

PSYCHOLOGICAL FACTORS INFLUENCE ON FINANCIAL VULNERABILITY: A CONCEPTUAL PAPER

Umi Hamidaton Mohd Soffian Lee ⁱ, Nuradli Ridzwan Shah Mohd Dali ⁱⁱ, Hanifah Abdul Hamid ⁱⁱⁱ, Wan Rasyidah Wan Mohd Nawang ^{iv} & Wan Nur Fazni Wan Mohamad Nazarie ^v

ⁱ (*Corresponding author*). Lecturer, Institution. Faculty of Economics and Muamalat, Universiti Sains Islam Malaysia. umihamidaton@usim.edu.my

ⁱⁱ PM Dr., Faculty of Economics and Muamalat, Universiti Sains Islam Malaysia. nuradli@usim.edu.my

ⁱⁱⁱ Lecturer, Faculty of Science and Technology, Universiti Sains Islam Malaysia. hanifah@usim.edu.my

^{iv} Lecturer, Institution. Faculty of Economics and Muamalat, Universiti Sains Islam Malaysia. wrasyidah@usim.edu.my

^v Lecturer, Institution. Faculty of Economics and Muamalat, Universiti Sains Islam Malaysia. fazni@usim.edu.my

Abstract

The recent financial and economic crisis highlights a worsening in the economics and financial situation of household to deals with debt burden, financial distress and unexpected expenses. In the context of increasing rising poverty and social inclusion a discussion on this phenomenon is required in order to identify the major factor may influence individual financial vulnerability which cause inability to assess and make effective decision regarding personal finances. This is library research where content analysis method was applied. This paper aims to identify the elements of psychological factors and its influence on financial vulnerability and proposes a conceptual model to further understand the area of research context. Besides, this paper then develop into concrete research hypotheses for future studies. Findings and discussion will serve as a useful guideline to develop comprehensive understanding on major factors related to financial vulnerability among individual especially in Malaysia. In addition, this study can be a platform and source of reference for others to propose an indicator to overcome the issues of financial vulnerability and reduce financial fragility.

Keywords: Psychology factor, financial vulnerability

INTRODUCTION

Global economic uncertainties in recent years have an adverse impact on many households and individuals across nations including Malaysian. It is due increasing of competitive business environment, tough labour market, high cost of living and firms

across various sectors have had to downsize their workforce (O'Connor et.al., 2019). These factors have undesirable impacts on financial vulnerability of Malaysians such as strain on household purchasing power, upsurge in the use of credit and debt and plausibly developing into other socio-economics adversities such as increased crime, poverty, and unemployment. Recognizing this financial hardship, over the years especially during the pandemic COVID-19 many agencies in Malaysia have continuously put efforts to uplift the issues related to financial vulnerability among its society. Malaysia government as a policy maker have paid close attention to overcome these challenges, particularly for low-income households (denoted as the bottom 40% or B40 group) and middle-income households (denoted as the middle 40% or M40 group), as these two income groups account for a major 80% of total households in Malaysia (Mahdzan et al., 2020). Numerous initiatives to increase knowledge, skills and educational attainment have also been implemented in efforts to improve the livelihood of these segments of society.

Financial vulnerability is defined as the risk of an individual entering difficulty for example being unable to sustain their level of life rather than living in a state of poverty or necessity. According to Anderloni et al., (2012) and Clercq et al., (2015) financial vulnerability refers to situation in which individuals are not able to sustain their expenses, unforeseen expenses cannot be met, and debts or real household net wealth decrease to the income ratio. Besides, financial vulnerability (FV) is often considered a problem affecting the individual's financial stability and, in many cases, they do not even know they are financially vulnerable due to differences in feelings, beliefs, values, habit and preferences.

For example, 74% of Americans report that they are financially stable, however most of them do not have enough funds to deals with unforeseen disaster while maintaining their living standards (Pew Charitable Trusts, 2017; Federal Reserve, 2018). In addition, Malaysia public employees typically spend more than half or 52% of their salaries on debt repayment, which is 20% higher than the national average (Bank Negara Malaysia, 2018). Consequently, this will inevitably leave them with a limited financial buffer against any income shocks.

