

Ruin and Discipline: How Behavioural Finance Explains India's Investing Paradox

Why the Same Mind that Loses ₹1 Lakh Crore in F&O Builds ₹32,000 Crore a Month in SIPs



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Two numbers from the same market, in the same year, drawn from the same population of investors, tell contradictory stories. The first: in a study of the equity derivatives segment released in July 2025, SEBI found that the net losses of individual traders in futures and options had widened to about ₹1.06 lakh crore in 2024-25 and more than nine in ten traders, roughly 91 per cent, ended the year in the red. This was not a one-off. An earlier SEBI study, covering the three years from 2021-22 to 2023-24, had already put cumulative individual F&O losses above ₹1.8 lakh crore, with barely one per cent of traders earning a profit greater than ₹1 lakh after costs. More than three-quarters of those who lose money keep trading anyway. The regulator's curbs have slowed the activity but not the bleeding: with equity indices falling through 2025-26 and trading still skewed toward options, there is little reason to think the losses eased much in the year just ended. The second: monthly contributions through systematic investment plans, or SIPs, crossed ₹32,000 crore in early 2026, powered by close to ten crore SIP accounts and an investor base past 27 crore folios. Where the F&O figure is wealth destruction, the SIP figure is the opposite: disciplined wealth creation, and very likely the most successful savings habit the Indian financial system has cultivated.

Here is the puzzle - these are not two different species of investor. They are drawn from the same population. The mind that loses money in one channel and builds it in the other is, very often, the same mind. The comfortable reading is that this is simply rationality versus recklessness, the prudent investor's SIP set against the gambler's option trade. That reading is shallow. Neither the F&O trader nor the SIP investor is the cool, calculating *homo economicus* of the textbooks. Both are driven by behavioural biases. The difference is not that one is rational and the other irrational. It is that one environment switches on a cluster of biases that compound toward ruin, while the other switches on a cluster that compounds toward wealth. What decides which instincts fire, and whether they enrich or strip you, is the architecture into which the psychology is poured. In the same India, the two architectures, a casino and a compounding machine, are pointed at the same crore-strong stream of investors. It is indeed a striking experiment in behavioural finance in the world today.

The Casino

Begin with the machine that sucks money. The F&O numbers are not an Indian anomaly. They are an Indian instance of a pattern that behavioural finance documented decades ago. Brad Barber and Terrance Odean, in their landmark study published in *The Journal of Finance* in 2000, titled "Trading Is Hazardous to Your Wealth," found that the most active fifth of investors underperformed the market by about 6.5 percentage points a year. Their later work with Yi-Tsung Lee and Yu-Jane Liu on the entire Taiwanese day-trading population from 1992 to 2006 reached a verdict that reads like a prophecy of India's data: fewer than one per cent of day traders could reliably earn positive returns net of fees, and the losses persisted, year after year, in the same people.

Why do rational adults keep doing this? The first, and perhaps the most explanatory for index-option buying, is the mishandling of probability, what Kahneman and Tversky's prospect theory calls the overweighting of small chances. People systematically overvalue tiny probabilities of large payoffs; it is the same wiring that sells lottery tickets. A cheap, far-out-of-the-money weekly option is a lottery ticket dressed in the language of finance: it has a high probability to expire worthless, but the slim chance of a large multiplier is overweighted by the buyer. Nicholas Barberis's "A Model of Casino Gambling" (2012) explains why that thrill keeps players at the table long past the point of rational exit. The individual option buyer seems to sit in exactly that seat.

The second is overconfidence. Barber and Odean's 2001 paper, memorably titled "Boys Will Be Boys," showed that the more confident investors are in their own skill, the more they trade, and the more they trade, the less they earn. Every winning F&O trade feels like vindicated skill. Every loss feels like bad luck or a near miss.

The third is the illusion of control, described by Ellen Langer in 1975, our tendency to believe we can steer outcomes that are largely random. The charts, the alerts, the one-tap order and the gamified frictionlessness of the trading app manufacture a feeling of mastery.

The fourth is the disposition effect. Odean's 1998 study documented investors' deep reluctance to realise losses. The pain of booking a loss, which per Kahneman and Tversky is roughly about twice as large as the pleasure of an equivalent gain, drives traders to hold losers and double down to "get even". SEBI's finding that over three-quarters of loss-makers keep trading despite consecutive years of losses is this reluctance written across a crore of accounts.

