

Individual preference towards risk (extract from a multi-stage survey on investment intelligence)

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The individual preference towards risk is a fundamental concept in economics, and especially in the general field of investment choice. A number of scholars in the area have studied the phenomenon and since they have used various sets of assumptions and various experiment designs, they have reached different conclusions with “rational risk-averse investor” emerging as the ruling paradigm. A somewhat contradictory paradigm is the so called “prospect theory” developed by Kahneman and Tversky. They have designed and conducted numerous experiments on individual choice which could be interpreted that either the essence of the human being is encoded with irrationality/non-rationality or at least that the concept of “rational investor” should be reviewed and widened. The tricky part of changing a paradigm in social science is that no experiment or survey can be conclusive and indisputable enough.

The paper analyzes some of the results from a survey recently conducted by the author among Bulgarian investment professionals. Some of the questions of the survey inquired about individual preference towards risk by pointing out simple choices in a series of fair games of chance. The experiment is based on known exercises but it is designed entirely from scratch. To the best of the author’s knowledge it is a first for Bulgaria. Important remark is that the respondents are counted as experts (with unknown general population) so judgmental sampling is used. To tackle the unwanted effects of the sampling technique the data resulted from, some of the questions are processed similarly to Delphi approach. Additionally a similar but shorter control experiment is conducted with randomly sampled non-experts. The collected data show some properties as suggested by the prospect theory. It is reasonable (but likely not rationally) to speculate that the risk related behaviour of the experts would not be as expected by the current popular paradigm in investment sciences. Several special regions of interest (in the risk-investment space) are additionally surveyed so that a better picture of professional investor behaviour could be sketched.

Keywords: Individual risk preference, Kahneman & Tversky Prospect theory, Game of chance, St. Petersburg paradox, Expert opinion survey, Delphi approach