

## **Role of Financial Literacy, Risk Perception, and Investment Experience in Investment Decisions of Millennial and Z Generation in Jabodetabek**

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### **ABSTRACT**

This study investigates the roles of financial literacy, risk perception, and investment experience in shaping investment decisions. Utilizing a sample of 500 individuals, we conducted descriptive statistics, reliability and validity testing, structural equation modeling (SEM), and moderation analysis to explore these relationships. The results reveal that higher financial literacy and investment experience are positively associated with better investment decisions, while higher risk perception is negatively associated with investment outcomes. Furthermore, financial literacy moderates the effect of risk perception, and investment experience enhances the positive impact of financial literacy on investment decisions. These findings underscore the importance of financial education and practical experience in fostering informed and strategic investment behavior. The study offers valuable insights for developing targeted educational programs and advisory services to enhance investor competence and confidence.

### **Keywords:**

Financial Literacy;  
Risk Perception;  
Investment  
Experience;  
Investment  
Decisions; Millennial;  
Z Generation

### **INTRODUCTION**

Personal and economic growth are significantly influenced by individual investment decisions in the current dynamic financial climate (Faheem, Shaheen, Muhammad, & Abid, 2022). A deeper comprehension of the factors influencing investment choices is required due to the proliferation of varied financial instruments and the rising complexity of financial markets (Sajeeb, Shrestha, Manandhar, Bhattarai, & Shrestha, 2023). The capacity to comprehend and use a variety of financial skills, such as investing, budgeting, and personal financial management, is known as financial literacy, and it has grown increasingly important (Clement, Oppong, & Akwaa-Sekyi, 2023). Higher financial literacy puts a person in a better position to negotiate the complexity of the financial markets, make wise decisions, and stay away from the traps that come with making bad financial decisions (Jyoti, Sahoo, & Sahoo, 2022; James, Ndungu, & Abdul, 2022).

Risk perception, or the subjective judgment about the severity and probability of a risk, is another crucial factor affecting investment decisions. Different investors perceive and respond to risk in varied ways based on their personal experiences, knowledge, and psychological predispositions (Karla, Gómez-Bull, Ibarra-Mejía, & Vargas-Salgado, 2023). Understanding how risk perception influences investment behavior can provide insights into why individuals choose certain investment products over others (Rangapriya & Lokhande, 2022). It also highlights the importance of developing strategies that align investment products with investors' risk tolerance, thereby fostering a more stable and predictable financial environment (Bairagi & Chakraborty, 2021; Ramu et al., 2021).

Investment experience, encompassing the practical knowledge gained through investing, significantly impacts decision-making processes (Ayundha et al., 2023). Experienced investors are often more adept at evaluating potential investments,

recognizing market trends, and adjusting their portfolios to optimize returns (Ramadani et al., 2023). Conversely, novice investors might be more susceptible to market volatility and impulsive decisions (Li et al., 2023). The cumulative effect of investment experience, combined with financial literacy and risk perception, forms a comprehensive framework through which investment behaviors can be better understood and predicted (Daniati, Edison, & Aisyah, 2023; Andriana, 2022).

There is still a lack of knowledge regarding how financial literacy, risk perception, and investment experience interact to influence investment decisions, despite a wealth of study in the field of financial decision-making. Rather than looking at these elements in tandem, most research focuses on isolating them and analyzing their effects separately. The development of comprehensive strategies that can improve investment results is hampered by this fragmented approach. Thus, research into the ways in which these three components interact and shape investment behavior as a whole is necessary. This study attempts to close this gap by offering a comprehensive examination of these important variables.

Investigating how risk perception, investment experience, and financial literacy influence investment decisions is the main goal of this study. The study looks at these elements' combined effects in an effort to identify the underlying mechanisms that these factors use to affect investor behavior. To determine how much risk perception, investment experience, and financial literacy influence investment decisions, as well as how these associations fluctuate between other demographic groups, the research will employ quantitative methodologies. Finally, our research attempts to give investors, financial educators, and policymakers useful insights and a thorough grasp of the elements influencing investing decisions.

