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Impact on Herd Behaviour and FOMO on Retail Investor Decision Making in Stock Markets: A Behavioural Finance Perspective

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ABSTRACT: The stock market has long been influenced by psychological forces that extend beyond rational financial analysis. This study examines the profound impact of herd behaviour and Fear of Missing Out (FOMO) on retail investor decision-making in equity markets. Retail investors, often lacking institutional resources and expertise, are disproportionately susceptible to cognitive biases that drive irrational investment choices. Herd behaviour compels individuals to mirror the trading actions of the majority, abandoning independent judgment in favour of collective sentiment. Simultaneously, FOMO accelerates impulsive investment decisions, particularly during bull markets and speculative asset rallies. Together, these phenomena contribute to asset price bubbles, heightened market volatility, and significant financial losses among retail participants. Drawing on behavioural finance theory, this paper analyses the psychological mechanisms, socioeconomic triggers, and digital amplifiers — including social media and online trading platforms — that intensify these biases. Recommendations are proposed to foster financial literacy and encourage disciplined, evidence-based investment practices.

KEYWORDS: Herd Behaviour, Fear of Missing out(FOMO), Behavioural Finance, Investment Decision-Making, Investor Psychology, Social Media Influence, Stock Market Sentiment.

I. INTRODUCTION

The financial markets have historically been perceived as arenas governed by logic, data, and rational economic decision-making. Classical financial theories, such as the Efficient Market Hypothesis (EMH), long assumed that investors act as rational agents who process all available information objectively to maximize returns. However, decades of empirical research and real-world market events have consistently challenged this assumption, revealing that human psychology plays an equally — if not more — decisive role in shaping investment behaviour. In this context, behavioural finance has emerged as a critical discipline that bridges the gap between economic theory and psychological reality.

Among the many psychological phenomena that influence financial markets, herd behaviour and Fear of Missing Out (FOMO) stand out as two of the most pervasive and consequential forces affecting retail investor decision-making. Retail investors — individuals who invest personal funds in equity markets without the backing of institutional infrastructure, professional research teams, or algorithmic tools — are particularly vulnerable to these behavioural biases. Unlike institutional investors who operate within structured risk management frameworks, retail participants often rely on social cues, market sentiment, and emotional impulses when making investment choices.

Herd behaviour refers to the tendency of individuals to mimic the financial decisions of a larger group, often disregarding their own independent analysis. This phenomenon is deeply rooted in human evolutionary psychology, where following the crowd was associated with safety and survival. In the context of financial markets, however, this instinct can prove catastrophically counterproductive. When a large number of retail investors collectively buy or sell a particular stock based on popular sentiment rather than fundamental value, it creates artificial price movements that distort market efficiency and increase systemic risk. Historical events such as the dot-com bubble of the late 1990s and



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the GameStop short squeeze of 2021 serve as powerful illustrations of how herd mentality can drive asset prices to unsustainable levels before triggering sharp corrections.

FOMO, on the other hand, is a distinctly modern psychological trigger that has been significantly amplified by the rise of digital technology and social media platforms. When retail investors observe peers or online communities celebrating extraordinary gains from a particular stock, cryptocurrency, or investment trend, an overwhelming anxiety of being left behind takes hold. This fear overrides rational risk assessment and pushes investors toward impulsive, poorly researched investment decisions. The rapid dissemination of financial information — and misinformation — across platforms such as Reddit, Twitter, YouTube, and Instagram has created an environment where FOMO-driven investing is not just common but normalized.

The intersection of herd behaviour and FOMO creates a compounding effect on market dynamics. Together, they fuel speculative bubbles, encourage momentum-based trading, and expose retail investors to disproportionate financial losses. In an era where commission-free trading apps have democratized market access, millions of first-time investors enter the market emotionally charged and informationally underprepared, making them especially susceptible to these biases.

This paper seeks to investigate the nature, triggers, and consequences of herd behaviour and FOMO on retail investor decision-making, while also exploring how financial literacy and regulatory awareness can serve as meaningful countermeasures in building a more informed and resilient retail investing community.

