Investment Decision Making of Institutional Investor: What is Behind It?

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Abstract: **The purpose of this study is to analyze the relationship between financial behavior and investment decisions of institutional investors in Batam City. The importance of financial behavior and uncertainty of capital market information enables investors to use the obtained information for more significant result investment, but there are different situations to achieve the result. The study collected feedback from 80 investors from Insurance, Banking, Finance, and Securities companies using targeted sampling techniques. Data analysis used partial least squares structural equation model (PLS-SEM) by testing the inner and outer model. The result showed that financial tools and firm-level corporate governance have a significant positive effect on investment decisions. It allows financial instruments to make investment decisions through fundamental analysis, and firms with corporate governance levels can provide value to shareholders. Capital markets always reflect information and may have a positive or negative impact. The result also found that heuristic and risk a version do not affect investment decisions. It concluded that respondents tended to take rational actions when evaluating information and were not risk-averse investors.**

Keywords: **investment decision, financial behavior, institutional investor, corporate governance, financial tools**

I. INTRODUCTION

The capital market is one element of a country's economic growth. The role of community and government in the capital market is an element that provides a source of funding for national development. The analogy of a capital market is the same as that of other markets, where supply and demand activities occur between buyers and sellers. The event intended by the seller in the capital market is the securities offered by the issuer to investors so that the buying and selling of shares take place. Investors who invest in the capital market tend to wait a long time and expect large profits. One way for issuers to find sources of funds in the capital market is to be list on the stock exchange by issuing shares and bonds offered to the public.

Various investment methods have become popular, and investors make decisions about choosing different investments. Economic theory shows that investors are rational and make decisions by assessing all available information. As time passes, it becomes difficult for investors to make investment decisions since they need to consider different components before making a decision. In the past, investors had limited information, and they made decisions based on some data, which was promptly accessible, but with advances in technology, investors had to deal with much information to make decisions (Qasim, Hussain, Mehboob, & Arshad, 2019).

Institutional investors have a large portion of supporting the growth of the Indonesian capital market. The existence of institutional investors is very dominant in enlivening trade transactions on the Indonesia Stock Exchange (IDX), which in turn becomes a representation of the progress of the national economy. As of the end of March 2015, the percentage of ownership of institutional investor assets on the IDX reached 73.14%. A conscious movement in the capital market, especially the stock market, is often a benchmark for retail investors to invest in. The participation of institutional investors in the capital market is safeguarded and even increased by continuing to increase confidence in the capital market.

Direct connection with the issuer's executives is a form of openness and transparency of the highest quality information desired by investors. Direct communication allows investors to explore various work plans and target issuers in the future as a real preference in making investment decisions. Issuers must have direct communication because it is beneficial to open full access and relationships with investors to gain higher trust in increasing the value of the company. The movement of transaction volume and value is one measure of how investors behave in making both short and long term decisions (IDX, 2018).

Investors usually make many different decisions and prioritize the choice, which would maximize returns. Investors also consider the techniques for the right timing to enter the market. Conversely, some investors prefer to avoid risk if the stock has a high level of risk, and other investors also tend to bear the high risk with some diversification to control unsystematic risk (Areiqat, Abu-rumman, Al-alani, & Alhorani, 2019).

In the research of Mumtaz, Saeed, and Ramzan (2018), heuristic factors, financial tools, risk aversion, firm-level of corporate governance, and day to day experience have a positive impact on investment decision making. Institutional investors always buy and sell equity in large amounts of money. The development of the capital market is presently getting more volatile and unstable. The impact of volatility and instability on the stock market would increment investment risk. Stock market fluctuations continuously remain a concern of institutional investors and also catch the attention of professionals. Most investors make mistakes in investing because of psychological and behavioral biases. Institutional investors who are also as a company have a better understanding of governance, which is vital for investment decision making. The implementation of bad governance will not provide value to investors.

Potential institutional investors are also targets of the market. Currently, large institutions such as pension funds considered to be still low in the portion in stock portfolios; this constrained by investment strategies that are related to performance measurement. IDX is active in providing education that expected to increase investment in shares to 20% of the total investment allocation, while currently, the average is only 11% (CNBC, 2019).

II. LITERATURE REVIEW AND CONCEPTUAL FRAMEWORK

The main problem of investment decision making is challenging to make a choice. Investors must have wise analytical skills in making investment decisions. Most investors have analytical skills, but they do not have underlying reasons for ensuring an investment decision (Farooq, Afzal, Sohail, & Sajid, 2015). According to Qureshi, Rehman, and Hunjra (2012), traditional financial theories assume that investors use all information and make rational investment decisions, but it does not happen in reality according to the increasing importance of financial behavior. Mumtaz *et al*. (2018) illustrate that the right investment decision has a positive impact on firm-level results, such as the company's financial performance. The right choice based on investments that contained information collected by investors from various sources, such as the internet, television, and even other media, to increase the company's profitability. Investment decisions can adversely affect the performance of an organization or institution. Investments that have clear goals with wise investors in the decision have the potential to obtain the expectations that have set.

