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JUDUL: PENENTU BAGI KERELAAN MENGAMBIL RISIKO ANTARA INDIVIDU DI KOTA KINABALU

IJAZAH: SARJANA PENGURUSAN PERNIAGAAN (MBA)

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DECLARATION

The materials in this dissertation are original except for quotations, excerpts, summaries and references, which have been duly acknowledged.

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ABSTRACT

The objective of this study is to examine the determinant of risk taking among individual when they decided to become a guarantor. Factors used to determine this dissertation of research are demography, socioeconomic and psychology. Demography factors consist of age, gender, marital status and education level while socioeconomic factors consist of income level and financial knowledge. Psychological factors consist of birth order, personality and risk perception. The sample for this study comprises of citizens in Kota Kinabalu. For the purpose of this study, self-designed and mostly adopted questions were used as the main research instrument in the questionnaires. This research had developed ten hypotheses. From the result of the analysis, it found that individuals in Kota Kinabalu are moderate when they confront of risk. Only gender and financial knowledge show relationship to willingness to take risk therefore theses two hypotheses were substantiated. This study hoping that the result and findings can create awareness about the willingness to take risk as a guarantor and can be used as additional inputs for creditors or practitioners to determine the factors influencing the willingness of taking risk.

ABSTRAK

PENENTU BAGI KERELAAN UNTUK MENGAMBIL RISIKO DI ANTARA INDIVIDU DI KOTA KINABALU

Objektif kajian ini adalah untuk menyelidik faktor yang mempengaruhi individu mengambil risiko apabila mereka menjadi penjamin. Faktor yang akan diuji dalam kajian ini adalah demografi, sosioekonomik dan psikologi. Faktor demografi terdiri daripada umur, jantina, status perkahwinan dan tahap pendidikan manakala faktor sosioekonomik pula terdiri daripada pendapatan dan pengetahuan mengenai kewangan. Faktor psikologi terdiri daripada urutan kelahiran, keperibadian dan persepsi risiko. Sample kajian ini adalah terdiri daripada penduduk di sekitar Kota Kinabalu. Kajian soal selidik digunakan sebagai instrument kajian. Sebanyak sepuluh hipotesis telah dibentuk. Daripada keputusan yang dianalisa, penduduk Kota Kinabalu adalah golongan sederhana semasa berhadapan dengan risiko. Didapati hanya jantina dan pengetahuan mengenai kewangan mempunyai hubungan dengan kerelaan mengambil risiko maka kedua-dua hipotesis ini dapat disokong. Kajian ini diharap dapat memberi kesedaran kepada orang awam mengenai faktor yang mempengaruhi individu mengambil risiko dan sebagai input tambahan kepada pemberi pinjaman untuk menentukan faktor yang mempengaruhi individu mengambil risiko.

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CHAPTER 1

INTRODUCTION

1.1 Overview

Normally people are risk averse and try to avoid risk if possible. Individuals are more likely to be strongly risk averse (Cowen Tyler, Glazer Amihai, 2003). According to Bauneister & Scher (1988), individuals will only engage in risk-taking behaviours when the possibility of a negative outcome is perceived to be minimal or the potential gain is perceived to be great.

According to Sabah Senior Assistant Official Assignee Kamin Kusaran, out of the number 6,168, 50% are loan guarantors, 20% defaulting credit card holders and about 30% are borrowers under the hire-purchase, personal loan, study loan and other loan schemes. (*Source: Daily Express, 30 June 2003*)

For instance, Malaysian Olympic chief Tunku Imran Tunku Jaafar (grandson of Malaysia's first constitutional monarch Tunku Abdul Rahman), was a guarantor for a company that owed Boult Wade Tennant (BWT) money has been declared bankrupt. The High Court's Bankruptcy Division moved to declare Tunku Imran bankrupt after he failed to settle a RM154, 742 (S $69,000) debts with British-based patent lawyers BWT. *(Source: Straits Times, 16 September 2005)*

On 21 May 1979, Esah Abdul Ghani (surety) became a guarantor for a loan of $16,000 granted by the Bank Bumiputra Malaysia Berhad (BBMB) to Mohammad Yusoff Ibrahim (borrower). As security the bank also held a charge over two properties EMR 877 Lot 937 & EMR 878 Lot 939 in Luit, Pekan belonging to the principal debtor and two others namely Alias Ibrahim and Rokiah Ibrahim. The two pieces of land were valued at $21,500 on 4 Jan 1979. It is one of the cases happened in Malaysia where the principal failed to pay and the bankruptcy notice was issued calling on the surety to pay the amount owning. (*Source: Federal Court of Malaysia, 10 June 1985)*

References was made to Ng Yik Seng versus Perwira Habib Bank Malaysia Berhad (1980) 2 MLJ 83. There the respondent granted on overdraft to a company. The two appellants and two other directors stood as guarantors in their personal capacities. When the demand was not repaid the responded sued the guarantors. Subsequently, the respondent applied for summary judgement against the two appellants who denied executing the guarantee. (*Source: Federal Court of Malaysia, 10 June 1985)*

