The Application of Behavioral Finance in Improving the Economic Level of Poor Families

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Abstract: ***Family financial behavior determines the economic level of the family, a prosperous family is not measured by the level of income or overall income in a family, but with an indicator of balanced income and expenditure. Family financial behavior needs to be done rationally, because mathematical calculations are very important in planning long-term financial management. Previous research shows that financial behavior is not always based on logical considerations, but rather focuses on emotional considerations. This study uses a qualitative approach with a case study method that aims to focus on explaining the events that occur in a case, where the research was conducted in Cadas Gantung Village, Mekarmanik Village, Cimenyan District, Bandung Regency.Data collection techniques using structured interviews, observation and documentation, data obtained are then analyzed using data reduction, data presentation and conclusion drawing. The results of the study show that the application of financial behavior based on bounded rationality can increase family knowledge in considering financial decisions, so that financial planning can be planned well and programmed. This research is theoretically useful, especially in adding references to economics studies and in practice in helping the economies of underprivileged families.***

Keywords: Behavioral Finance, Economy, Poor Families

1. Introduction

Financial behavior is felt to be very important today, considering that the current growth in public consumption continues to increase along with the increase in people's incomes and increasingly improving economic growth. The level of well-being becomes a person's goal in work, many opinions say the higher the level of one's income, the more prosperous the person will be. It seems that this view is currently not very relevant anymore. High income levels without being accompanied by good management will not bring prosperity to someone (Putra, Handayani and Pambudi, 2013). This indicates that every community of various groups needs to understand and know about financial behavior.

Micro-financial behavior will have an impact on the level of welfare of the community, the community that is classified as prosperous and underprivileged is not only measured by its income, but also from its expenditure. So that doing long-term oriented finance behavior will form a prosperous family and be able to deal with a financial crisis. Previous research shows that the family financial behavior will have an impact on the level of welfare (Farmer & Tiefenthaler, 1997), this is due to the existence of expenditure factors, income and good financial reserves.

A person's behavior in carrying out activities relating to financial aspects is not only based on rational aspects, but also emotional aspects. Encouragement of someone to buy goods that do not have primary benefits in life, precisely the goods that become desires or adjust to modern lifestyles, often a reason for someone to do financial behavior based on emotional considerations. This indicates that there is a link between psychology and economics in carrying out actions relating to finance (Ramadhaniyati & Hayati, 2014).

Problems that occur from the actions of someone who conducts activities related to finance on an emotional basis, that is, occur in underprivileged families, because they have economic constraints to take actions related to finance. Problems that often occur are often the many loans that are not balanced with income, so that poor families are very difficult to rise to become prosperous families. The results of previous studies show that underprivileged families have no knowledge of financial management (Hermanus, Evelyn, & Patricia, 2013) which impact on bad financial behavior.

Problems regarding financial behavior are not only caused by community culture, but also by gender. Research conducted by Arifin and Robin (2016, p. 105) that in carrying out daily activities is never separated from the use of money. There are things that are quite unique in using money (financial behavior) if you see from two genders, men and women. This unique thing is derived from the nature of psychology that exists in the individual that causes the way of using between these individuals is different. This study aims to examine the differences between gender in Batam City in looking at financial psychology. A total of 500 sets of questionnaires were distributed with a rate of return of 471 questionnaires with the object of research of the people of Batam City who were or had worked.

2. Theoretical

2.1 Meanings of Behavioral Finance

Such behavior is not only related to the existing financial theory and economic law, but tends to be influenced and / or based on psychological factors. Behavioral finance combines both, namely economics and psychology (Barberis and Thaler, 2003). Financial behavior (behavioral finance) which is the application of psychology in financial disciplines. Financial behavior plays an important role in making investment decisions. Investment decision making is influenced by the extent to which investment decisions can maximize wealth, and behavioral motivation, investment decisions based on the psychological aspects of investors. Investment decision makers do not always behave in ways that are consistent with assumptions made in accordance with the perceptions and understanding of information received (Peteros and Maleyeff, in Prawirasasra and Dialysa, 2016, p. 23).

Financial behavior (performance and performance of all types of investors categories (Grinblatt, M., & Keloharju, M, 2000). The discussion related to financial behavior was also carried out by Sahi (2017) stating that financial behavior theory based on psychology is as understandable as how emotions and cognitive deviations affect investor behavior. Whereas, Barberis and Thaler (2003, p. Xvii) state that behavioral finance is a study of how humans interpret and act on information to make informed investment decisions.

