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An Analysis of the Effects of Financial Literacy, Overconfidence Bias, and Herding Behavior on Investment Decisions Among Millennial and Gen Z Workers in Surabaya

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A B S T R A C T

This study aims to examine the influence of financial literacy, overconfidence bias, and herding behavior on investment decisions among Millennial and Generation Z workers in Surabaya. The research adopts a quantitative approach with an explanatory design to analyze the causal relationships between variables. Primary data were collected through a structured questionnaire distributed to 100 respondents selected using purposive sampling techniques. The results indicate that financial literacy has a positive and significant effect on investment decisions, suggesting that individuals with higher financial knowledge are more capable of making rational and informed investment choices. These findings highlight the importance of both rational and behavioral factors in influencing investment decisions. Financial literacy enhances individuals' ability to process financial information effectively, while herding behavior reflects the influence of social dynamics in investment activities. This study contributes to the behavioral finance literature by providing empirical evidence from an emerging market context and emphasizes the need for improving financial literacy among young workers.

INTRODUCTION

Investment is commonly acknowledged as a fundamental financial activity that involves allocating current resources to generate future profits. According to the Financial Services Authority (Otoritas Jasa Keuangan/OJK, 2024), investment is the placement of cash over time to earn profit, whether through asset ownership or securities. Similarly, Addinpujoartanto & Darmawan (2020)define investment as the utilization of current funds to meet future financial needs with the expectation of obtaining returns or capital gains. In line with the rapid development of capital markets and financial accessibility, investment has become an essential instrument for income management, particularly among workers.

In the capital market, stocks continue to be one of the most appealing investment vehicles. However, investment decisions are not solely rational; they are also impacted by psychological and behavioral aspects. Widarno et. al (2024) Emphasize that investment decisions are influenced by a combination of cognitive factors (financial literacy), psychological biases (overconfidence and herding tendency), and personal traits such as income and age. This viewpoint is consistent with behavioral finance theory, which claims that investors are frequently boundedly rational and prone to biases (Kahneman & Tversky, 1979).

Figure 1. Age Data of Investors in 2024

According to data from the Indonesian Central Securities Depository (KSEI), as shown in Figure 1.1, younger generations make up the majority of Indonesian investors. Generation Z accounts for 54.92% of total investors, while Millennials account for 24.41%, implying that these two cohorts account for over 80% of investors. This trend shows a huge growth in financial activity among young people. Nonetheless, prior research (Merter & Selim, 2025) indicates that such engagement should be accompanied by excellent analytical and financial planning skills. In practice, however, the rapid expansion of young investors is frequently not accompanied by proper financial literacy, resulting in poor decision-making (Fong & Mitchell, 2025).

Indeks	2019	2022
Literasi	38,03%	49,68%
Inklusi	76,19%	85,10%
Gap	38,16%	35,42%

Source: Financial Services Authority data processed by the author (2025)

Figure 2. Financial Literacy and Inclusion Index for 2019 and 2022

Financial literacy data support the disparity between participation and capability. According to Figure 1.2, the National Survey of Financial Literacy and Inclusion (SNLIK) reveals that Indonesia's financial literacy score is 49.68%, while financial inclusion is 85.10%. This huge disparity suggests that many people actively utilize financial services without a thorough comprehension of the goods, risks, and investment procedures. According to Safryani et al. (2020) a lack of financial literacy increases the possibility of making poor investing decisions, such as selecting the wrong asset, taking too much risk, and failing to diversify. Globally, Lusardi and Mitchell (2014) confirm that financial literacy is a significant predictor of healthy financial behavior and investment outcomes.

Surabaya was chosen as the research location because of its status as a major metropolitan metropolis with a thriving economic and investment climate. Unlike Jakarta, which tends to dominate investor asset concentration, Surabaya gives a more representative picture of urban economic activity. The city has a sizable workforce, with roughly 1.62 million workers and a labor force participation rate of 70.49%. Furthermore, OJK (2024) reported that stock transactions in Surabaya totaled IDR 13.16 trillion, showing robust participation in the capital market. These qualities make Surabaya a suitable location to study investment behavior among working people.