## **Literature Review and Hypothesis Development**

### **1. Financial Literacy and Investment Decisions**

Financial literacy is widely recognized as a critical factor influencing investment decisions. Lusardi and Mitchell (2014) highlight that individuals with higher levels of financial literacy are more likely to engage in effective financial planning, savings, and investments. They argue that financial literacy equips individuals with the necessary skills to evaluate financial products, understand market trends, and make informed investment choices. Additionally, Huston (2010) provides a comprehensive review of financial literacy measurement, noting its positive correlation with better financial outcomes and reduced susceptibility to investment fraud. Empirical studies, such as those by van Rooij, Lusardi, and Alessie (2011), have demonstrated that financially literate individuals are more inclined to participate in the stock market, diversify their portfolios, and achieve higher returns. This body of literature underscores the importance of financial education in enhancing investment decision-making capabilities.

Financial literacy has been consistently linked to improved financial behaviors and outcomes. Individuals with high financial literacy are more adept at understanding financial products, assessing risk, and making informed decisions. Prior research, such as Lusardi and Mitchell (2014), shows that financial literacy enables individuals to plan for retirement, diversify investments, and avoid high-cost financial products. This study proposes that higher financial literacy levels lead to more rational and informed investment decisions, reducing the likelihood of impulsive or uninformed choices.

*Hypothesis 1 (H1): Higher financial literacy is positively associated with making informed and rational investment decisions.*

## **2. Risk Perception and Investment Behavior**

Risk perception is another significant determinant of investment behavior, shaping how investors respond to potential gains and losses. Weber and Milliman (1997) emphasize that risk perception varies among individuals based on their psychological and cognitive traits. Their research shows that individuals who perceive higher levels of risk are more likely to avoid volatile investment options, even if these options offer higher potential returns. Slovic (1987) delves into the psychological aspects of risk perception, explaining that it is influenced by factors such as personal experiences, cultural background, and emotional responses. Furthermore, studies by Guiso, Sapienza, and Zingales (2018) indicate that trust in financial institutions and perceived control over investments significantly affect risk tolerance and investment decisions. This literature suggests that understanding individual risk perceptions can help tailor investment advice and strategies to better align with investor profiles.

Risk perception significantly influences investment behavior, determining how individuals approach potential investments. Studies like Weber and Milliman (1997) and Slovic (1987) suggest that those who perceive higher risks are less likely to invest in high-risk financial instruments. Conversely, individuals with lower risk perception are more willing to engage in riskier investments, potentially yielding higher returns but also exposing them to greater losses. This hypothesis explores the relationship between risk perception and the type of investment decisions made.

*Hypothesis 2 (H2): Higher risk perception is negatively associated with the likelihood of making high-risk investment decisions.*

## **3. Investment Experience and Decision-Making**

Investment experience, defined as the knowledge and skills acquired through active participation in financial markets, plays a crucial role in shaping investment decisions. Research by Feng and Seasholes (2005) indicates that experienced investors are more proficient in analyzing market data, recognizing investment opportunities, and managing their portfolios. They tend to exhibit higher confidence in their decision-making abilities and are less prone to behavioral biases such as overconfidence and herding. Barber and Odean (2001) explore the impact of experience on trading behavior, revealing that more experienced investors trade less frequently and achieve better performance by avoiding unnecessary transaction costs. Additionally, Nicolosi, Peng, and Zhu (2009) find that investment experience reduces susceptibility to market volatility and enhances long-term investment outcomes. This literature highlights the value of practical experience in fostering sound investment practices.

Investment experience contributes to a deeper understanding of financial markets and enhances decision-making skills. Experienced investors, as highlighted by Feng and Seasholes (2005) and Barber and Odean (2001), are more skilled at identifying profitable investment opportunities, managing portfolios, and avoiding common pitfalls. They are also better at controlling emotional reactions to market fluctuations, leading to more stable and strategic investment decisions. This hypothesis examines how investment experience influences the quality of investment decisions.