Dreman and Lufkin (2000) argue that financial behavior is a behavior that is based on psychology that influences the decision process which is subject to some cognitive illusions. This illusion is divided into two groups, namely the illusion caused by heuristic and illusory decision processes adopted from the mental frame that is in the prospect theory.

Rinderle and Reichert (2006) explain that there are two thoughts, that investors cannot always process data in the right way so that it creates the wrong probability of distribution to predict future returns. Second, if the distribution is in actual condition, investors tend to also make non-optimal decisions. These two thoughts reinforce that investors can make irrational decisions. Finance behavior is included in decision making because it can be a driving factor in market prices.

The premise of behavioral finance is that conventional financial theory ignores how people actually make decisions and that everyone makes different decisions (Barberis and Thaler, 2003). Financial behavior at the practical level is strongly influenced by the financial management behavior that is related to one's financial responsibility regarding financial management. Charles (2011) states that good and correct financial decisions are needed to increase income, manage expenses, pay taxes so that family financial management is good. Positive childhood experiences about managing finance, the social environment, and attitudes towards saving play the role of financial management in family behavior in the future.

2.2 Behavioral Finance in Business Practice

Behavioral finance began to replace the standard financial concept and replaced the concept of rational investors to be normal investors who had bias bias socially, cognitively, and emotionally. Behavioral finance and decision making are closely related to psychological factors and also how much risk the investor will face (Wiryaningtyas, 2016, p. 339).

Behavioral finance according to science in which there is interaction from various disciplines (interdisciplinary) and continues to integrate so that in the discussion can not be done isolation. Behavioral finance grows from various assumptions and ideas of economic behavior. In behavioral finance also involves emotions, traits, likes and various kinds of things that exist in human beings as intellectual and social beings who will interact based on the emergence of decisions in carrying out actions (Riciardi, 2000).

Behavioral finance needs to be divided into two sub-topics, first is behavioral finance micro that is testing behavior or it can be from different individual investors with rational actors envisioned in classical economic theory. Second, behavioral finance macros that detect and illustrate that behavioral models can explain the occurrence of anomalies in efficient market hyphotesis (Pompian, 2006). Behavior finance is based on an alternative notion that investors, or at least a significant minority of them, are subject to behavioral biases that mean their financial decisions can be less than rational (Brooks, 2008).

Furthermore, Pompian (2006) states that behavioral finance is divided into two topics, namely behavioral finance macros and behavioral micro finance. Micro Behavioral Finance detects and describes anomalies in an efficient market hypothesis that might be explained by the behavioral model. While behavioral micro finance tests the behaviors or psychological biases of individual investors that distinguish them from rational behavior proposed by classical economic theory, portfolio theory and efficient market hypotheses.

2.3 Theory of Financial Behavior

Developing countries such as Indonesia have a vast area and the fourth largest population in the world, Indonesia faces the problem of many people who do not understand financial problems. In other words, the level of financial literacy of Indonesian people is still low. The real evidence of the low level of financial literacy is shown by the small number of people who come into contact with financial institutions and financial products (Setiawati and Nurkhin, 2017, p. 728).

In this discussion, we will present five theories relating to investor behavior as an effort to comprehensively understand contemporary finance.

a) Regret Theory

This theory relates to people reacting to emotional experiences after realizing they have made a mistake in the assessment. Faced with the prospect of selling shares, investors are emotionally affected by the price at which they buy shares. So, they avoid selling it as a way to avoid regret for making a bad investment, and ashamed to report a loss. This theory can also apply to investors who find their shares considered to be buying but do not rise in value. Some investors avoid the possibility of feeling this regret by following conventional wisdom and buying only the shares that other people buy, rationalizing their decisions with others do so (Zeelenberg, M., & Pieters, R, 1982).

b) Theory of Mental Accounting

This theory states that humans have a tendency to place certain events into mental compartments, and the differences between these compartments sometimes impact our behavior more than the event itself. Examples of this theory are illustrated by doubts about selling investments that once had terrible profits and now have simple advantages. When the market correction deflects investor net worth, they are more hesitant to sell at smaller profit margins. They make mental compartments for the profits they once had, causing them to wait for the return of a favorable period (Sagoff, 2012).