From a behavioral standpoint, psychological biases such as herding behavior and overconfidence bias are critical in financial decision-making. Herding behavior is frequently influenced by the Fear of Missing Out (FOMO), in which investors follow others to avoid missing potential rewards (Pratama & Nawangsari, 2025) . According to prospect theory (Kahneman & Tversky, 1979), such behavior reflects an attempt to minimize perceived risk and avoid regret by relying on collective decisions. Empirical studies (Adil & al, 2022) confirm that herding is prevalent among investors facing uncertainty, although some findings (Wijaya & al, 2024)indicate that its influence may not always be significant.

Furthermore, overconfidence bias refers to a person's tendency to overestimate their knowledge, skills, and predicting abilities (Barber & Odean, 2001). Overconfident investors are more likely to misjudge risks and engage in excessive trading, which can have a detrimental influence on investment success. While numerous studies (Mahmood & al, 2024) demonstrate a strong favorable effect of overconfidence on investment decisions, other studies produce conflicting results, emphasizing the need for additional research.

Ideally, smart investment decisions should be accompanied by adequate financial literacy. Financial literacy refers to the information, skills, and confidence that affect financial behavior and decision-making (OJK, 2024). In the context of the Theory of Planned Behavior (Ajzen, 1991), financial literacy serves as a form of perceived behavioral control that enables individuals to make informed decisions. Empirical evidence (Hidayat, 2024)suggests that individuals with higher financial literacy are better equipped to manage financial resources and make sound investment choices.

However, earlier research has yielded conflicting results on the effects of financial literacy, overconfidence bias, and herding tendency on investment

decisions. Some research discover significant beneficial associations, whereas others provide insignificant or contradicting results (Widarno & al, 2024).

Furthermore, most previous studies have mostly used students as research subjects. Students usually have limited financial resources and a variable income, which may not truly reflect real-world investment behavior. Workers, particularly Millennials and Generation Z, have a consistent income, greater financial responsibility, and are more exposed to economic constraints, making them a more relevant demographic for researching investment decisions.

This work adds to the behavioral finance literature in three ways. First, it combines logical elements (financial literacy) with behavioral biases (overconfidence and herding) into a single empirical model. Second, it focuses on working people rather than students, which gives a more accurate picture of investment behavior. Third, it provides empirical evidence from a developing market scenario that has been understudied in the previous literature.

THEORETICAL REVIEW

Theory of Planned Behavior

The Theory of Planned Behavior (TPB), developed by Ajzen (1991), is a popular framework for analyzing human behavior in certain settings. This theory builds on the Theory of Reasoned Action by including perceived behavioral control as an extra factor, allowing for improved prediction of behavior in situations where individuals lack complete volitional control. According to TPB, three major factors influence behavior: attitude toward the behavior, subjective norms, and perceived behavioral control.

Financial literacy has a significant impact on people's views about investment activities. Individuals with more financial understanding are more likely to see investing as helpful and manageable, resulting in more reasonable and optimistic attitudes. Furthermore, subjective norms are directly tied to social effects, notably herding behavior, in which people tend to emulate the acts and recommendations of others. Perceived behavioral control, on the other hand, is influenced by both financial literacy and psychological characteristics like overconfidence bias, as people evaluate their capacity to manage investment decisions based on their knowledge and self-perception.

Several empirical research support the use of TPB in financial decision-making. For example, Hidayat et al. (2024) discovered that financial literacy has a considerable impact on investment attitudes and behaviors. Similarly, research on young investors suggests that social influence and perceived control are important predictors of investment engagement. Based on theoretical explanations and empirical evidence, the following hypothesis is proposed:

H1: Financial literacy has a positive and considerable impact on investing decisions.

Prospect Theory

Kahneman and Tversky (1979) established Prospect Theory, which provides a behavioral framework for understanding risk and uncertainty in decision-making. Unlike classic economic theories that presume rational decision-making, prospect theory proposes that people evaluate outcomes in relation to a

reference point and exhibit loss aversion, which means that losses are perceived more strongly than similar benefits.

This theory is especially useful for describing behavioral biases in financial decision-making, such as overconfidence and swarming behavior. Overconfidence bias refers to people's tendency to overestimate their knowledge and forecasting ability, which can lead to excessive risk-taking and wrong evaluations of investment outcomes. Meanwhile, herding behavior arises when people rely on other people's actions to lessen ambiguity and avoid regret, especially in turbulent market environments.

