Mental Accounting: Investors Create Different Accounts for Dividends and Capital Gains

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ABSTRACT

The purpose of this research is to explore more about the behavior of investors who tend to create different accounts for dividends and capital gains. The method used in this research is literature study. The result obtained shows that investors tend to be willing to spend dividends but are not willing to realize capital gains by selling a small portion of shares for the same purpose. Stock investors generally create separate accounts for dividends and capital gains. Investors should focus on the total yield and view both as fungible and interchangeable. Furthermore, investors treat dividends the same as property rental income and share portfolios as property assets, while realizing capital gains to be spent. This can cause regret when the stock price turns up.

INTRODUCTION

Every individual is faced with a decision-making situation in the financial market and capital market; therefore decision-makers must prioritize rationality so that it does not lead to non-optimal results. From the various decisions that must be taken immediately, it will arise how to manage existing finances to get a maximum income (Marissa, 2012).

When making investment decisions, standard traditional theory in finance is relatively dominated by expected utility theory. Expected utility theory assumes that individuals are rational decision makers, but they are often irrational when they make their choices (Robison, Shupp, & Myers, 2010). There are many psychological factors, such as emotions, moods, psychological biases, and others that affect the decision-making process. Even Kahneman and Tversky (1979) developed the Prospect Theory, in which there are factors such as regret, loss avoidance, and mental accounting that can influence a person's decision-making process.

Investment activities that are generally carried out by investors are investing several funds in real assets in the form of buildings, gold, machinery, or land as well as financial assets in the form of shares, bonds or deposits. For investors who are more experienced and dare to take risks, they usually invest in more complex financial assets such as options, features, warrants or international equities (Kartini, 2019). Investors are individuals or institutions that invest their funds in financial instruments such as stocks, bonds, and so on.

Investing is basically placing a certain amount of funds today with the hope of making a profit in the future. Investors do not only consider the estimated prospects of investment instruments in their investment behaviour, but also involve psychological factors in making their investment decisions. This means that the analytical approach begins to use psychology and financial science to understand financial behaviour.

This theory implies that investors divide their investments in various portfolios based on several mental categories that they have. Then they separate the investment policies for each mental account in a way that each of them has a specific goal to achieve and the goal is to maximize returns while minimizing risk. This can result in unfavourable portfolio selection but satisfy investors' emotions (Barberis & Huang, 2001).

Behavioral finance study how humans behave in financial decisions that focus on how psychology affects financial decisions, companies, and financial markets (Kim and Nofsinger, 2008). Aspects of rationality are often faced with uncertainty in terms of making financial decisions, because humans as individuals do not always prioritize their reasoning but cannot be separated from the aspect of bias when making decisions or human error.

Assumptions about investor behavior are sourced from classical and neoclassical economic literature. In the sense that humans are seen as creatures who can make decisions based on very logical and transparent considerations. Therefore, humans are referred to as homo economicus, beings who can calculate and find the optimal point as an answer to the financial economic problems they face. The optimal point is a point that can provide maximum utility for a decision maker (Muniya A and M Harsono, 2001).

In Pompian (2011) states that the criticism of the homo economicus theory is aimed at questioning the basis of the three assumptions. In fact, humans can act socially by being influenced by emotions and it is impossible for someone to get complete and continuous information. One example of phenomena that show irrationality by investors is the fall of the United States capital market, known as Black Monday. Stock prices on the New York Stock Exchange at almost the same time experienced a very sharp decline for no apparent reason and the incident was recorded as the worst day of the American capital market since 1929 (the great depression crash). At that time, investors panicked, and the market became very out of control.

Thaler and Shefrin (1981) suggested that aThe reason someone makes decisions in financial matters can be explained by the term "mental accounting. A phenomenon of financial behavior or behavioral economics (behavioral finance) which was first investigated by Richard Thaler. The theory states that individuals assign a different level of utility to each group of assets which then influences consumption decisions, investment decisions, and other financial behavior. Instead of rationally treating every Rupiah they own, mental accounting helps explain why many investors designate some of their money as safety capital that they invest in low-risk investments, while at the same time treating their risk capital very differently. Investors do not only consider the estimated prospects of investment instruments in their investment behavior, but also involve psychological factors in making their investment decisions. This means that the analytical approach begins to use psychology and financial science to understand financial behavior.

