Abstract

The relationship between behavioural characteristics (both rational and irrational measures) and capital structure determinants has been empirically validated. The study examines whether capital structure determinations by Indonesian publicly listed firms (Tbks) are influenced by the behavioural biases of overconfidence and optimism, with the underlying rationality frameworks being framed by relevant financial information and impacted by the demographic attributes of the decision-makers. Data are obtained from survey respondents as well as secondary data on financial reporting and stock prices of the sampled Tbks, and statistically analysed using partial least squares structural equation modelling, regressional and path analyses, to identify the indicators of causative dynamics within the hypothesised relationships. A comprehensive hypothesis modelling construction is introduced to include empirically validated capital structure determinants (market timing, profitability, tangibility, size and their impacts on stock price). This research finds that the managers of the sampled Tbks displayed the inherent behavioural traits of overconfidence and optimism with respect to their capital structure determinations. However, such behavioural variables are not statistically proven to significantly influence capital structure decision-making, and, hence, are not validated as capital structure determinants. In this research, the pecking order framework is revealed to have a significant framing effect on the capital structure decision-making by the management of the sampled Tbks. The demographic attributes and backgrounds of the sampled managers are revealed to be capital structure determinants but do not have a mediating or moderating influence on the modelled construct between behavioural variables and capital structure. This study finds that optimism, market timing and adjusted debt on market timing are not determinants of capital structure for Tbks, while overconfidence and the control variables firm profitability, firm’s asset tangibility and firm size are statistically validated as capital structure determinants. The less aggressive leveraged models adopted by the sampled Tbks may indicate that implemented good principles of corporate governance have played a role in preventing capital structure determinations skewed by managements' behavioural biases or psychological tendencies.

Key Words: overconfidence, optimism, behavioural bias, pecking order theory, demographic attributes, framing effects, capital structure determinants, Indonesian public firms.