II. REVIEW OF LITERATURE

1. Behavioural Finance and Investor Psychology

The foundation of behavioural finance was established by Kahneman and Tversky (1979) through Prospect Theory, which demonstrated that individuals make financial decisions based on perceived gains and losses rather than objective probabilities. Thaler (1985) further introduced mental accounting, arguing that investors treat money differently depending on its psychological context. These studies established that cognitive biases are systematic patterns deeply embedded in human financial behaviour, laying the groundwork for understanding herd behaviour and FOMO in modern stock markets.

2. Herd Behaviour in Financial Markets

Bikhchandani, Hirshleifer, and Welch (1992) introduced informational cascades, explaining how rational individuals ignore private information and follow crowd actions when they believe the majority possesses superior knowledge. Christie and Huang (1995) found that retail investors increasingly suppress independent beliefs and conform to market consensus during high-volatility episodes. Nofsinger and Sias (1999) further established that retail investors are more susceptible to following price trends without conducting independent fundamental analysis compared to institutional counterparts.

3. FOMO and Investment Decisions

Przybylski et al. (2013) formally defined FOMO as a pervasive apprehension that others are having rewarding experiences from which one is absent. Baker and Wurgler (2007) demonstrated that emotional states significantly influence market pricing among retail participants. Lerner et al. (2015) argued that emotions such as anxiety and excitement systematically alter risk perception and financial decision-making, connecting FOMO explicitly to overtrading, speculative purchases, and reduced portfolio diversification.

4. Social Media as an Amplifier

Bollen, Mao, and Zeng (2011) demonstrated that social media sentiment has a measurable predictive relationship with stock market movements. The Reddit-driven GameStop phenomenon of 2021 became a landmark case study in social media-induced herding, where coordinated retail investor activity fuelled by FOMO caused extraordinary short-term price distortions. Antweiler and Frank (2004) similarly found that online discussion significantly influences stock trading volume and short-term price volatility.



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5. Retail Investor Vulnerability

Barber and Odean (2000) established that excessive trading among retail investors leads to significantly below-average returns, largely attributable to emotional decision-making. Kumar and Lee (2006) identified correlated trading patterns among retail investors, suggesting shared behavioural biases create systematic price distortions in equity markets. These findings underscore the disproportionate influence of psychological factors on retail investor outcomes.

6. Market Bubbles and Collective Irrationality

Shiller (2000) argued that speculative bubbles are fundamentally driven by social contagion — the spread of investment narratives through social networks rather than rational valuation. Kindleberger and Aliber (2005) identified herd behaviour as the central mechanism behind every major market bubble. Corbet et al. (2018) extended these arguments to cryptocurrency markets, documenting intense herding and FOMO-driven price cycles among retail participants.

7. Financial Literacy as a Moderating Factor

Lusardi and Mitchell (2014) found a strong positive correlation between financial literacy and reduced susceptibility to financial fraud and impulsive investing. Aren and Zengin (2016) specifically found that investors with higher financial knowledge are significantly less likely to follow crowd-based investment strategies, suggesting that financial education serves as an effective intervention against herd behaviour and FOMO.

Research Gap

While existing literature has examined herd behaviour and FOMO independently, limited research explores their combined impact on retail investors within digitally connected, app-based trading environments. This paper aims to address this gap by examining the compounding effect of both phenomena in shaping retail investment behaviour in contemporary stock markets.

III. OBJECTIVES OF THE STUDY

1. To examine the nature and extent of herd behaviour among retail investors and its influence on their stock market investment decisions.
2. To analyse the role of Fear of Missing Out (FOMO) in driving impulsive and emotionally charged investment choices among retail market participants.
3. To assess the combined impact of herd behaviour and FOMO on market volatility, asset price bubbles, and overall stock market stability.
4. To investigate the influence of social media platforms and digital trading applications in amplifying herd behaviour and FOMO among retail investors.
5. To explore the moderating role of financial literacy in reducing the adverse effects of herd behaviour and FOMO on retail investor decision-making and investment outcomes.

IV. RESEARCH METHODOLOGY

4.1 Research Design

The study employs a descriptive research design with a quantitative methodology. This approach is appropriate for characterizing consumer attitudes, attention behaviors, and marketing response patterns, providing a structured basis for hypothesis testing and statistical inference. The research follows a cross-sectional design, collecting data from respondents at a single point in time to capture current behavioral patterns rather than longitudinal changes.