In the heuristic approach, investors and financial analysts accelerate investment analysis and decisions. Heuristic guidelines for poor decision making are based on limited data references and are easy to obtain. Heuristics also refers to rules of thumb, which make decision making easier through reference to information sets and peculiarities that are easily obtainable (Nayak & Kumar, 2020). Heuristics theory reported biases, including representation, overconfidence, anchoring, gambler’s fallacy, and availability significantly affected investment decisions (Keswani, Dhingra, & Wadhwa, 2019).

Mumtaz *et al*. (2018) reported that heuristic has a positive impact on investment decision making. In a complex situation and uncertainty condition, investors tend to use practical methods to make decisions. Investor assesses information that is available objectively in a limited of time and which is useful for applying in the investment decision-making process. The same results also showed in research by Rehan and Umer (2017) and Qureshi *et al*. (2012).

H_1: The higher level of heuristic improve how the way institutional investor in making their investment decision

Risk aversion is the desire of individuals to avoid uncertainty and affects investment decisions. Risk avoidance negatively influences investors' trading activities and the size of their portfolios. It affects investor wealth by generally making bad decisions. Individuals are rational, reluctant to take risks and attempt to maximize wealth under challenging alternatives. Investors are irrational and inconsistent in risky decisions. Investors feel the risk after determining it, then look for opportunities, and change aversion in different situations. Investors tend to be unstable towards risk aversion in financial decision making (Farooq *et al*., 2015).

Mumtaz *et al*. (2018) found that risk aversion has a positive effect on investment decision making. Investors tend to be rational, avoid risk, and make investment decisions that increase profits. Investors will have a risk-averse tendency if they have the certainty to get profits. When investors are confident about the expected rate of return, investors will tend to become risk-averse. The result of the study is the same as research by Qureshi *et al*. (2012).

H_2: Risk-averse institutional investor would be better in making an investment decision

According to Mumtaz *et al*. (2018), financial tools have a positive effect on investment decisions. Financial tools determine the capital asset pricing model, portfolio management, portfolio diversification, technical and fundamental analysis, which have a vital role in making the right investment decisions. Practitioners use this tool to measure returns and risks in the stock market. The fundamental analysis assesses the economic environment, firm performance, and industry performance before making investment decisions, and technical analysis considers price movements through the volume of supply and demand in the capital market. Several other behavioral factors considered, such as when the right time to buy shares, aside from the risk and return. The same result showed in Farooq *et al*. (2015) and Qureshi *et al*. (2012) research.

H_3: Financial tools could help an institutional investor in making a better investment decision

Corporate governance is one of the key components in increasing efficiency, growth, and investor confidence. Corporate governance includes a series of relationships between company management, the board of directors, shareholders, and other stakeholders. Corporate governance also provides a structure in which objectives are set, and the implies to achieve those goals and monitor performance are determined (Al-Sager & Samontaray, 2018).

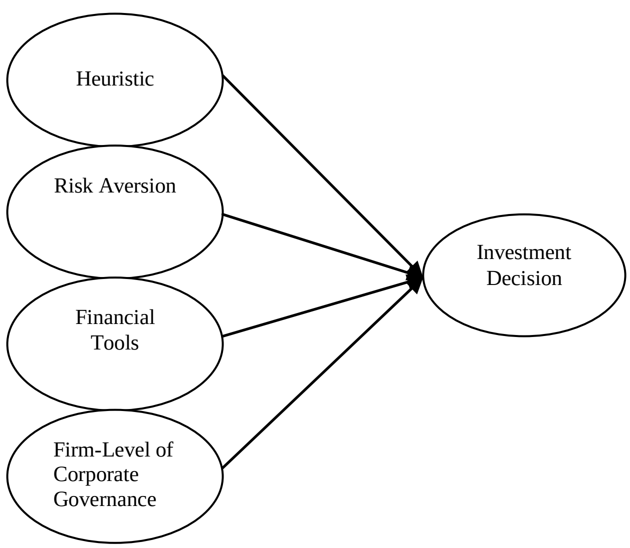
Firm-level of corporate governance has a positive effect on investment decisions in the research of Mumtaz *et al*. (2018). Corporate governance acts as a mechanism in making investment decisions. Firm performance is directly related to corporate governance performance. Effective governance ensures that the process structure of a company is well organized and helps in making the right and efficient decisions to achieve the company's objectives. The implementation of an effective corporate governance system will be able to provide value to shareholders, convince investors, and increase the value of the company. The result also in line with research by Qureshi *et al*. (2012).

Farooq *et al*. (2015) illustrate that when performance deviations occur, corporate or organizational systems can be directed and controlled in a manner called corporate governance. This research follows aspects of assessing corporate level corporate governance, which includes several elements such as transparency, fairness, discipline, responsibility, accountability, and social awareness. The corporate governance system plays an important role in the value of the organization. Hence, the hypothesis proposed as:

H_4: Invest in a firm with a high level of corporate governance could lead to a better investment decision

The conceptual framework of this research shown in this figure below.

