

The Effect of Bad Reputation and Increasing Factor Towards Investment Decision: Experimental Study on Young Investor

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Abstract

The purpose of this research is to examine the effectiveness of clawback to increase the intention of young investors in companies that have a bad reputation. This research also examines the intention to invest between independent income groups and non-independent income groups in bad reputation companies. This study uses an experimental method with a 2x2 design between subjects. The subjects of this study amounted to 70 participants. The result showed that there was no difference in the investment interest of young investors, both those who already have income and those who do not have income in bad reputation companies. In addition, clawback could increase the investment interest of young investors to invest in companies that had a bad reputation because of their sense of security.

Keywords: *investment, investor, bad reputation, clawback*



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INTRODUCTION

In 2019, the Indonesia Stock Exchange (IDX) recorded a total of 2.48 million investors, an increase of 53% from the previous year. Unlike the previous year, in 2020, there were interesting facts. Although this was a tough year for the Indonesian capital market due to the Covid-19 pandemic, there was an increase in the number of investors by 56%. This growth is the highest in the last three years. Data from the Financial Services Authority show that the average increase in investors is domiciled in Java, namely DKI Jakarta, Banten, and the Special Region of Yogyakarta). This strengthens the basis for the need for further research related to the investment interest of investors in Yogyakarta. This result can be said to be quite interesting because, during the pandemic, when many people have lost their jobs, many people became aware of the importance of investing.

The purpose of this research is to examine the effectiveness of clawback to increase the intention of young investors in companies that have a bad reputation. This research examines the intention to invest between the independent income group and the non-independent income group. This study focuses on novice investors to see the impact of implementing rules related to trust guarantees, namely clawback. This guarantee is very important to be applied in companies listed on the Indonesia Stock Exchange (IDX) related to maintaining investor confidence. Guarantees provided by companies to investors in the form of deductions from bonuses received by directors (Brink and Rankin, 2013) are carried out to mitigate managers or directors due to intentional or unintentional reporting errors. Reputation greatly influences the decision to take ethical actions or not. (Iskandar-Datta and Jia, 2013) (Stevens, 2002) (Webb, 2002) (Kaplan et al., 2007).

A state-owned company is experiencing a case related to fraud in its financial statements. Large companies that already have a very good reputation must be bad because of an error in the preparation of

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DOI: <https://doi.org/10.31098/bmss.v1i3.343>

Research Synergy Foundation

financial statements by allegedly making mistakes or allocating the company's receivables so that the profits generated look good. This study uses this case and wants to see how the impact of a bad reputation on the intention of young investors is. In addition, this study also provides a clawback variable to increase investor confidence in companies that already have a bad reputation. This is important to do to restore confidence in investors by providing guarantees to them regarding the safety of the money they provide to the company.

LITERATURE REVIEW

Investment Intention

In accordance with the theory presented by Ajzen and Fishbein (1975), it shows that there are several factors that influence behavior, namely beliefs, attitudes, and intentions (intentions). The intention factor consists of behavioral elements, the target to be treated, the situation, and the time of the action.

Reputation

Company reputation is defined as a picture of a company that is profitable or unprofitable in terms of the characteristics of the company (Chong and Loy, 2015). Reputation is important to maintain because it shows whether or not a company is safe to invest in. In building a company's reputation, it is necessary to consider the management control system within the company to produce output that is in accordance with the company's vision and mission. Companies that have problems will have an impact on their reputation on investor views.

Clawback

Iskandar-Datta and Jia (2013) state that clawback is the return of incentives that have been received by managers or executives due to not achieving company goals or intentionally making mistakes that result in a reduction in company revenues. Companies that have previously made reporting errors voluntarily apply a clawback incentive system to restore investor confidence (Iskandar-Datta and Jia, 2013; Fried and Shilon, 2011). Adoption of clawback can also improve quality financial reporting and investors' perceptions of the company's financial statements (Dehaan, Hodge, and Shevlin, 2013). Fung et al. (2015) compared the risk of fraudulent financial reporting for companies that apply clawback and do not apply clawback, and the results show that there is a significant reduction in the risk of fraudulent reporting. The results of Hirsch, Reichert and Sohn (2017) show that clawback can improve earnings quality (Chan et al., 2012) and financial reporting quality (Dehaan, Hodge, and Shevlin, 2013). The implementation of clawback frames is very effective in reducing unethical behavior within the company. Withdrawal of bonuses that have been received makes individuals deterrent and do not want to commit violations again.