Tow Kong Liang nominated Harvey International Limited (Harvey), his investment holding company incorporated in the British Virgin Islands to take up the facility. Nomura Singapore Limited sued Tow and Harvey in the High Court in Singapore in 1998 obtained judgement for the sum of RM 14,294,605 and interest thereon. (*Source: Makhamah Rayuan Malaysia, Rayuan Sivil No. W-02-906-2001)*

When people take risk it must have return associated with. For this study, becoming a guarantor does not have any potential gain and the risk is equally same with the borrower. People who are leverage or borrow money mean taking risk. In other word, people who take risk and do not border about return are those people with high risk tolerance. But why the percentage of guarantor is consist of 50% of the bankruptcy cases? Does it mean that Kota Kinabalu citizens are mostly risk takers? Are we saying that majority people in Kota Kinabalu like risk? If so, what is affecting them to take that kind of risk?

In business, financial leverage is related to the extent to which a firm relies on debt. The more debt a firm has, the more likely it is that the firm will become unable to fulfill its contractual obligations. In other words, too much debt will lead to higher probability of insolvency and financial distress. On the positive side, debt is an important form of financing, and provides a significant tax advantage because interest payments are tax deductible. If a firm uses debt, creditors and equity investors may have conflicts of interest. Leverage has been popularized to mean the use of special force and effects to produce more than normal results from a given course of action.

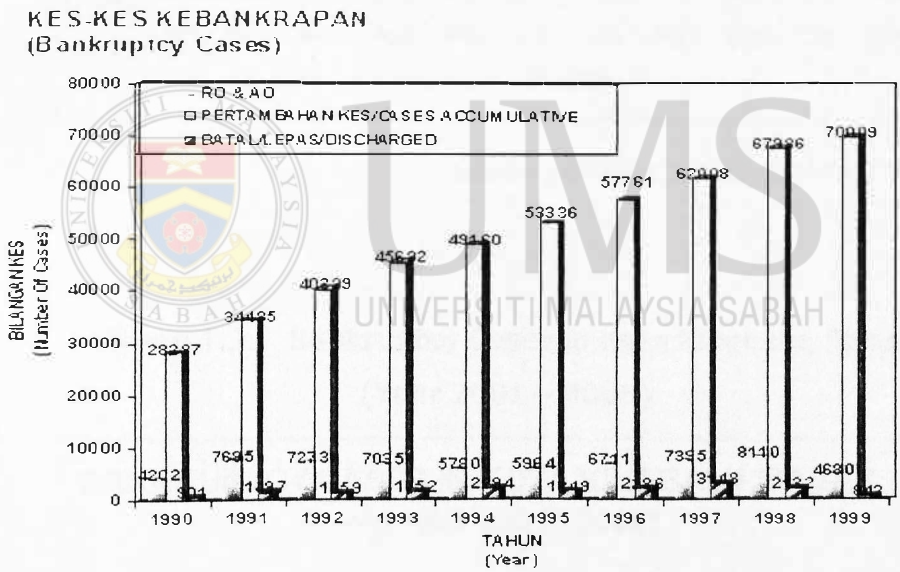
Borrower somehow will share the risk with guarantor during the application of loan. In legal term, a guarantor is a person who has been requested by the hirer to guarantee to the owner the performance of his obligations under the certain agreements. Lenders don't make money unless their loans are paid back. So a lender will want to do everything possible to make sure a loan is repaid even if the borrower defaults. A very effective way to do this is to require as a condition to making the loan that one or more persons guarantee the obligation. Guaranteeing a loan is agreeing to put his or her personal assets to pay back the loan if the borrower fails to do so.

Even if there's collateral for the loan, a lender may still not be able to get enough money on a foreclosure to pay off the loan. And lenders don't like foreclosures, because they can be time consuming, difficult and expensive. So a lender may insist on a personal guarantee from someone else in addition to the borrower, someone who would be a better source of recovery if the borrower defaults.

Another common situation where a guarantee will be required is with a loan to a small business that has been organized as a corporation or some other type of legal entity that protects owners from liability (for example, a limited liability company). Most of the time, a lender in this situation will insist on a personal guarantee, so that the owners are on the hook personally for any credit extended to the business.

Becoming a guarantor is a gamble where we bet that borrower will pay the amount of loan rather than escape from it. Individuals that perceive a greater risk will be less likely to become a guarantor individuals that perceive a lower degree of risk, and willingness to become a guarantor are driven by the interaction between risk perception and risk preference (Lusk Jayson L., Coble Keith H. 2004). Individuals' choices in the decision task can be used to determine risk preferences.