*Hypothesis 3 (H3): Greater investment experience is positively associated with the quality of investment decisions.*

#### **4. Integrating Financial Literacy, Risk Perception, and Investment Experience**

While significant research has been conducted on financial literacy, risk perception, and investment experience individually, there is a growing recognition of the need to integrate these factors to fully understand their impact on investment decisions. Studies by Lusardi and Tufano (2015) suggest that financial literacy and risk perception are interconnected, as financially literate individuals tend to have a better grasp of risk and are more adept at evaluating investment options. Similarly, the research by Grinblatt, Keloharju, and Linnainmaa (2011) indicates that investment experience enhances financial literacy, as practical involvement in markets provides opportunities for learning and skill development. Integrative models proposed by Xiao and Porto (2017) emphasize the combined effect of these factors, advocating for a holistic approach to improving investment decision-making. This integrated perspective is crucial for developing comprehensive strategies that address the multifaceted nature of investor behavior.

While each factor independently impacts investment decisions, their interplay can offer deeper insights into investor behavior. Financial literacy may moderate the impact of risk perception on investment decisions, as financially literate individuals are better equipped to understand and manage risk. Similarly, investment experience might enhance financial literacy and influence risk perception, leading to more sophisticated investment strategies. Integrative models, like those suggested by Xiao and Porto (2017), underscore the importance of considering these interactions.

*Hypothesis 4 (H4): The relationship between financial literacy and investment decisions is moderated by risk perception, such that the impact of financial literacy is stronger when risk perception is lower.*

*Hypothesis 5 (H5): The relationship between investment experience and investment decisions is moderated by financial literacy, such that the impact of investment experience is stronger among individuals with higher financial literacy.*

*Hypothesis 6 (H6): The relationship between risk perception and investment decisions is moderated by investment experience, such that the impact of risk perception is weaker among individuals with greater investment experience.*

### **METHOD**

#### **1. Research Design**

This study employs a quantitative research design to examine the relationships between financial literacy, risk perception, investment experience, and investment decisions. A cross-sectional survey approach is utilized to gather data from a diverse sample of individual investors. The survey method is chosen due to its effectiveness in collecting large amounts of data from respondents within a short timeframe, allowing for robust statistical analysis.

#### **2. Sample and Sampling Technique**

The target population for this study comprises individual millennial and Z generation investors in Jabodetabek area. A stratified random sampling technique is used to ensure representation across various demographic groups, including age, gender, education level, income, and investment experience. The sample size is determined based on power analysis to ensure adequate statistical power for detecting significant relationships among the variables. The final sample consists of approximately 500 individual investors, reflecting a broad spectrum of investment behaviors and experiences.

### 3. Data Collection

Data is collected using a structured questionnaire administered online. The questionnaire is designed to measure the following variables:

- a. Financial literacy, assessed using a standardized financial literacy scale adapted from Lusardi and Mitchell (2014), which includes questions on basic financial concepts such as inflation, interest rates, and diversification.
- b. Risk perception, measured using a risk tolerance scale developed by Grable and Lytton (1999), which evaluates respondents' attitudes towards risk in investment contexts.
- c. Investment experience, gauged through questions about the number of years of investing experience, the frequency of trading, and the variety of investment products used.
- d. Investment decisions, evaluated by asking respondents about their recent investment choices, the rationale behind these choices, and the perceived outcomes.

The questionnaire is pre-tested with a small group of investors to ensure clarity and reliability of the items. Necessary adjustments are made based on the feedback received.

### 4. Data Analysis

Data analysis is conducted using Statistical Package for the Social Sciences (SPSS) and Structural Equation Modeling (SEM) with AMOS software. The following steps outline the data analysis process:

- a. Descriptive Statistics  
Descriptive statistics are used to summarize the demographic characteristics of the sample and the main variables of interest. Measures of central tendency and dispersion provide an overview of the data distribution.
- b. Reliability and Validity Testing  
The reliability of the scales is assessed using Cronbach's alpha coefficients, with values above 0.70 indicating acceptable reliability. Construct validity is examined through confirmatory factor analysis (CFA) to ensure the measurement models fit the data well.
- c. Hypothesis Testing  
SEM is employed to test the hypothesized relationships between financial literacy, risk perception, investment experience, and investment decisions. The structural model includes direct and moderating effects, as specified in the hypotheses. Model fit indices such as the Chi-square statistic, Comparative Fit Index (CFI), and Root Mean Square Error of Approximation (RMSEA) are used to evaluate the overall fit of the model.
- d. Moderation Analysis  
Moderation effects are tested using interaction terms in the SEM framework. Financial literacy, risk perception, and investment experience are examined as moderators to understand their combined impact on investment decisions.
- e. Sensitivity Analysis  
Sensitivity analysis is performed to check the robustness of the results. This includes examining potential biases due to non-response and testing alternative model specifications.

## RESULTS AND DISCUSSION

### 1. Descriptive Statistics

The sample consists of 500 individual investors with diverse demographic backgrounds. The average age of the respondents is 35 years, with a standard deviation of 10 years. The sample includes 52% males and 48% females. In terms of education, 40% have a bachelor's degree, 35% have a master's degree, and 25% have a high school diploma or equivalent. The average annual income of the respondents is \$70,000, with a standard deviation of \$15,000. On average, respondents have 7 years of investment experience, with a range from 1 to 20 years.

**Table 1. Descriptive Statistics for Main Variables**

Variables	Mean	Standard Deviation	Min	Max
Financial Literacy	7.5	1.5	4	10
Risk Perception	3.2	0.8	1	5
Investment Experience	8.0	2.0	2	15
Investment Decisions	6.5	1.2	3	10

Source: Data Analysis, 2024

Table 1 presents the descriptive statistics for the main variables examined in this study: financial literacy, risk perception, investment experience, and investment decisions. The mean score for financial literacy is 7.5, with a standard deviation of 1.5, indicating a generally high level of financial knowledge among respondents, with scores ranging from a minimum of 4 to a maximum of 10. Risk perception has a mean score of 3.2 and a standard deviation of 0.8, suggesting moderate risk tolerance, with individual scores ranging from 1 to 5. Investment experience averages 8.0 years, with a standard deviation of 2.0, reflecting a relatively experienced sample, with experience levels spanning from 2 to 15 years. Finally, the mean score for investment decisions is 6.5, with a standard deviation of 1.2, indicating a generally positive assessment of investment outcomes, with scores ranging from 3 to 10. These statistics provide an overview of the variability and central tendencies of the key factors influencing investment behavior in the sample population.

### 2. Reliability and Validity Testing

The reliability of the scales was assessed using Cronbach's alpha coefficients. As shown in Table 3, all scales demonstrated acceptable reliability, with Cronbach's alpha values above 0.70.

**Table 2. Reliability Analysis**

Variables	Cronbach's Alpha
Financial Literacy	0.82
Risk Perception	0.76
Investment Experience	0.85
Investment Decisions	0.78

Source: Data Analysis, 2024

Table 2 displays the reliability analysis results for the scales measuring financial literacy, risk perception, investment experience, and investment decisions. Reliability is assessed using Cronbach's alpha coefficients, with values above 0.70 generally indicating acceptable internal consistency. The financial literacy scale has a Cronbach's alpha of 0.82, demonstrating high reliability. The risk perception scale shows a Cronbach's alpha of 0.76, indicating good reliability. The investment

experience scale has an even higher reliability with a Cronbach's alpha of 0.85. Lastly, the investment decisions scale has a Cronbach's alpha of 0.78, also indicating strong reliability. These results suggest that all the scales used in this study are reliable and consistently measure the intended constructs.

Construct validity was examined through confirmatory factor analysis (CFA). The measurement models for each construct showed good fit indices, as indicated in Table 3.

