noteworthy in this case is 6.45% percentage of respondents who believe that low volatility in the market would bring greater benefits. Similarly, a rate of 6.45% of respondents believes that high volatility in the market would be beneficial for their actions investment.

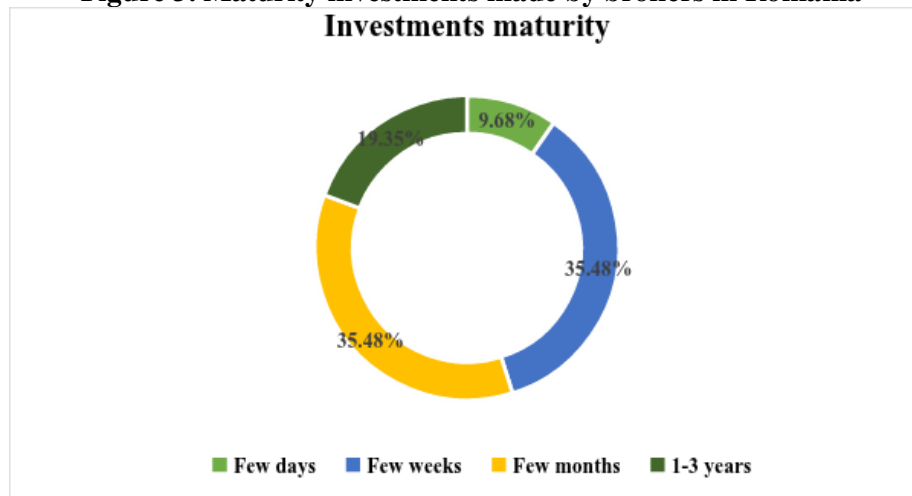
Based on the results presented so far, we can say that most brokers in the Romanian capital market show a certain penchant for speculative transactions, this mostly as a result of market volatility level that they deem to be consistent with their investment objectives.

Maturity investments

According to the results obtained from the questionnaire on the Romanian capital market of brokers, we can reconfirm the conclusion reached earlier regarding propensity to speculation brokers, if we look at things from the perspective of maturity investments. Most brokers in the Romanian capital market set their time horizon for their investments to several weeks (35.48% of them) or months (35.48% of them). Brokers who are considered highly

speculative set their time horizon of up to several days for their investments (9.68% of them). I believe that this percentage, almost 10% is slightly too high for a capital market at the beginning, as Romania. The effect of a massive presence of speculators participants in such a market can be a very powerful destabilizing factor for the entire market. So, from this point of view financial supervisory authority must be very careful to transactions entered into by these participants.

Figure 3. Maturity investments made by brokers in Romania

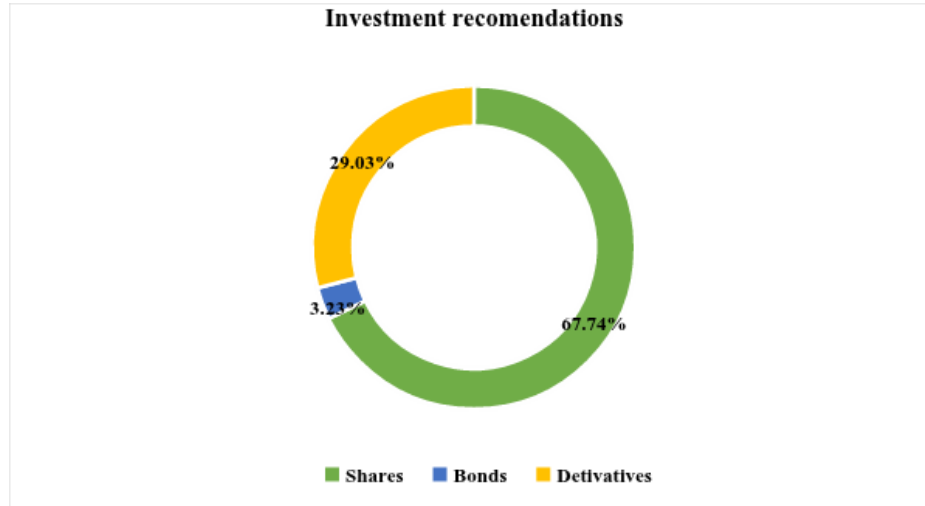


Brokers more conservative in a ratio of 19.35% report entering into transactions with a maturity between 1 and 3 years, so they are oriented on a longer term. None of the respondents said that brokers enter into transactions with a maturity of more than 3 years. This can be explained by the fact that the questionnaire was applied in early 2012, when the changing market trend was still obvious after several years of decline.

We therefore conclude that, at least in terms of the time horizon for which brokers in Romania conclude transactions, they have adapted to market needs and their customers.

Broker's investment recommendations

Regarding investment recommendations of the brokers from Romanian capital market, they are presented in the following figure:

Figure 4. Investment recommendations of the Romanian brokers

Source: own calculations

It can be seen from the previous figure that most of the brokers in the Romanian capital market (67.74%) often consider investments in shares. Somewhat paradoxically, they advised their clients to invest only in bonds at a rate of 3.23%, while 29.03% of them recommended investments in financial derivatives. Although worldwide, the percentage of the trades with financial derivatives is much higher, the percentage of 29.03% of brokers in Romania which recommends investments in such securities is quite good. This is especially true because the derivatives segment is still underdeveloped in Romania.

According to the results presented earlier, we may be tempted to invalidate the conclusion drawn earlier on the propensity to speculation brokers in Romania. There is however a sufficient explanation relevant confirming the hypothesis exposed earlier. In Romania, the spot market is still clearly more developed than the future market, which is why they recommend their clients investments in shares. Perhaps less surprising is in this case, that no respondent said that recommends investing in mutual funds, bank deposits or real estate.

The 29.03% of brokers who say that recommend investments in financial derivatives, reconfirms the earlier hypothesis namely propensity towards speculation of the brokers in Romania.

Conclusions

Regarding hypothesis launched in the beginning of this article, we can say that based on the responses obtained from the authorized brokers in the capital market from Romania, it is confirmed. So, generally speaking, a broker in Romania can be characterized by the following lines profile:

- He has an average aversion to risk.
- A medium to high level of volatility in the market could satisfy its investment objectives.
- Most initiated transactions have a maturity of a few weeks, at most a few months.
- Most often recommends investments in shares, but also recommends investments in financial derivatives, but rarely recommends investments in fixed income instruments.

We note again that these profile lines were made on the basis of the questionnaire applied in 2012, so responses were influenced by the state of brokers and their perception vis-à-vis the market at that time. A more complete picture regarding the investment behavior of market brokers can be made after the application of a new questionnaire at the beginning of 2015, so their answers can show off their attitude in terms of an upward trend in the market.

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