Empirical investigations yield conflicting results about the significance of behavioral biases. Barber and Odean (2001) discovered that overconfident investors tend to trade excessively, resulting in lower performance. However, some studies, such as Ramashar et al. (2022), show that overconfidence does not always have a major impact on investment decisions. Similarly, multiple studies have demonstrated that herding behavior has a considerable impact on investment decisions (Salsabila & Arifin, 2024), while the results vary depending on the context and sample characteristics. Based on these theoretical and empirical considerations, we offer the following hypotheses:

H2: Overconfidence bias significantly influences investing decisions.

H3: Herd behavior has a big impact on investment decisions.

Financial Literacy and Investment Decision

Financial literacy is described as the capacity to understand and apply financial knowledge to effectively manage one's finances. According to Lusardi & Mitchell (2014), define financial literacy as knowledge of financial concepts such interest rates, inflation, risk diversification, and investment tools. It also requires the capacity to make intelligent decisions about saving, borrowing, and investing.

Financial literacy is a type of human capital that improves people's capacity to make sensible financial decisions and avoid costly mistakes. Individuals with more financial literacy are better equipped to assess risks, choose appropriate investment vehicles, and devise long-term financial strategy.

Previous research has repeatedly shown a positive influence of financial literacy on investment decisions. Jonathan & Pradana (2025)found that financial literacy significantly influences investment behavior, while Asfira et al. (2019) discovered that financial literacy increases risk tolerance, which in turn influences investment decisions.

Overconfidence Bias and Investment Decision

Overconfidence bias is the tendency for people to overestimate their knowledge, abilities, and forecast accuracy. In financial markets, overconfident investors believe they can outperform others, resulting in excessive trading and risk underestimating (Barber & Odean, 2001).

This bias is strongly related to prospect theory since it represents inaccurate risk perception and an overestimation of future gains. Overconfidence bias can emerge in a variety of ways, including overestimation, overplacement, and overprecision, all of which contribute to irrational investment decisions.

Empirical evidence on overconfidence bias is mixed. Some research (Budiman, 2021) show that overconfidence has a considerable favorable effect on investment decisions, whereas others find no significant association. This contradiction implies that the impact of overconfidence may vary depending on factors such as investor experience, market conditions, and financial understanding.

Herding Behavior and Investment Decision

Herding behavior refers to investors' tendency to mimic the acts of others rather than depending on their own information and analysis. This behavior is prevalent in financial markets, especially during times of uncertainty and insufficient information.

Prospect theory and social influence mechanisms both help to explain herding behavior. Investors may emulate others to eliminate uncertainty, avoid regret, and obtain psychological comfort. Furthermore, the quick dissemination of information via digital channels has increased the impact of herding behavior among younger investors.

Empirical research typically supports the importance of herding behavior in investment decisions. Adielyani and Mawardi (2020) and Farhan Abid Pratama and Nawangsari (2025) found that herding tendency had a favorable influence on investment decisions, particularly among young and inexperienced investors. However, some research provide contradictory results, implying that herding behavior may not always be the major cause.

METHODOLOGY

This study uses a quantitative research approach with an explanatory (causal) design to look into the impact of financial literacy, overconfidence bias, and herding behavior on investing decisions. The quantitative approach tests hypotheses using numerical data analysis, allowing for objective measurement and generalization of results. The explanatory approach is especially useful for investigating causal links between variables in a specific demographic context.

The study's demographic consists of Surabaya-based Millennial and Generation Z workers who actively participate in capital market investments. This group was chosen because it represents people who are financially independent and actively involved in real-world investment decisions. Because the precise population number is unknown, the sample size was calculated using the Lemeshow formula, with a 95% confidence level and 10% margin of error. Purposive sampling was used, with respondents chosen based on specified criteria such as being classed as workers (such as private employees, public personnel, or entrepreneurs), being between the ages of 18 and 40, and actively engaging in investing activities.

Primary data were obtained using a structured questionnaire with a Likert scale to assess respondents' views, attitudes, and behaviors regarding the study variables. This method converts subjective reactions into measurable data suited

for statistical analysis. To ensure validity and reliability, variable measurements were designed using recognized theoretical frameworks and previous empirical investigations.