An increasing body of research in the subject of behavioural economics reveals that individual financial decisions are influenced not just by socioeconomic circumstances, but also by psychological issues (Anderloni et.al., 2012). These

psychological elements may cause people to act in ways that contradict standard economic rationale (Meier and Sprenger, 2010). There are many internal and external factors affecting financial behaviour of individuals. Currently, a diverse body of literature related to financial vulnerability exists across different research domains including economic and marketing. Besides, extent researcher also suggests there several individual factors that contribute to one's financial vulnerability. Hoffmann & McNair (2019) measured financial vulnerability for the US consumers using psychological characteristics to understand the relationship between financial vulnerability and financial outcomes. The relationship between positive and negative financial outcomes is used to determine financial vulnerability.

Therefore, this study will determine the psychological factors influence on financial vulnerability. Previous research mainly focusses on issues of financial vulnerability among household in developed countries whereas little work has been done in the context of developing countries such as Malaysia (Magli et a., 2020).

METHODOLOGY

This study employs content analysis where an inductive strategy is used in tracking and gathering relevant materials related to psychological factors and financial vulnerability. The information obtained is from various sources such as books, journals, articles newspapers and magazines. This information is collected and screened and analyzed using contents analysis. Content analysis resulted when the researcher had the goal of conducting a literature review. By analyzing the opinions of scholars, researchers, as well as reporters in disseminating information the analytical approach was used to develop understanding on factors of psychological factors and it influence on financial vulnerability.

LITERATURE REVIEW ON PSYCHOLOGICAL FACTORS

Psychological factors are used to provide answers in situations where an individual's plan under a climate of uncertainty without knowing the expected outcome, he may derive from the decision have been made. Reflecting financial vulnerability and psychological characteristics are intertwined, which lead to a direct impact upon one another. According to Mcree and John (1992), psychology characteristic relatively as a permanent form of individual thoughts, emotions, motives and behaviour. According to Starkey, Keane, Terry, Marx, & Ricci, (2013), financial vulnerability refers to the

cognitive, emotional, and behavioural responses to the experience of economic hardship that happens when real costs surpass income, and one is not able to meet their financial responsibilities.

Researchers started to focus on the relation between psychological factors and financial well-being after scholars realized that financial well-being (vulnerable or not vulnerable) is frequently, strongly linked with stable personality of individuals. It involves four major elements which are locus of control, instant gratification, social norms and materialism (Refer to Figure 1).

Locus of control is a psychological concept that refers to how strongly people believe they have control over the situations and experiences that affect their lives (McCormack and Cotter, 2013). Individuals are said to have an internal locus of control when they believe they can control and, if necessary, change workplace events and environment. They feel that what happens to them is the result of their own actions, behaviour or attitudes, and that it is within their power to make changes. In contrast, individuals are said to have a locus of control that is external when they believe that forces or powers outside or beyond themselves are in control of their future and environment which also involve financial capability (Mohammad Fazli Sabri et al. 2021).

Instant gratification is the desire to experience pleasure or fulfilment without delay or deferment. Basically, it's when you want it; and you want it now. This is a classic study in psychology referring to the experimental of giving the choice to children of having 1 marshmallow now or getting 2 marshmallows after an hour (Luo and Pattanakul, 2020). Instant gratification or delay gratification affect the decision making of consumers and will have positive and negative consequences as a result to financial status.

Social norms are regarded as collective representations of acceptable group conduct as well as individual perceptions of particular group conduct. They can be viewed as cultural products (including values, customs, and traditions) which represent individuals' basic knowledge of what others do and think that they should do. For example, differences in cultural context can influence economic outcomes, including people's financial status and behaviour, largely through socioeconomic background,

financial socialization, risk preference, and attitudes towards money (Brown et al., 2018; Falk et al., 2018)

In addition, materialism is about values and desire for money, possessions, and the like (Dittmar et al., 2014). Materialism is a post-modern culture which perceived that consumption status is power and an indicator of life success. Materialistic people are less happy, more likely to spend money, more likely to show a favourable outlook about borrowing money for luxury purchases, and more likely to be compulsive buyers.

