ABSTRACT

This study draws on early research about the implication of regulatory orientation in the context of investment decision-making, and explores how different individual investment patterns can be best captured through objective financial indices. After drawing a sample (N = 213, 49.8% male, 18-year-old or above) from Hong Kong, this study first examined the regulatory orientation of all participants using the Regulatory Focus Questionnaire (Higgins et al., 2001). Based on the result, participants were categorized as either promotion-focused (109 participants) or prevention-focused (104 participants).

The study then examined the relationship between the regulatory orientations of the participants and their investment preferences. Two economic indices (i.e., the Sharpe ratio and the D-Index) were manipulated to produce four graphs, each represents the performance of a different investment portfolio over the past 12 months. The results showed that (i) when two investment portfolios have the same Sharpe ratio and the end-of-period return, the portfolio with a lower ex-post D-Index value were favored, regardless of the regulatory orientations of the investors, and (ii) when two investment portfolios have the same D-Index value, promotion-focused investors favored the portfolio that has a higher end-of-period return, even though it is more volatile, and prevention-focused investors favored the portfolio that is more stable, even though it has a relatively lower end-of-period return. External factors, such as global economic conditions and the length of the investment period, have a significantly larger impact on the prevention-focused investors than the promotion-focused investors.

Finally, results also indicated that promotion-focused investors are more likely to dispose an investment early if they believe the portfolio does not have a good potential for future growth, while prevention-focused investors tend to sell early if the accumulated net profit is above their

initial investment amount. Prevention-focused investors would also dispose an investment if they do not believe the value of the portfolio will ever return to the break-even point.

These findings suggest that both the objective performance of investment products and the subjective psychological experiences of investors are important in investment decision-making process. Using the Sharpe ratio and the D-Index side-by-side can help financial practitioners to identify the most suitable investment products for their clients with different regulatory orientations.

Keywords: regulatory orientation; regulatory fit; coping strategies and tactics; investment decision-making; Sharpe ratio; D-Index