The study focuses on one dependent variable, investment choice, and three independent variables: financial literacy, overconfidence bias, and herding tendency. Financial literacy is determined by an individual's awareness of essential financial concepts such as general financial knowledge, savings and borrowing, insurance, and investing. Overconfidence bias is measured using dimensions such as overestimation, overplacement, and overprecision, which represent people's inclination to overestimate their abilities and expertise.

Individuals' proclivity to mimic others' investment decisions, such as stock selection, trading conduct, and market trend responsiveness, is used to assess herding behavior. Meanwhile, investment decisions are operationalized using variables such as investment preference, analytical technique utilization, market signal responsiveness, and performance orientation.

Before hypothesis testing, many preliminary analyses were performed to guarantee the model's robustness. The instrument's validity was verified using Pearson correlation, while reliability was analyzed using Cronbach's Alpha to demonstrate internal consistency. In addition, standard assumption tests such as normality, multicollinearity, and heteroscedasticity were used to ensure that the regression model matched statistical assumptions.

Hypothesis testing was done utilizing both simultaneous and partial approaches. The F-test was used to investigate the combined influence of all independent variables on investment decisions, whilst the t-test was utilized to assess the individual effect of each independent variable. The coefficient of determination (R^2) was used to evaluate how well the independent factors explain the variation in investment decisions.

Overall, this methodological framework takes a systematic and rigorous approach to analyzing the impact of rational and behavioral factors on investment decision-making among Surabaya's Millennial and Generation Z workers, ensuring that the findings are both empirically valid and theoretically grounded.

RESULTS

This study examined data from 100 valid respondents chosen from a total of 128 disseminated questionnaires following data screening methods to assure compliance with the set criteria. The respondents were Surabaya-based Millennial and Generation Z workers who are active investors. The demographic characteristics of the respondents show a somewhat fair distribution in terms of gender, with female respondents slightly dominating (51%), while male respondents account for 49%. In terms of age, the bulk of respondents (51%) are

between the ages of 18 and 29, followed by those between the ages of 30 and 40 (49%), showing that the sample represents productive-age investors.

In terms of occupational background, the majority of respondents (47.6%) are private employees, followed by entrepreneurs (18.1%) and other occupations (21.9%), while civil servants and state-owned firm employees make up a smaller number. In terms of income, the majority of respondents (41%) earn between IDR 3-5 million, with those earning less than IDR 3 million (31.4%) and more than IDR 5 million (27.6%). These data indicate that respondents have sufficient financial resources to engage in investment activities.

To assure data quality, the measurement device utilized in this investigation was validated and tested for dependability. The validity test findings show that all questionnaire items have correlation coefficients (r-count) greater than the r-table value of 0.165, indicating that they are valid and capable of reliably measuring the target constructs. Table 1 presents an overview of the validity test results.

Table 1. Summary of Validity Test Results

Variable	Range of r-count	r-table	Result
Financial Literacy	0.516 – 0.583	0.165	Valid
Overconfidence Bias	0.594 – 0.735	0.165	Valid
Herding Behavior	0.430 – 0.644	0.165	Valid
Investment Decision	0.456 – 0.598	0.165	Valid

The results in Table 1 clearly show that all indicators match the validity criteria, indicating that the research instrument is suitable for additional statistical analysis.

Furthermore, reliability testing with Cronbach's Alpha reveals that all variables have values greater than 0.60, indicating a high level of internal consistency. The reliability test results are shown in Table 2.

Table 2. Reliability Test Results

Variable	Cronbach's Alpha	Result
Financial Literacy	0.748	Reliable
Overconfidence Bias	0.761	Reliable
Herding Behavior	0.809	Reliable
Investment Decision	0.643	Reliable

These findings confirm that the instrument used in this study is both valid and reliable, ensuring the credibility of the collected data.

Prior to regression analysis, conventional assumption tests were used to ensure that the model was suitable. The normality test with the Kolmogorov-Smirnov method yielded a significance value of 0.200, which is greater than 0.05, suggesting that the residual data is normally distributed. The multicollinearity test returns tolerance values more than 0.10 and Variance Inflation Factor (VIF) values less than 10, indicating that there is no multicollinearity problem. Furthermore, the heteroscedasticity test results show that all independent

variables have significance levels larger than 0.05, indicating that the model is free of heteroscedasticity concerns. These findings show that the regression model fits all classical assumptions and is suitable for future investigation. The findings of the multiple linear regression analysis are shown in Table 3.