c) Prospect/Loss-Aversion-Theory

This theory shows that people express different levels of emotions towards the benefits of the direction of loss. Individuals are more emphasized by potential loss than they are happy from the same benefits. Investors often make the mistake of pursuing market action by investing in stocks or funds that collect great attention. Research shows that money flows to high-performing mutual funds faster than money flows out of funds that are left behind (Abdellaoui, M., Bleichrodt, H., & Paraschiv, 2007).

d) Over/Under Reacting Theory

Investors get optimistic when the market rises, assuming it will continue to do so. Conversely, investors are becoming very pessimistic in the midst of a slump. The consequences of anchoring, putting too much importance on recent events while ignoring historical data, are over or under reaction to market events that result in prices falling too much on bad news and rising too much good news. At the height of optimism, investors' greed moves shares outside of their intrinsic value (Drumheller, 2000).

e) Theory of Overconfidence

People generally judge themselves as being above average in their abilities. They also overestimate the accuracy of their knowledge and relative knowledge to others. Many investors believe they can consistently market time. But in reality there is a large amount of evidence that proves otherwise. The results are too trusting in excessive trade, with the benefits of Bimbang trade costs (Burks et al., 2013).

2.4 Understanding Bounded Rationality

Herbert Simon is himself the pioneer of bounded rationality, and it is true that in economics every time the concept of bounded rationality is discussed, it will be directed to a Herbert Simon (Barros, 2010). Simon's 1950s paper inspired scientists related to concepts, which then showed that empirical studies were very important in the real world (Kamarck, 2005, p. 64). In its development, the concept of bounded rationality has been proven in a variety of impressive work (Conlisk, in Firmansyah, Suman and Susilo, 2013, p. 230).

The development of the study of rationality occurs not only quantitatively, but also in terms of its impact. As an illustration, of the two Nobel prizes in economics given to psychology researchers, both are related to rationality in decision making. The first Nobel Prize was given to Herbert Simon in 1978 for his contribution related to bounded rationality (Hidayat, 2016, p. 102).

Furthermore, Hidayat (2016, p. 105) states that the essence of the conception of bounded rationality is that human individuals are not perfectly rational beings as assumed in mainstream economic theory. Human rationality knows the limits of ability, because it is called bounded rationality. One of the main manifestations of bounded rationality is that in decision making, the best results-oriented individuals that are capable of being achieved, or referred to as satisficing, are not the greatest results that should be achieved. Thus satisficing is a theoretical alternative to the optimal utility (the greatest result that should be achieved) in rational behavior.

3. Method

This research was carried out in Cadas Gantung Village, Mekarmanik Village, Cimenyan District, Bandung Regency. The choice of place of research is based on academic and social considerations, in the academic realm, the need for universities to improve the condition of society.

The research method used in this study is a case study. Maxfield (in Nazir, 2011, p. 57) case study is "research on the status of the subject of research relating to a specific or typical phase of the overall personality". The research subjects are individuals, groups, institutions and communities, the purpose of the case study is to provide a detailed description of the background, traits and characteristics that are typical of the case, or the status of the individual, then from the traits and characters -The typical character above will be a general matter (Nazir, 2011, p. 57).

The researcher used interview guidelines, observation guidelines and documentation studies. In addition, the researcher also uses tools to facilitate research, including:

a) Notebook (notebook), which functions to record in the process of interviews, observations and other activities relating to the process of collecting data.
b) Tape recorder, which is used by researchers to record during interviews with resource persons, so that data accuracy is more valid.
c) Cameras, which are used in every research activity, both in the interview process, observation and other activities relating to the research process.

In practice, researchers use direct observation techniques regarding the application of finance behavior, after knowing the focus of the problem to be discussed. So the researchers conducted interviews with those who could support the research data, as well as conducting documentation studies while conducting research. The results obtained are then tested for the truth and a conclusion is taken as the answer to the formulation of the problem made by the researcher based on the problems in the field.

The process of data analysis in this study will be carried out continuously from the beginning to the end of the study, both on the field and outside the field. Data analysis takes place simultaneously with the data collection process. Among them are data reduction, data presentation and conclusions/verification.