4.2 Sample and Data Collection

This study targets retail investors who actively participate in stock market trading through online platforms and mobile applications. A purposive sampling technique is adopted to ensure only experienced retail investors with a minimum of one year of market participation are included in the study. A sample size of 100 retail investors is selected, which is statistically adequate and consistent with comparable behavioural finance research. Primary data is collected through a structured questionnaire administered via Google Forms, distributed across investment communities, social media platforms, and online trading forums. The questionnaire employs a 5-point Likert Scale to measure respondents' perceptions of herd behaviour, FOMO, and social media influence on their investment decisions. Secondary data is



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gathered from published academic journals, research papers, and financial databases including Google Scholar, JSTOR, and SSRN.

4.3 Analytical Tools

Data analysis employed four complementary statistical techniques: (1) Percentage Analysis for descriptive profiling of the sample; (2) Likert Scale Analysis to measure respondents' agreement levels toward attention-related statements; (3) Regression Analysis and (4) ANOVA to test differences between group mean responses across various demographic segments. All analyses were conducted using SPSS.

V. ANALYSIS AND FINDINGS

4.1 Demographic Profile of Respondents

The demographic analysis reveals that the study is predominantly represented by young investors between 18 and 22 years of age. The majority of respondents (62.1%) belong to the 20–22 age group, followed by 34% aged 18 years. Gender distribution is nearly equal, with females accounting for 50.5% and males 49.5%, ensuring balanced representation. Regarding current status, 95.1% of respondents are students, reflecting the growing interest of young individuals in stock market participation. Investment experience analysis further confirms that 85.4% of respondents are beginners, suggesting that the study primarily captures the behaviour of new and inexperienced investors who are more susceptible to behavioural biases such as herd behaviour and FOMO. Social media emerged as the dominant source of investment information, used by 58.3% of respondents, followed by friends and peers at 27.2%, highlighting the significant role of digital platforms in shaping investment awareness among young investors.

4.2 Herd Behaviour Among Retail Investors

The analysis of herd behaviour reveals that while a majority of respondents maintain a neutral stance, certain behavioural tendencies are evident among a notable portion of participants. Approximately 45.6% of respondents agreed or strongly agreed that they feel safer investing when people of their age group invest in the same stock, indicating the presence of peer-driven investment behaviour. Rising stock prices were identified as a key trigger, with 37.8% of respondents agreeing that they invest quickly when a stock price is rising sharply. Social media profit screenshots were found to moderately influence investment urges among beginners. However, a considerable portion of respondents disagreed with selling stocks simply because others in their age group are selling, suggesting that herd behaviour in selling decisions is comparatively weaker than in buying decisions. Overall, herd behaviour exists among retail investors but is not overwhelmingly dominant, reflecting that investors attempt to exercise independent judgment while still being partially influenced by crowd actions.

4.3 FOMO and Emotional Investment Behaviour

The analysis of FOMO-related statements indicates that emotional factors play a moderate but meaningful role in retail investor decision-making. Around 37.9% of respondents agreed that they fear missing opportunities if they do not act immediately, while 32.1% agreed that they have invested in a stock without proper analysis due to FOMO. A significant 40.7% of respondents remained neutral regarding whether their decisions are influenced more by emotions than fundamentals, suggesting uncertainty rather than outright denial. The regression analysis for emotional investment decisions produced a statistically significant F-value of 6.241 with a p-value of 0.00063, confirming that psychological factors including fear of missing opportunities, stress from others' profits, and reliance on market sentiment collectively and significantly influence emotion-driven investment decisions. These findings confirm that FOMO is an active psychological force shaping retail investor behaviour, particularly among student investors with limited market experience.