The implementation of clawback compensation makes managers more concerned with market views and more accountable to investors (Brown et al., 2015). Companies that have made misreporting will voluntarily apply clawback incentives for their executives, and this is done to regain market confidence (Brown et al., 2015). Clawback not only has an impact on executives but also on the entire management control system in the company. Managers will be more careful in making investment decisions (Hirsch, Reichert, and Sohn, 2017).

Based on the results of the research above, it is important to apply clawback in companies, especially companies that have been caught red-handed in misrepresenting financial statements (Chan et al., 2015). This will have an impact on the desire of individuals to make investment decisions (Brink and

Rankin, 2013). In accordance with the endowment effect theory, individuals who are able to earn income independently will consider investing in companies that have implemented clawback because the fear of loss or loss of money will be greater than individuals who don't make money on their own.

H1: Individuals' intention to invest in independent income groups will be greater than individuals in non-self income groups.

The application of clawback can improve the quality of financial statements, and this happens because CEOs in companies that implement the clawback provision will be careful and avoid misstatements in financial reporting given the impact of declining income and a bad reputation (Chan et al., 2012) and also prevent unethical behavior (Stevens, 2002). The results of the survey conducted indicate a positive perception of investors and auditors on the company's financial statements after the implementation of the clawback provision (Chan et al., 2012). The auditor views that companies that implement the clawback provision have low audit risk, the auditor also finds that companies that have implemented the clawback provision have good internal control (Chan et al., 2012). The implementation of the clawback provision makes the CEO and management more responsible for providing actual reporting after a merger or acquisition is held (Webb, 2002).

The voluntary application of clawback causes the CEO's power to be reduced (Brown et al., 2015). Several studies have shown that the adoption of clawback can reduce earnings management (Chan et al., 2012), improve financial reporting quality, perceived financial reporting quality, and performance (Dehaan, Hodge and Shevlin, 2013), increase managers' rationality in investing (Hirsch, Reichert and Sohn, 2017), reduce fraud risk (Fung et al., 2015), and improve earnings quality and auditor trust (Chan et al., 2012).

In accordance with the endowment effect theory that individuals do not want to lose income by making analytical errors (Bobek, Hageman, and Kelliher, 2013). Moral hazard theory also states that individuals will be selfish (Quadrini, 2004). Until they can increase investor confidence to invest. However, there are differences in sources of income. Individuals with an income that comes from hard work will be more careful in investing their money. The endowment effect emphasizes that a person will take irrational actions to maintain something he already has even though in the eyes of others it is no longer valuable (Kahneman, Knetsch and Thaler, 1991).

H2: Individual investment intention in companies that implement clawback will be greater in individuals that do not implement clawback.

RESEARCH METHOD

The research design used is experimental research. The experiment is a research design to investigate a phenomenon by manipulating conditions or conditions through certain procedures and then observing the results (manipulation) and interpreting them (Nahartyo, 2012). The independent variable in this study is clawback. The moderating variable in this study is the type of income of novice investors. This study uses 2 x 2 factorial between-subject factorial designs. The subjects in this study are 70 students. One of the requirements in this research is the student has taken investment courses.

Data collection is carried out with media zoom meetings to ensure participants work at the same time. Experiments were carried out by following several procedures that had been prepared by the experimenter. The following is the experimental procedure in this study; first, the experimenter divided the participants into two groups randomly. A group is a group that has a clawback application and a group that does not apply clawback. In this context, the company is experiencing financial problems, and it is

found that there is a financial misrepresentation. Second, participants were then given an explanation through a google form regarding their biodata and financial condition. This is to find out whether the participants have earned income independently or not. After that, participants will answer several questions, including how much they want to invest in the conditions presented in the case. Researchers will make four different cases; each participant will work on only one case. This experiment will be carried out directly through zoom media so that researchers can control participants and reduce bias. Next, participants fill out manipulation check questions and demographic data. The last step is debriefing. Researchers provide information about the objectives of the experiment that has been undertaken by the research subjects. Researchers also explain the hypotheses proposed in the study (Blumberg, Cooper, and Schindler, 2014).

Data processing in this study using independent t-test testing. If the test results show that the two groups are significantly different, then the hypothesis is accepted. However, if the results do not show a significant difference between the two groups, then the hypothesis is not supported. The indicator used is a significance value of 0.05.

FINDINGS AND DISCUSSION

The results of descriptive statistics are presented in Table 1 to show the mean, standard deviation, minimum, and maximum of all variables.