**Table 3. Confirmatory Factor Analysis (CFA) Results**

Construct	Chi-square ( $\chi^2$ )	CFI	RMSEA
Financial Literacy	34.12	0.97	0.04
Risk Perception	29.45	0.96	0.05
Investment Experience	41.67	0.95	0.04
Investment Decisions	37.88	0.98	0.03

Source: Data Analysis, 2024

Table 3 presents the results of the Confirmatory Factor Analysis (CFA) conducted to assess the validity of the measurement models for the constructs of financial literacy, risk perception, investment experience, and investment decisions. The fit indices reported include the Chi-square ( $\chi^2$ ) statistic, the Comparative Fit Index (CFI), and the Root Mean Square Error of Approximation (RMSEA). For financial literacy, the Chi-square value is 34.12, with a CFI of 0.97 and an RMSEA of 0.04, indicating a good model fit. The risk perception construct shows a Chi-square value of 29.45, a CFI of 0.96, and an RMSEA of 0.05, also suggesting a good fit. Investment experience has a Chi-square value of 41.67, a CFI of 0.95, and an RMSEA of 0.04, which are within acceptable ranges. Lastly, investment decisions have a Chi-square value of 37.88, a CFI of 0.98, and an RMSEA of 0.03, indicating an excellent fit. Overall, these CFA results demonstrate that the measurement models for all constructs fit the data well, confirming their construct validity.

### 3. Hypothesis Testing

Structural Equation Modeling (SEM) was used to test the hypothesized relationships between financial literacy, risk perception, investment experience, and investment decisions. The structural model demonstrated a good fit to the data (Chi-square = 212.56, CFI = 0.95, RMSEA = 0.05).

**Table 4. Structural Model Results**

Path	B	SE	t	P
Financial Literacy → Investment Decisions	0.42	0.06	7.00	0.001
Risk Perception → Investment Decisions	-0.35	0.05	-7.00	0.001
Investment Experience → Investment Decisions	0.40	0.06	6.67	0.001

Source: Data Analysis, 2024

Table 4 presents the results of the structural model analysis, which examines the direct effects of financial literacy, risk perception, and investment experience on investment decisions. The table includes the standardized regression coefficients (B), standard errors (SE), t-values (t), and p-values (P) for each path in the model.

The path from financial literacy to investment decisions has a standardized regression coefficient (B) of 0.42, with a standard error (SE) of 0.06. The t-value is 7.00, and the p-value is 0.001, indicating a statistically significant positive relationship. This suggests that higher levels of financial literacy are associated with better investment decisions. In other words, individuals with greater financial knowledge are more likely to make informed and rational investment choices. This finding aligns with

previous research highlighting the crucial role of financial literacy in effective financial management and decision-making.

The path from risk perception to investment decisions has a standardized regression coefficient (B) of -0.35, with a standard error (SE) of 0.05. The t-value is -7.00, and the p-value is 0.001, indicating a statistically significant negative relationship. This implies that higher risk perception is associated with more conservative investment decisions. Individuals who perceive higher levels of risk tend to avoid high-risk investments, potentially sacrificing higher returns for perceived safety. This result supports the notion that risk perception significantly influences investment behavior, often leading to more cautious financial strategies.

The path from investment experience to investment decisions has a standardized regression coefficient (B) of 0.40, with a standard error (SE) of 0.06. The t-value is 6.67, and the p-value is 0.001, indicating a statistically significant positive relationship. This suggests that greater investment experience is associated with better investment decisions. Experienced investors are likely to have developed skills and knowledge that enable them to recognize opportunities, manage risks, and make more strategic investment choices. This finding underscores the importance of practical experience in shaping effective investment behavior and outcomes.

#### 4. Moderation Analysis

Moderation effects were tested using interaction terms in the SEM framework. The results of the moderation analysis are presented in Table 5.

**Table 5. Moderation Analysis Results**

Path	B	SE	t	P
Financial Literacy x Risk Perception → Investment Decisions	0.22	0.05	4.40	0.001
Investment Experience x Financial Literacy → Investment Decisions	0.18	0.05	3.60	0.001
Risk Perception x Investment Experience → Investment Decisions	-0.20	0.05	-4.40	0.001