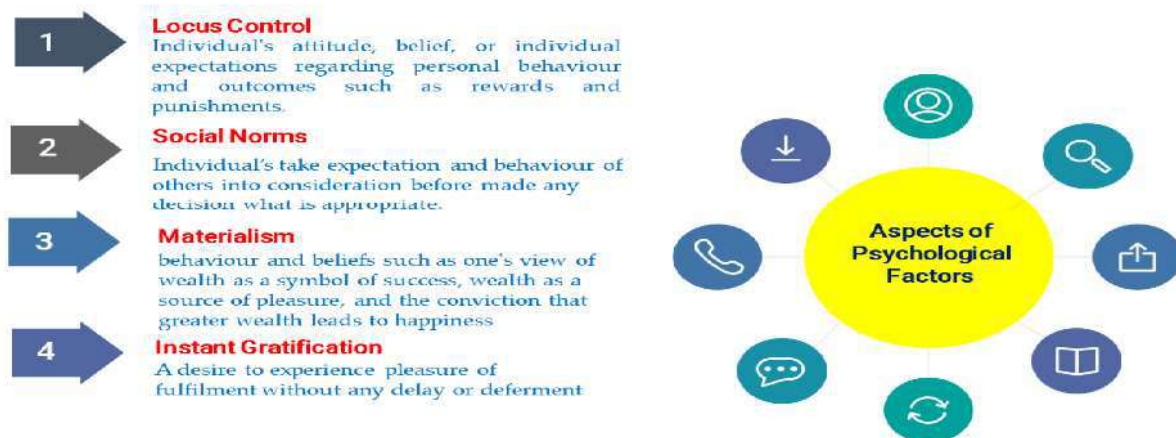


Figure 1: Elements of Psychological Characteristics

RESEARCH FRAMEWORK

A research study between China and South Africa focus on the linkage between locus of control and financial vulnerability. There is correlation between locus of control, and it became as determinants factor towards economic and financial problems (Mohammad Fazli Sabri et al., 2021). Highest level of locus of control identifies progressively towards beneficial financial outcome. In addition, Faizah and Hashim (2013) showed that there is correlation between locus of control on economic problems among household. On the other hand, a study was conducted by Sabri et al., (2012) and Sharif and Naghavi, (2020) agreed that people in Malaysia tend to acquire financial status (vulnerable or not) and mould their financial behaviour through social norms and financial socialization agents, such as family, friends, or even religion. Materialism culture in Malaysia is found to be significant in younger generations nowadays whereby people have been competing to be trendsetters resulting them falling in debts trap should the maladaptive behaviours gone uncontrolled. The financial vulnerability is often incurred due to unwise

borrowing choice, which causes households unable to cope with debts given their current and future level of their life satisfaction (Loke, 2017). Households who are financially vulnerable tend to engage in suboptimal financial choices upon their own instant needs and they face greater risk of suffering financially (Hoffmann and McNair, 2018).

According to Loke (2017), 51.7% of Malaysian were reported to demonstrate moderate level of financial vulnerability, 15.2% were highly financial vulnerable and 33.1% were possessed low level of financial vulnerability. It reflects the personal behaviour of individual as one of determinant factors towards the issues of financial vulnerability.