Binding all of these together is the herd mentality, amplified by survivorship and availability bias. Index-option volumes exploded partly because trading became a social, viral activity, fuelled by Telegram tip-groups and influencer reels in which the visible winners, floated to the top of every feed, makes it look like easy moany. SEBI's data lays the

transfer bare. In 2023-24, foreign portfolio investors and proprietary traders made profits of ₹28,000 crore and ₹33,000 crore respectively, the overwhelming majority through algorithms, while individuals supplied the losses. On a casino floor the house always wins. Here, the house wears the clothes of an algorithm.

The Compounding Machine

Now the machine built to make you money. The SIP is, at heart, a piece of behavioural engineering, a textbook application of the ideas that won Richard Thaler the Nobel Prize in 2017. Its genius is that it does not ask the investor to be rational. It asks for one decision, once, and then nothing.

The first instinct it enlists is inertia, or status quo bias. Brigitte Madrian and Dennis Shea's celebrated 2001 study, "The Power of Suggestion," showed that simply switching a retirement plan's default from opt-in to opt-out lifted participation from well under half of employees to above four-fifths. The behaviour did not change. The default did. The SIP performs the same trick. Once the standing instruction is set, doing nothing is the act of investing. The investor's natural laziness, ruinous at the casino, becomes the engine of accumulation.

The second is the self-control problem, and the SIP's answer to it, the commitment device. Thaler and Hersh Shefrin's "economic theory of self-control" (1981) models each of us as a far-sighted "planner" at war with a myopic "doer" who wants to spend now. Left to fight that war afresh every month, most people lose. The SIP lets the planner win in advance, pre-committing the doer through automation, so the impulsive present self never gets a monthly vote. Thaler and Shlomo Benartzi's "Save More Tomorrow" programme (2004) made the same principle explicit by channelling future pay raises into saving, lifting participants' savings rates from around 3.5 per cent to over 13 per cent within a few years. The SIP is "Save More Tomorrow" with an auto-debit.

The third is mental accounting, Thaler's insight that we treat money differently depending on the bucket we file it in. The SIP corpus, ring-fenced as a long-term, almost untouchable "investment," is protected from the everyday raids that deplete a general savings balance.

The fourth is the benign use of narrow framing. A lump-sum decision to invest ₹60,000 feels weighty and fraught. A monthly debit of ₹5,000 feels almost painless. By slicing the commitment into small, recurring bites that the mind evaluates one at a time, the SIP turns our habit of judging the small sum rather than the large annual total to the investor's advantage.

The fifth is the neutralising of regret aversion. Much of what paralyses the lump-sum investor is the fear of buying at the wrong moment. By spreading purchases mechanically across time, rupee-cost averaging removes the timing decision altogether, and with it the regret that keeps anxious money sitting idle. The SIP is, among other things, a regret-minimisation machine.

Around all of these plays a milder optimism, faith in India's long-run growth story that keeps investors buying equity. There is a constructive herd at work too. "Everyone my age has an SIP" is social proof at national scale, and the "Mutual Funds Sahi Hai" campaign was an effective attempt to move a generation toward a good habit. AMFI's record of relentless monthly inflows, sustained even through bouts of sharp foreign selling, is the signature of a herd moving, for once, toward the machine that compounds rather than the one that consumes.

The Regulator's Two Hands

The same regulator is working both machines at once. With one hand, SEBI is shrinking the casino. Since October 2024 it has tightened the screws with fewer weekly expiries, larger contract sizes, upfront collection of option premiums and intraday monitoring of position limits. The early results are visible: the number of unique F&O traders fell sharply, from 61.4 lakh in the first quarter of 2024-25 to 42.7 lakh in the fourth, with overall participation down about 20 per cent year on year. This is necessary work, grounded in SEBI's own transaction-level evidence.

With the other hand, SEBI is trying to feed the compounding machine. In May 2026 it floated a proposal to let employers deduct a portion of an employee's salary and route it directly into mutual fund units on the employee's behalf, with consent. Read against the behavioural logic of the SIP, this is no small administrative tweak. It takes the commitment device that already makes the SIP work, the automation that lets the far-sighted planner overrule the impulsive doer, and hard-wires it one step earlier, into the payslip itself. It is "Save More Tomorrow" written into the salary structure.

Put the two hands together and a strategy comes into focus. We cannot legislate away the appetite for risk; it is human nature, and human nature does not respond to circulars. What a regulator can do is make the destructive machine harder to reach and the constructive one harder to avoid: raise the cost and friction of the casino, lower them for the compounding machine. The aim is not to make Indian investors rational, as that may be futile ambition, but to engineer the environments their biases flow into. Call it behavioural judo: the regulator is trying to ensure that the same person, with the same instincts, meets the right machine more often than the wrong one.

The gambler and the saver are the same person. Only the machine is different, and the machine is something we choose to build.