4.4 ANOVA and Regression Analysis Results

The ANOVA analysis revealed statistically significant differences in investment behaviour across different levels of investment experience. For the tendency to buy trending stocks, the F-value was 4.756 with a p-value of 0.002, leading to the rejection of the null hypothesis and confirming that investment experience significantly influences trend-following behaviour. Respondents with 6 months to 1 year of experience showed the highest tendency to buy trending stocks (mean = 4.00), while those with 1–3 years of experience were least likely to do so (mean = 1.67). Similarly, for social media profit screenshot influence, the F-value was 3.296 with a p-value of 0.014, confirming significant variation across experience groups. The regression model for herd selling behaviour was also statistically significant (F = 4.673, p = 0.0017), confirming that difficulty holding investments, reliance on market sentiment, and fear of missing



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opportunities collectively drive herd selling decisions. However, the regression model for trend-following behaviour returned a non-significant result ($F = 0.678$, $p = 0.608$), indicating that FOMO-related variables alone do not sufficiently explain regret-driven trend-following investment behaviour.

VI. DISCUSSION

The study reveals that the majority of respondents are young student investors with beginner-level experience, indicating that findings primarily reflect the behavioural patterns of inexperienced market participants. Social media emerged as the most dominant source of investment information at 58.25%, confirming that digital platforms centrally shape investment awareness among young investors. While many respondents maintained neutral attitudes, a notable proportion acknowledged that rising stock prices and social media profit posts increase their urge to invest. FOMO was found to moderately influence investment decisions among less experienced investors, with emotional factors such as fear of missing opportunities and stress from peers' profits affecting their overall decision-making behaviour.

Young investors should prioritise fundamental analysis and develop disciplined long-term investment strategies rather than reacting impulsively to social media trends or short-term market movements. Educational institutions should introduce structured financial literacy programmes to equip students with the analytical tools necessary for rational investment decision-making. Regulatory authorities should promote responsible financial content on social media to prevent misleading investment advice that fuels herd behaviour and FOMO. Beginner investors should seek guidance from certified financial advisors and consciously avoid making decisions based purely on peer influence or social comparison.

This study confirms that while many retail investors attempt to exercise independent judgment, behavioural biases driven by social influence, emotional reactions, and digital media exposure meaningfully affect investment choices. Investment experience was found to play a more significant role than gender in shaping behavioural patterns, with less experienced investors being more susceptible to trend-following and peer-driven decision-making. Social media's dominant influence further amplifies these biases, normalising impulsive and emotionally charged investment decisions among young retail investors. Overall, improving financial literacy and investment awareness among young investors remains the most effective strategy for reducing the adverse impact of herd behaviour and FOMO on retail investment outcomes.

Future research could expand the sample beyond students to include diverse retail investors across different age groups, income levels, and geographic regions to enhance generalizability. Longitudinal studies tracking investor behaviour over time would provide deeper understanding of how herd behaviour and FOMO evolve with growing market experience. Qualitative methods such as in-depth interviews and focus group discussions could further uncover the underlying psychological motivations driving behavioural biases in retail stock market investment decisions.

VII. CONCLUSION

This study examined the impact of herd behaviour and Fear of Missing Out (FOMO) on retail investor decision-making in the stock market. The findings confirm that behavioural biases driven by social influence, emotional reactions, and digital media exposure meaningfully affect the investment choices of retail participants, particularly among young and inexperienced investors. While many respondents demonstrated a tendency to maintain neutral stances, a considerable proportion acknowledged being influenced by peer behaviour, rising stock prices, and social media profit content when making investment decisions.

The statistical analyses further established that investment experience plays a significant role in determining the extent to which investors are susceptible to herd behaviour and FOMO. Less experienced investors were found to be more vulnerable to trend-following behaviour and emotionally driven decision-making, while moderate experience appeared to foster greater analytical discipline and independence. Social media emerged as the single most influential source of investment information among respondents, reinforcing its powerful role in amplifying behavioural biases within modern retail investing environments.

These findings are strongly aligned with the principles of Behavioural Finance, which recognize that psychological and emotional factors systematically influence financial decision-making beyond the boundaries of rational economic



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theory. The study ultimately concludes that enhancing financial literacy, promoting analytical thinking, and encouraging responsible consumption of financial information on digital platforms are essential steps toward reducing the adverse impact of herd behaviour and FOMO on retail investor outcomes. Building a generation of informed, disciplined, and emotionally aware investors remains the most sustainable pathway to greater stability and rationality in stock market participation.

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