One of the cognitive biases that investors often do is mental accounting bias. Stock investors generally create separate accounts for dividends and capital gains. There are two different sources of income from stock investments, namely dividends and capital gains. Broadly speaking, the two things are different in terms of the period, how to get it, the calculation and the things that affect it.

Thaler (1990) and Davis (2003) in Marissa (2012) argue why someone uses mental accounting? Because it allows transactions to be evaluated separately from other transactions. This will reduce the cognitive burden of decision making and make decision making easier. Chatterjee, Heath, and Min (2009) reveal that mental accounting can have a negative impact on decision making. However, Thaler (1999) states that there is no need to worry whether someone who experiences mental accounting is rational or not. Karlsson (1998) and Hoch & Loewenstein (1991) assert that mental accounting can be used as a self-control tool.

In Marissa (2012) said that from various studies or experiments that have been carried out, more researchers examine the impact of mental accounting from the negative side (wasteful) but have not comprehensively studied that mental accounting also has a positive impact (eg self-control). According to me, unlike self-control bias, illusion control bias, and disposition effects which can be very detrimental, the impact of mental accounting bias is less worrisome. Treating found money, house money, and annual bonuses differently from regular monthly income is reasonable. Indeed, mental accounting bias can also provide benefits.

In this paper, the investor behavior factor that will be discussed is mental accounting. Mental accounting describes the tendency of people to code, categorize, and evaluate economic outcomes by grouping their assets into several non-interchangeable mental accounts in their minds (R. Thaler, 1980). According to Pompian (2006), highly rational people will never be exposed to this psychological bias, because mental accounting will cause someone to take irrational steps to place money differently based on certain categories, such as how to get money (work, inheritance, gambling, bonuses, etc.). -other) or the nature of the use of money (recreation, necessities, etc.). Cheema & Soman (2006) says that a person might use different monthly budgets for grocery shopping and dinner at a restaurant, for example, and limit one type of purchase when the budget is exhausted while not limiting the other types of purchases, even though both expenditures use the same resources (income).

RESEARCH METHOD

In this study, the author uses literature research, including the type of library research. Library research is research in which data collection is carried out by collecting data from various literatures. The literature studied is not limited to books but can also be in the form of documentation materials, magazines, journals, and newspapers. The emphasis of library research is to find various theories, laws, propositions, principles, opinions, ideas, and others that can be used to analyze and solve the problems studied. The approach used in this study is a qualitative approach, namely by emphasizing the analyst on the process of inferring comparisons and on the dynamics of the relationship between observed phenomena using scientific logic (Saifuddin Azmar, 2001).

RESULTS AND DISCUSSION

Mental accounting indirectly has a close relationship in the stock market. One of the cognitive biases that investors often do is mental accounting bias. It is named accounting because this bias relates to separate accounts such as in an accounting ledger. Mental accounting bias is a person's tendency to make or assess economic decisions by grouping assets or sources of money into separate (non-fungible) accounts. Stock investors have two sources of income, namely dividends and capital gains. In general, stock investors create separate accounts for dividends and capital gains. Investors should pay more attention to the total yield and view dividends and capital gains as fungible (transferrable).

Mental accounting bias that occurs against stock investors is caused by two things. First, investors tend not to use their capital. Dividends are treated the same as property rental income and a stock portfolio is a property asset. Second, capital gains are used for spending activities which in the end can cause regret if the stock price turns up. The following are examples of bias in everyday life. “A friend realized a capital gain to buy a deer car for Rp. 250 million. A few months later, he regretted his decision because the shares sold rose 100% in price. He considers the value of the car is not Rp. 250 million, but Rp. 500 million". As an example, some investors divide their investments into safe investment portfolios and speculative portfolios to prevent negative returns owned by speculative portfolios that may affect the entire portfolio. The problem in this practice is that despite all the work and all the money an investor spends on separating their portfolios, their net worth will be no different when compared to those that have combined into a large portfolio.