Table 1. Descriptive Statistic Variables

Variable	Sample Size	Mean	Std. Deviation
Income	70	1,4714	0,50279
Clawback	70	2,9167	0,50340
Intention to Invest	70	3,1310	1,43770

The first hypothesis proposed in this study is that individuals' intention to invest in owned income groups will be greater than individuals' non-owned income groups. The dependent variable in this research is the intention to invest. Table 2 shows descriptive statistics, while Table 3 shows the results of testing Hypothesis 1 using an independent sample t-test with a significance of 0.205, so it can be concluded that H1 is not accepted. This result also shows that both investors who already have their own income and those who do not have their own income agree that investing in companies that have a bad reputation is a bad decision.

Table 2. Descriptive Statistic Income and Intention to Invest

	Income	N	Mean	Std. Deviation
Intention	Owned	37	2,9189	1,163
	Not Owned	33	2,5455	1,276

Table 3. Independent Sample Test Owned and Not Owned

Intention		t	df	Sig. (2 tailed)	Mean Difference
	Equal Variances Assumed		1,280	68	0,205
Equal Variances not Assumed		1,273	65,177	0,207	0,3724

The second hypothesis in this study is individual investment intention in companies that implement clawback will be greater in individuals that do not implement clawback. The independent variable in this study was implementation clawback. There are two treatments in testing this hypothesis, namely, the group with clawback implementation and the group without clawback implementation. Table 4 shows the descriptive statistical variables. Table 5 shows the results of the Independent T-Test. The results show that the two groups differ significantly. The group with clawback treatment (there is a guarantee that the CFO and CEO are responsible for returning investor losses if there is fraud in the financial statements) has a greater investment interest even though the company's reputation is bad. On the other hand, the intention of young investors in the group that is faced with no clawback tends to disagree with investing in companies with a bad reputation. The difference is at a significance level of 0.005. These results indicate that H2 is accepted.

Table 4. Descriptive Statistic Clawback and Intention to Invest

	Clawback	N	Mean	Std. Deviation
Intention	Clawback	34	2,3235	1,006
	No Clawback	36	3,3189	1,290

Table 5. Independent Sample Test Clawback Implementation

Intention		t	df	Sig. (2 tailed)	Mean Difference
	Equal Variances Assumed	2,935	68	0,005	0,2778
	Equal Variances not Assumed	2,956	65,67	0,004	0,2758

The effect of a bad company reputation, as described in the experimental case, which states that there is fraud in the financial statements presented, encourages young investors not to invest in the company. The desire to invest in individuals who are already working and not working is not significantly different. These results are in line with the results of moral hazard theory, which states that individuals will allocate their resources according to their respective interests (Quadrini, 2004).

After seeing the results of hypothesis 1 that individuals consider reputation in making investment decisions, furthermore, the researchers added an effective clawback variable to increase individual intentions to invest. The results show that the group with clawback implementation tends to have a higher investment decision than the group without clawback. These results indicate that the assurance that the company's executives guarantee that the financial statements are free from fraud can increase the desire of young investors to invest. These results are also in line with research conducted by Chan et al. (2015) that clawback is effective for mitigating negative behavior, one of which is fraud.

CONCLUSION AND FUTURE RESEARCH

The purpose of this research is to examine the effectiveness of clawback to increase the intention of young investors in companies that have a bad reputation. The subjects of this research are young investors because the current trend of investors is young investors who have just joined. There is one reason that new investors tend to be risk-averse. Young investors, both those who already have their own money and those who don't have the same decision not to invest in companies that have a bad reputation. The results of this study also provide additional knowledge that investors, especially young investors, will choose a company with a bad reputation if there is a guarantee from the executive that the financial statements produced are far from fraudulent.

The results of this study can provide an illustration that the company's reputation is one of the important factors considered in making investment decisions. Companies should maintain a reputation so that investors continue to consider investing in the company. Even large companies have no guarantee that their value will return after their reputation has fallen. One way that can be used is to provide assurance to investors from the executive that the executive will compensate if there is evidence of fraud in the preparation of financial statements. This way also forces the executive to be more stringent in controlling the management control system to the published financial reports (Dehaan, Hodge, and Shevlin, 2013).

Future research can consider comparing young investors with investors who have long invested their money in certain companies. In addition, if there is a new phenomenon, it can also be used as an experimental case so that the results obtained are more in line with the reality of conditions in the field.

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