Table 3. Multiple Linear Regression Results

Variable	Coefficient (B)	t-value	Sig.
Constant	11.124	4.506	0.000
Financial Literacy	0.504	5.445	0.000
Overconfidence Bias	-0.056	-0.799	0.426
Herding Behavior	0.331	3.361	0.001

Financial literacy positively impacts investment decisions, with a coefficient of 0.504 and a significance level of 0.000 (< 0.05). This means that increased financial literacy improves the quality of investing decisions. Herding behavior had a positive and significant effect, with a coefficient of 0.331 and a significance value of 0.001 (< 0.05). This suggests that those who are more influenced by others make more active investment decisions. In contrast, overconfidence bias has a negative but negligible effect on investment decisions, with a significance value of 0.426 (> 0.05), showing that this variable had no meaningful influence on investment decisions in this study.

Further analysis using the F-test yields a p-value of 0.000, showing that all independent factors had a significant effect on investment decisions. The coefficient of determination (R^2) is 0.333, indicating that financial literacy, overconfidence bias, and herding behavior explain 33.3% of the variation in investing decisions. The remaining 66.7% is impacted by variables not included in this study.

In conclusion, the findings show that financial literacy and herding behavior are significant predictors of investment decisions among Millennial and Generation Z workers, whereas overconfidence bias has no statistically significant effect.

DISCUSSION

This study's findings provide a thorough knowledge of how rational and behavioral factors influence investing decisions, particularly among young workers in emerging markets. The strong impact of financial literacy on investing decisions emphasizes the role of cognitive competence in affecting financial behavior. Individuals with a higher level of financial literacy are better able to understand financial products, assess risks, and make sound investment decisions. This conclusion lends substantial support to the Theory of Planned Behavior (Ajzen, 1991), particularly in terms of perceived behavioral control, which states that persons with enough knowledge and abilities are more confident in their capacity to undertake productive financial actions.

Furthermore, this finding is similar with the findings of Lusardi and Mitchell (2014), who state that financial literacy is an important predictor of financial well-being and investment engagement. More recent studies, such as

Hidayat et al. (2024) and Putri and Munari (2024), have confirmed that people with higher financial literacy make more reasonable and organized investing decisions. From a behavioral finance standpoint, financial literacy can lessen the influence of cognitive biases by allowing people to rely on objective knowledge rather than emotions or conjecture (OECD, 2020).

However, the negligible effect of overconfidence bias shows that respondents in this study do not have excessive confidence in their investment ability, or that such trust is controlled by other factors. This research suggests that investment decisions are impacted by both logical evaluation and external circumstances, rather than just subjective impressions of ability. According to Prospect Theory (Kahneman & Tversky, 1979), when confronted with prospective losses, people tend to be risk-averse, which may reduce the impact of overconfidence. In other words, even if people are confident, the fear of loss may cause them to be more cautious. This finding is consistent with other research such as Ramashar et al. (2022) and Silalahi et al. (2023), which found that overconfidence does not always have a substantial impact on investing decisions, especially among investors who are still growing their experience and knowledge. Furthermore, Statman (2014) contends that behavioral biases do not function in isolation, but rather in conjunction with other cognitive and contextual factors, which may explain the modest effect of overconfidence in this study.

Herding conduct, on the other hand, has been shown to have a considerable beneficial effect on investment decisions, highlighting the importance of social variables in financial decision-making. This research implies that when making financial decisions, people tend to rely on the actions and opinions of others, especially in situations with uncertainty and limited information. This finding lends credence to the Theory of Planned Behavior's subjective norm component, which holds that social pressure and collective behavior influence individuals.

According to Prospect Theory, herding behavior is a method for reducing uncertainty and avoiding regret. Investors may believe following the majority to be a safer option, even if it is not supported by basic analysis. This data is consistent with Bikhchandani and Sharma's (2001) argument that herding behavior is widespread in financial markets, particularly during times of uncertainty.

Recent empirical research back up this finding. Salsabila and Arifin (2024) and Krishna et al. (2025) show that herding behavior has a major impact on investing decisions among young investors, especially in the setting of social media and digital information flow.