Another aspect of mental accounting is that people treat money differently depending on its source. For example, people will tend to spend more money such as work bonuses and gifts, compared to the amount they would normally expect such as their salary. This is another example of how mental accounting can lead to an illogical use of money (wasteful). Logically, money should be used regardless of its source. Treating money differently because it comes from different sources is a violation of the logical premium. Just as investors treat dividends and capital gains differently. The logic is that investors don't need to sell shares to get dividends. If holding company shares within the specified time, investors will automatically receive dividends. Meanwhile, investors need to sell shares first if they want to get capital gains. Even though they have differences in terms of sources, investors still can get dividends and capital gains. Investors can apply strategies to obtain maximum profits.

The important thing to consider in minimizing mental accounting is that money is worth it, regardless of its source or intended use, all money is the same. In my opinion, unlike the very detrimental control illusion bias and self-control bias, the impact of mental accounting bias is not so worrying. I say this because in addition to having a negative impact (wasteful), mental accounting also has an impact on the positive side, namely as self-control. Thaler (1999) states that there is no need to worry whether someone who experiences mental accounting is rational or not. Karlsson (1998) and Hoch & Loewenstein (1991) assert that mental accounting can be used as a self-control tool.

Treating money differently from the results of the lottery (found money), wins at the casino (house money), and annual bonuses from regular monthly income is normal. Likewise, creating separate accounts for dividends and capital gains is a natural thing or there is nothing wrong with it. Such as grouping assets into current income, current assets, and future income is also something that makes sense. The thing that individuals need to remember and avoid is to allow high-interest loans when individuals have cash in savings or deposits that pay much lower interest rates. In Ajzen (1991) and Ajzen & Fishbein, (1980) define intention as a conscious possibility given by actors to engage in certain behaviors.

In this paper, I as a writer argue that mental accounting bias also provides benefits or positive impacts, namely self-control. Investors' decisions also depend on the expected profit expectations of investors, the cost of asset acquisition and the availability to manage the investment, as well as how to manage its finances (Harcourt, 1967). Associated with mental accounting bias for investor behavior in investment decisions, there are several recommendations for further research. First, attention should be paid to empirical research based on primary data to analyse investor behavior during investment decision making. Second, research can be done by combining various types of investors such as individuals, institutions (mutual funds, hedge funds, pension funds, investment advisors,

CONCLUSION

One of the cognitive biases that is often done by investors is mental accounting bias, where a person's tendency to make or assess economic decisions by grouping assets or sources of money in several separate (non-fungible) accounts. Financial theory needs to be understood and implemented in decision making to get a profitable investment. An understanding of financial theory can increase the wealth of shareholders and investors while increasing their potential to invest more. By understanding behavioral finance, an overview of the actual behavior of investors and the factors that cause differences in investor behavior is obtained.

Behavioral finance has also been heavily criticized. Behavioral finance only proposes empirical findings that refute the rationality-based traditional finance theory. In this context, behavioral finance still shows many limitations. Currently, there is no unifying behavioral finance theory or unifying behavioral finance theory (Statman, 2018). Behavioral finance is still composed of several theories that seem to be separate from each other. The point is that mental accounting also has an impact on the positive side, namely as self-control. Thaler (1999) states that there is no need to worry about whether someone who experiences mental accounting is rational or not. Karlsson (1998) and Hoch & Loewenstein (1991) assert that mental accounting can be used as a self-control tool. Treating money differently from the results of the lottery (found money), wins at the casino (house money), and annual bonuses from regular monthly income is normal. Likewise, creating separate accounts for dividends and capital gains is a natural thing and there is nothing wrong with it. Just as investors treat dividends and capital gains differently in terms of source or origin. The logic is that investors don't need to sell shares to get dividends. If you hold company shares within the specified time, investors will automatically receive dividends. Meanwhile, investors need to sell shares if they want to get capital gains. Even though they have differences in terms of sources, investors still can get dividends and capital gains.

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