Figure 1 Conceptual Framework



III. METHODOLOGY

The population of this study is the institutional investor in Batam city, Indonesia, and the sample was selected using the purposive sampling method. This research distributed 100 sets of questionnaires, and there were 80 sets of questionnaires completed. The analytical method used in this study is Partial Least Square-Structural Equation Modeling (PLS-SEM). Measurement of indicators in the questionnaire for each variable uses a Likert scale.

IV. RESULT AND ANALYSIS

Statistics descriptive showed the data of the respondents. Table 1 shows the demographic data of the respondents:

Table 1 Statistics Descriptive

Description	Frequency	Percentage
Gender:		
Male	52	65.00%
Female	28	35.00%
Age:		
18 to 25	30	37.50%
26 to 35	36	45.00%
36 to 45	11	13.75%
46 to 55	3	3.75%
More than 56	-	-
Industry:		
Bank	36	45.00%
Insurance	13	16.25%
Securities	16	20.00%
Financing	15	18.75%
Experience:		
Less than one year	4	5.00%
1 to 3 years	26	32.50%
3 to 5 years	19	23.75%
More than five years	31	38.75%
Certification:		
Capital Market	20	25.00%
Insurance	12	15.00%
Finance	8	10.00%
Banking	32	40.00%
None	8	10.00%
Analysis Methods:		
Fundamental	51	63.75%
Technical	29	36.25%

Source: Processed Data (2019)

Table 1 showed the result of the descriptive statistics of this research. It represents the demographic data of institutional investors. There are 52 (65 percent) male and 28 (35 percent) female investors. A total of 36 investors (45 percent) between the age of 26 to 35, and there are 30 investors (37.5 percent) in 18 to 25 age groups. There are also 11 institutional (13.75 percent) who are in 36 to 45 age groups and three investors (3.75 percent) within the age of 45 to 55. Mostly, the representative from the institution is from the banking industry, with a total of 36 investors (45 percent). There are also 16 investors from securities companies, 15 investors from financing companies, and 13 investors from an insurance company.

There are 31 investors (38.75 percent) who have experience for more than five years, 19 investors (23.75 percent) with 3 to 5 years experience, 26 investors (32.50 percent) with 1 to 3 years experience, and four investors with less than one year experience. Most of them own financial certification. A total of 32 investors (40 percent) own banking certification, and 20 investors (25 percent) have their certification in the capital market. Twelve investors (15 percent) have insurance certification, eight investors (10 percent) with finance certification, and another eight investors (10 percent) without any certification. In this research, respondents tend to be on using fundamental analysis methods than technical analysis.

There are 51 investors (63.75 percent) who use fundamental analysis and 29 investors who use technical analysis.

The outer model tested with validity and reliability. Table 2 showed the result of the validity and reliability test.

Table 2 Validity and Reliability Test

Variable	AVE	Cronbach's Alpha	Cronbach's Reliability
Heuristic	0.743	0.942	0.953
Risk Aversion	0.843	0.938	0.956
Financial Tools	0.736	0.879	0.917
Firm-level of Corporate Governance	0.882	0.983	0.984
Investment Decision	0.744	0.978	0.981

Source: Processed Data (2019)

The inner model tested to indicate the path coefficient. Table 3 represented the path coefficient test.

Table 3 Path Coefficient

Hypothesis	Coefficients	P-Value	Result
H_1	0.054	0.426	Rejected
H_2	0.057	0.622	Rejected
H_3	0.261	0.013	Accepted
H_4	0.608	0.000	Accepted

Source: Processed Data (2019)

The first hypothesis has a coefficient of 0.054, with a p-value of 0.426. It indicated that heuristic has an insignificant effect on investment decisions. It has the same result as the second hypothesis, which showed an insignificant effect with a coefficient of 0.057 and a p-value of 0.622. The third hypothesis has a coefficient of 0.261, with a p-value of 0.013. The fourth hypothesis has a coefficient of 0.608, with a p-value of 0.000.

Thus, H_1 and H_2 not supported, while H_3 and H_4 were accepted. It indicated that heuristic and risk aversion do not affect investment decisions, while financial tools and firm-level corporate governance have a significant positive impact on investment decisions.

Investment decisions might not be affected by heuristic because institutional investors have good knowledge in the analysis, whether it is fundamental or technical. So, it showed an insignificant relationship between heuristic and investment decisions. It also happened in risk aversion, which shows an insignificant relationship. Institutional investors tend to have stable risk management, so even if they are not risk-averse, it does not affect investment decisions.

Based on the result, it also showed that the use of financial tools and firm-level corporate governance lead to a better investment decision. Financial tools are the approaches adopted to measure a return and risk, so it supports institutional investors for making investment decisions. The financial tools approach is one of fundamental analysis. In this research, it showed that 63.75% of the respondent use fundamental analysis. A firm with good corporate governance also becomes an investment target for the institutional investor. Investor prefers to invest in a stock which has good governance. This result supported by Mumtaz et al. (2018), Farooq *et al*. (2015), and Qureshi *et al*. (2012).

V. CONCLUSION

This study concluded that heuristic and risk aversion do not affect investment decisions, while the use of financial tools and firm-level corporate governance would lead to better investment decisions.

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