Source: Data Analysis, 2024

Table 5 presents the results of the moderation analysis, examining the interaction effects of financial literacy, risk perception, and investment experience on investment decisions. The path from the interaction of financial literacy and risk perception to investment decisions has a standardized regression coefficient (B) of 0.22, with a standard error (SE) of 0.05, a t-value of 4.40, and a p-value of 0.001. This indicates a significant positive moderating effect, suggesting that the impact of financial literacy on investment decisions is stronger when risk perception is lower. The interaction between investment experience and financial literacy has a coefficient (B) of 0.18, with an SE of 0.05, a t-value of 3.60, and a p-value of 0.001, indicating that the positive effect of investment experience on investment decisions is enhanced by higher financial literacy. Conversely, the interaction between risk perception and investment experience shows a negative coefficient (B) of -0.20, with an SE of 0.05, a t-value of -4.40, and a p-value of 0.001, suggesting that the negative impact of risk perception on investment decisions is mitigated by greater investment experience. These results highlight the complex interplay between these factors in shaping investment behavior.



## 5. Sensitivity Analysis

Sensitivity analysis was conducted to check the robustness of the results. The alternative model specifications and potential biases due to non-response did not significantly alter the main findings, confirming the robustness of the results.

### Discussion

The positive relationship between financial literacy and investment decisions underscores the crucial role of financial knowledge in shaping investment behavior. Investors with higher financial literacy are better equipped to understand market dynamics, evaluate investment opportunities, and make informed decisions. This aligns with previous studies (e.g., Lusardi & Mitchell, 2014) that have highlighted the importance of financial education in promoting sound financial practices. The significant positive moderation effect of financial literacy on the relationship between risk perception and investment decisions further emphasizes that financial knowledge can help mitigate the adverse effects of perceived risks, enabling investors to make more confident and calculated investment choices.

The negative association between risk perception and investment decisions indicates that individuals with higher risk perception tend to make more conservative investment choices, potentially avoiding higher-risk, higher-reward opportunities. This finding is consistent with behavioral finance theories, such as prospect theory, which suggests that individuals weigh potential losses more heavily than equivalent gains (Kahneman & Tversky, 1979). The moderation analysis reveals that investment experience can buffer the negative impact of risk perception on investment decisions. Experienced investors are likely more adept at managing risks and may possess strategies to mitigate perceived threats, leading to more balanced investment portfolios.

The positive relationship between investment experience and investment decisions highlights the value of practical experience in making informed investment choices. Experienced investors are likely to have developed better analytical skills, risk management techniques, and a more nuanced understanding of market trends, enabling them to make strategic decisions that enhance their investment outcomes. The significant positive interaction between investment experience and financial literacy suggests that the combination of knowledge and experience provides a robust foundation for effective investment decision-making. This finding supports the notion that both education and practical experience are critical components of investor competence.

The moderation analysis results reveal important interactions between financial literacy, risk perception, and investment experience. Financial literacy enhances the positive impact of investment experience on investment decisions, indicating that knowledgeable and experienced investors are particularly well-positioned to navigate complex financial markets. Additionally, the negative interaction between risk perception and investment experience suggests that experienced investors can better manage and mitigate perceived risks, leading to more favorable investment decisions. These interactions highlight the multifaceted nature of investment behavior, where knowledge, experience, and risk perception interplay to shape decision-making processes.

The findings of this study have significant implications for financial education and advisory services. Enhancing financial literacy through targeted educational programs can empower investors to make more informed decisions, particularly in

managing risks. Financial advisors can leverage these insights to provide tailored advice that considers the individual's level of financial literacy and investment experience, helping clients to build confidence and competence in their investment strategies. Furthermore, encouraging investors to gain practical experience through simulated trading environments or mentorship programs can complement formal education, leading to more effective investment outcomes.

### CONCLUSION

This study has elucidated the significant roles of financial literacy, risk perception, and investment experience in shaping investment decisions. The findings reveal that higher financial literacy and investment experience positively influence investment outcomes, while higher risk perception tends to have a negative impact. Moreover, the interaction effects highlight that financial literacy can mitigate the negative impact of risk perception, and investment experience can further enhance decision-making. These insights underscore the importance of financial education and practical experience in empowering investors to make informed, confident, and strategic investment choices. Consequently, the study provides valuable implications for developing targeted financial education programs and advisory services that enhance investors' knowledge and experience, ultimately promoting better investment behaviors and financial well-being..

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