Overall, the findings of this study show that investing decisions are influenced by both rational and behavioral aspects. Financial literacy represents the intellectual dimension that improves decision-making quality, whereas herding behavior represents the social dimension that motivates collective decision-making. The minor contribution of overconfidence bias indicates that not all behavioral factors have equal importance, emphasizing the complexities of investor behavior.

These findings add to the increasing body of literature in behavioral finance by presenting empirical evidence from an emerging market setting, specifically among Millennial and Generation Z workers. The study underlines the need of

improving financial literacy and addressing behavioral characteristics that may influence investment decisions.

CONCLUSIONS AND RECOMMENDATIONS

The purpose of this study is to look at how financial literacy, overconfidence bias, and herding behavior affect investing decisions among Surabaya's Millennial and Generation Z workers. According to the findings of the empirical investigation, financial literacy and herding tendency play important roles in affecting investing decisions, although overconfidence bias has no statistically significant impact.

Financial literacy has been shown to have a positive and significant impact on investment decisions, implying that those with a higher level of financial understanding are better equipped to make logical, educated, and structured investment decisions. This research emphasizes the significance of financial literacy as a critical factor in increasing the quality of investing decisions. Individuals who grasp financial concepts like risk, return, and diversification are better able to assess investment opportunities and avoid speculative or irrational behavior.

In contrast, overconfidence bias has no substantial effect on investing decisions. This shows that the respondents in this study have a generally balanced view of their talents, and that confidence does not always lead to biased or unreasonable investment behavior. The lack of a meaningful effect suggests that investment decisions are influenced by a variety of factors rather than merely on individual confidence.

Meanwhile, herding behavior has been shown to have a positive and significant impact on investment decisions, implying that social influence is crucial in determining investor behavior. When faced with ambiguity, people tend to look to the actions and decisions of others for guidance when making financial decisions. This research demonstrates that investment decisions are impacted by both social and psychological variables, as well as rational analysis.

From an implementation standpoint, the findings of this study have significant consequences for a variety of stakeholders. For policymakers and financial institutions, the findings highlight the importance of strengthening financial literacy initiatives, particularly those aimed at young workers, to increase their capacity to make sound financial decisions. Educational programs, financial training, and easily accessible financial information are critical to improving people's understanding of investing and lowering the risk of poor financial behavior.

For investors, This study emphasizes the necessity of gaining financial knowledge and critical thinking abilities in investing decision-making, particularly for individuals who are Millennials or Generation Z. Investors are advised to focus on basic analysis and trustworthy financial data rather than just on market movements or societal influence. At the same time, awareness of behavioral biases is required to avoid making irrational judgments that could harm investment performance.

Furthermore, for academics and future scholars, this study provides a foundation for further research into behavioral finance in emerging market environments. Future studies should broaden the area of research by considering new variables such as risk tolerance, financial technology, and emotional elements, as well as using mixed-method approaches to acquire a better understanding of investor behavior.

Despite its contributions, this study has some limitations, including the use of self-reported questionnaire data and a sample size restricted to a narrow geographic area. Future research is intended to include a larger and more varied sample to improve the generalizability of the findings.

Overall, this study advances our understanding of investment behavior by demonstrating that both rational factors, such as financial literacy, and behavioral factors, such as herding behavior, have a significant impact on investment decisions, particularly among young workers in an emerging market environment.

FURTHER STUDY

Despite its merits, this study has some drawbacks that should be noted. First, the use of a self-administered questionnaire may induce response bias because the data is based on respondents' subjective judgments. Second, the sample is restricted to Millennial and Generation Z workers in Surabaya, which may limit the findings' applicability to larger populations or geographic contexts. Furthermore, the model only explains a significant amount of the variance in investment decisions, implying that other influential factors were not considered in this study.

Future research should broaden the reach by including a broader and more diverse sample from different places to improve generalizability. Furthermore, future research may examine incorporating additional variables such as risk tolerance, financial technology adoption, and emotional elements to gain a more complete picture of investment behavior. Mixed-method approaches, which combine quantitative and qualitative techniques, are also recommended for gaining deeper insights into the psychological and contextual aspects that influence investment decisions.

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