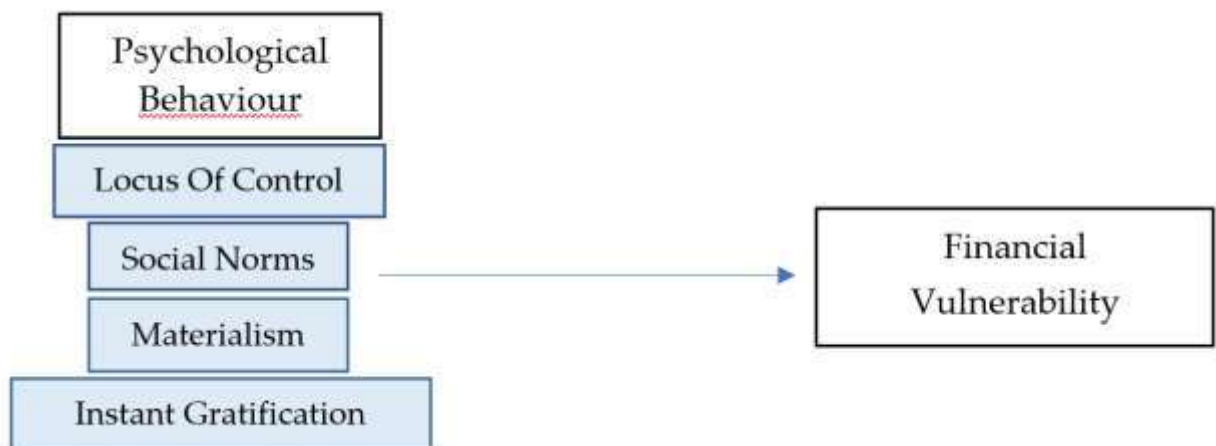
Based on literature, the following hypotheses were developed. In particular, the paper proposes a model that examines impact of psychological behaviour on financial vulnerability.

H1: Locus of Control influence financial vulnerability

H2: Social Norms influence financial vulnerability

H3: Materialism influence financial vulnerability

H4: Instant Gratification influence financial vulnerability



These variables are eventually related to financial vulnerability. The research model for this study can be explained based on Bandura's Self Efficacy Theory (1977), which

suggests that a person's confidence in their proficiency for carrying out specific tasks is called self-effectiveness which related to the elements of psychological behaviour such as locus of control, social norms, materialism, and instant gratification affecting financial vulnerability.

CONCLUSION AND FUTURE RESEARCH

Previous researchers have highlighted the impacts of financial behaviour, self-belief and financial attitudes. This research on the other hand, attempt to provide insight into these facets, thus providing psychological variables as these elements may closely correlate a person's feeling, particularly, with the sense of money management. It is predicted that these elements will be significantly influence on financial vulnerability. the current economic challenges faced by Malaysian household have attracted special attention from researcher, policy makers and academics. There is a potential benefit of this research. Firstly, the main thrust of this study is to explore the factors influence financial vulnerability among individuals which expected finding will allows people to improve their personal quality and virtuous financial factors. Second, this study will provide numerous key understanding and implications of psychological behaviour towards financial vulnerability. Thus, psychological behaviour in undoubtedly an important contributor towards individual journey in determine the success of failure in dealing with financial status and aspects. Perhaps by applying a good and proper element of psychological behaviour throughout life will lead and generate a better financial management behaviour. Third this research could identify the impacts of psychological behaviour on financial vulnerability based on demographic characteristics such as level of income. By identifying this, government and other agencies will be able to implement intervention programs geared towards ensuring better focus on managing financial administrative tasks among respective groups to minimize their financial vulnerability.

This research could also be expanded to include other psychological variables as they may closely correlate a person's feeling, particularly, with the sense of money management. It would be interesting to understand which dimensions are more significant in this research area.