4. Results and Discussion

Based on the results of the study indicate that the way to change the financial behavior of poor families is to know good financial planning. Good financial planning is largely determined by the level of family knowledge about financial priority scales. In the stages of planning and expenditure, it is necessary to have a mathematical calculation between the income earned and expenses incurred by the family. The most important aspect is that disadvantaged families must manage money with logical aspects, not based on emotional aspects.

Implementing finance behavior must be able to understand the problem of poverty in society. Meadows (1987) tried to identify the causes of poverty in terms of the economy. First, micro-poverty arises because of the inequality of resource ownership which causes an unequal income distribution. The poor have only limited resources and low quality. Second, poverty arises from differences in the quality of human resources. Low human resource quality means that productivity is low, which in turn low wages. The low quality of human resources is due to low education, the fate of being less fortunate, the existence of discrimination or because of offspring.

Third, poverty arises due to differences in access in capital. These three causes of poverty lead to the theory of the vicious cycle of poverty (vicious circle of poverty). This theory was discovered by Ragnar Nurkse (1953) stating that "a poor country is poor because it is poor". The existence of backwardness, market imperfections, and lack of capital have caused low productivity. Low productivity results in low income they receive. Low income will have implications for low savings and investment. Low investment results in underdevelopment. Therefore, every effort to reduce poverty should be directed at cutting this poverty circle and trap (Kuncoro, 2004). Here's a picture of the poverty vicious circle (vicious circle of poverty).

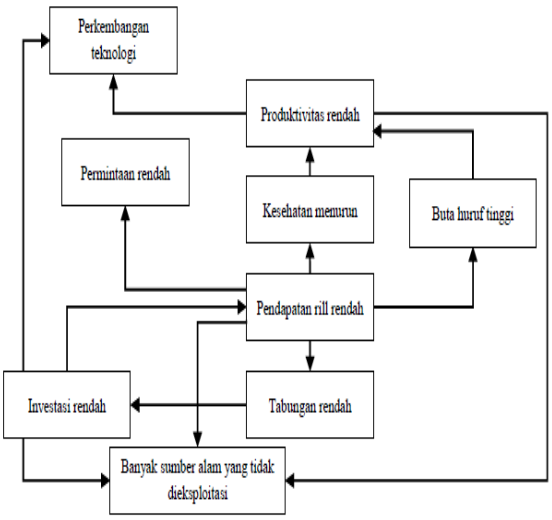

Figure 1: Satan's Circle of Poverty
(Nurkse, in Kuncoro, 2004)

In his opinion the core of the vicious cycle of poverty is the conditions that cause barriers to the creation of high capital formation. On the one hand the formation of capital is determined by the level of savings and on the other hand by incentives to invest. In developing countries these two factors do not allow for a high level of capital formation. So, according to Nurkse's view, there are two types of vicious circles of poverty that prevent developing countries from achieving rapid development, namely in terms of offering capital and capital demand.

In the context of a wider society there are several groups of people who have interests in behavioral finance. Ricciardi and Simon (2000) divide three groups of individuals who have a direct or indirect interest in behavioral finance:

a) Individual, yang terdiri dari small investor, portfolio manager, pension board
b) Group, yang terdiri dari investor reksadana (portfolio)
c) Organization, misalnya financial institution, non profit organization universities.

This interest group in the context of society will be very influential in making family financial behavior.This study experienced challenges in the application of behavioral finance based on bounded rationality, because teaching the same understanding of finance was not easy and not done in a fast time. Every individual has different characteristics and tendencies of financial behavior as a result of the factors that influence the individual from both the internal and external individuals. Psychological influences such as character and character are the strongest factors that influence a person's financial behavior. In addition there are many external factors that are influenced by a person's financial behavior, including financial knowledge (financial knowledge), financial attitude (financial attitude) and income level

This indicates that there are aspects of knowledge, attitudes and income that will affect financial behavior. Mathematical calculation is a very important aspect in managing finances. The idea of bounded rationality is built through the following steps (Dequech, in Firmansyah, Suman and Susilo, 2013, p. 230) individuals or organizations often pursue a number of objectives, which may conflict. The alternative choice for pursuing that goal was not previously given to decision makers, so it was necessary to adopt a process to produce alternatives, then there were limits to the decision maker's mental capacity compared to environmental complexity in decision making, so that the various limitations caused decision makers to adopt " satisficing "rather than optimizing strategies, looking for solutions that are" good enough "or satisfying, and given several levels of aspiration.

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