REFERENCE

- Anderloni, L., Bacchiocchi, E., & Vandone, D. (2012). Household financial vulnerability: An empirical analysis. *Research in Economics*, 66(3), 284-296
- Bandura, A., & Adams, N. E. (1977). Analysis of self-efficacy theory of behavioral change. *Cognitive therapy and research*, 1(4), 287-310.
- Bank Negara Malaysia. (2018). *The financial stability and payment systems report 2018*. Government Printing Office.
- Brown, M., Henchoz, C. and Spycher, T. (2018). Culture and financial literacy: Evidence from a within-country language border. *Journal of Economic Behavior & Organization*, 150, pp. 62-85
- Clercq, B., van Tonder, J. A., & van Aardt, C. J. (2015). Consumer financial vulnerability: Identifying transmission linkages that could give rise to higher levels of consumer financial vulnerability. *Southern African Business Review*, 19(1), 112-136.
- Faizah, G., & Hashim, H. B. (2013). Challenges and locus control among single mothers in Muar, Johor. *Journal of Emerging Trends in Educational Research and Policy Studies*, 4(5), 760-765.
- Falk, A., Becker, A., Dohmen, T., Enke, B., Huffman, D. and Sunde, U. (2018). Global evidence on economic preferences. *The Quarterly Journal of Economics*, 133(4), 1645-1692
- Dittmar, H., Bond, R., Hurst, M., & Kasser, T. (2014). The relationship between materialism and personal well-being: A meta-analysis. *Journal of personality and social psychology*, 107(5), 879.
- Hoffmann, A. O., & McNair, S. J. (2019). How does consumers' financial vulnerability relate to positive and negative financial outcomes? The mediating role of individual psychological characteristics. *Journal of Consumer Affairs*, 53(4), 1630-1673.
- Loke, Yiing Jia (2017) : *Financial vulnerability of working adults in Malaysia*, *Contemporary Economics*, University of Finance and Management in Warsaw, Faculty of Management and Finance, Warsaw, Vol. 11 (2), 205-218,
- Luo, Y., & Pattanakul, D. (2020). Infant expectations of instant or delayed gratification. *Scientific Reports*, 10(1), 1-7.
- Magli, A. S., Sabri, M. F., & Rahim, H. A. (2020). The influence of financial attitude, financial behaviour, and self-belief towards financial vulnerability among public employees in Malaysia. *Malaysian Journal of Consumer and Family Economics*, 25, 175-193.

- Mahdzan, N. S., Zainudin, R., Abd Sukor, M. E., Zainir, F., & Ahmad, W. M. W. (2020). An exploratory study of financial well-being among Malaysian households. *Journal of Asian Business and Economic Studies*.
- McCormack, N., & Cotter, C. (2013). *Managing burnout in the workplace: A guide for information professionals*. Elsevier.
- Mohamad Fazli Sabri, Thinagaran Moga Dass, Nik Ahmad Sufian Burhan, Husniyah Abdul Rahim Abdul Wahab, Rusitha Wijekoon, & Megawati Simanjuntak. (2021). Determinants of Life Satisfaction among Female-Headed Households in Malaysia. *International Journal of Business and Society*, 22(1), 276-295.
- O'Connor, G. E., Newmeyer, C. E., Wong, N. Y. C., Bayuk, J. B., Cook, L. A., Komarova, Y. & Warmath, D. (2019). Conceptualizing the multiple dimensions of consumer financial vulnerability. *Journal of Business Research*, 100, 421-430.
- Sabri, M. F., Cook, C. C. and Gudmunson, C. G. (2012). Financial well-being of Malaysian college students. *Asian Education and Development Studies*, 1(2), pp. 153-170.
- Starkey, A. J., Keane, C. R., Terry, M. A., Marx, J. H., & Ricci, E. M. (2013). Financial distress and depressive symptoms among African American Women: identifying financial priorities and needs and why it matters for mental health. *Journal of Urban Health*, 90(1), 83-100. doi:10.1007/s11524-012-9755-x.
- Magli., S.A., Sabri., F.M., Abdul Rahim., H. 2020. The Influence of Financial Attitude, Financial Behaviour, and Self-Belief towards Financial Vulnerability among Public Employees in Malaysia. *Malaysian Journal of Consumer and Family Economics*, 25, 175-193.
- Maccarrone-Eaglen, A., & Schofield, P. (2017). Compulsive buying behavior: Re-evaluating its dimensions and screening. *Journal of Consumer Behaviour*, 16(5), 463-473.
- Meier, S., & Sprenger, C. (2010). Present-biased preferences and credit card borrowing. *American Economic Journal: Applied Economics*, 2(1), 193-210.
- Sabri, M. F., Aw, E. C. X., Abdul Rahim, H., Burhan, N. A. S., Othman, M. A., & Simanjuntak, M. E. G. A. W. A. T. I. (2021). Financial literacy, behavior and vulnerability among Malaysia households: Does gender matter. *International Journal of Economics & Management*, 15(2), 241-256.
- Starkey, A. J., Keane, C. R., Terry, M. A., Marx, J. H., & Ricci, E. M. (2013). Financial distress and depressive symptoms among African American women: identifying financial priorities and needs and why it matters for mental health. *Journal of Urban Health*, 90(1), 83-100.