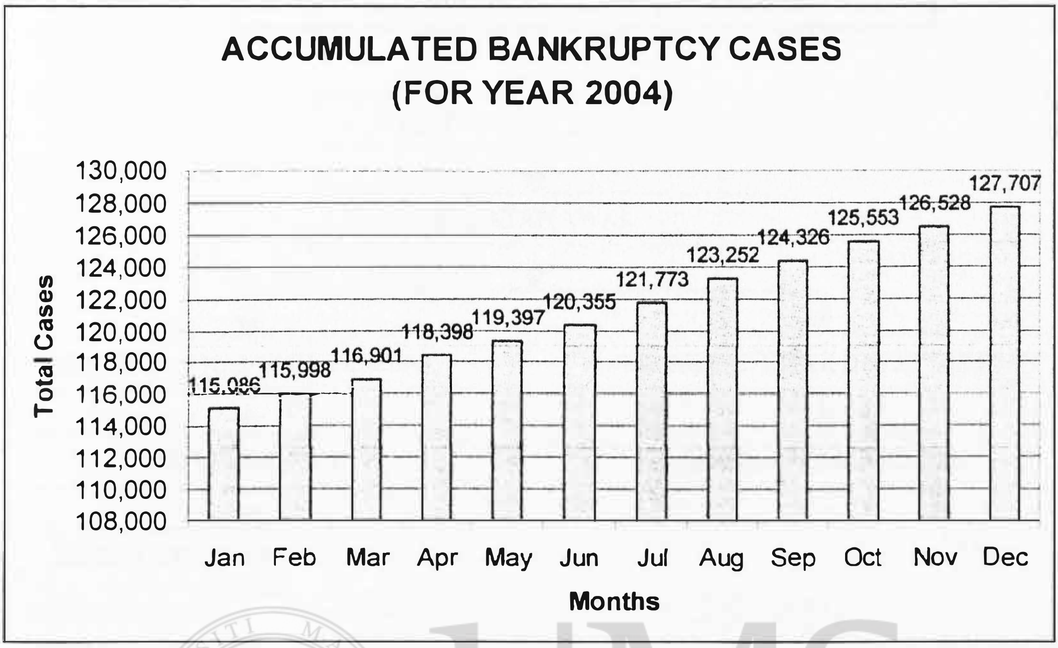
Figure 1.1: Bankruptcy Cases from year 1990 to 1999



Sources: Insolvency Department, Annual Report 2004

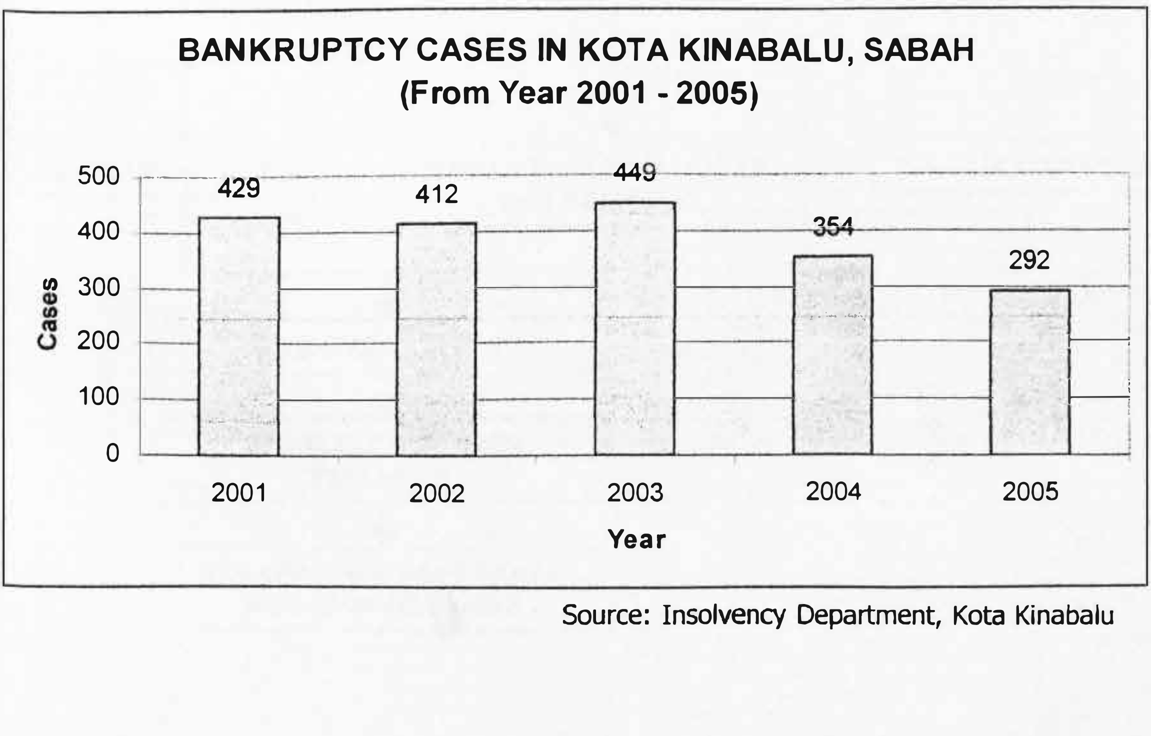
Risk has been interpreted in many ways even within the academic community, the most common interpretation being the variance of the probability distribution of possible outcomes (Pratt 1964; Arrow 1971). Risk can be defined as the appraised likelihood of a negative outcome for behavior (Zuckerman, 1994). Risk taking behaviors are volitional, purposive, goal-oriented and carry potential for arm (Lightfoot, 1997).

Figure 1.2: Accumulated Bankruptcy Cases for year 2004



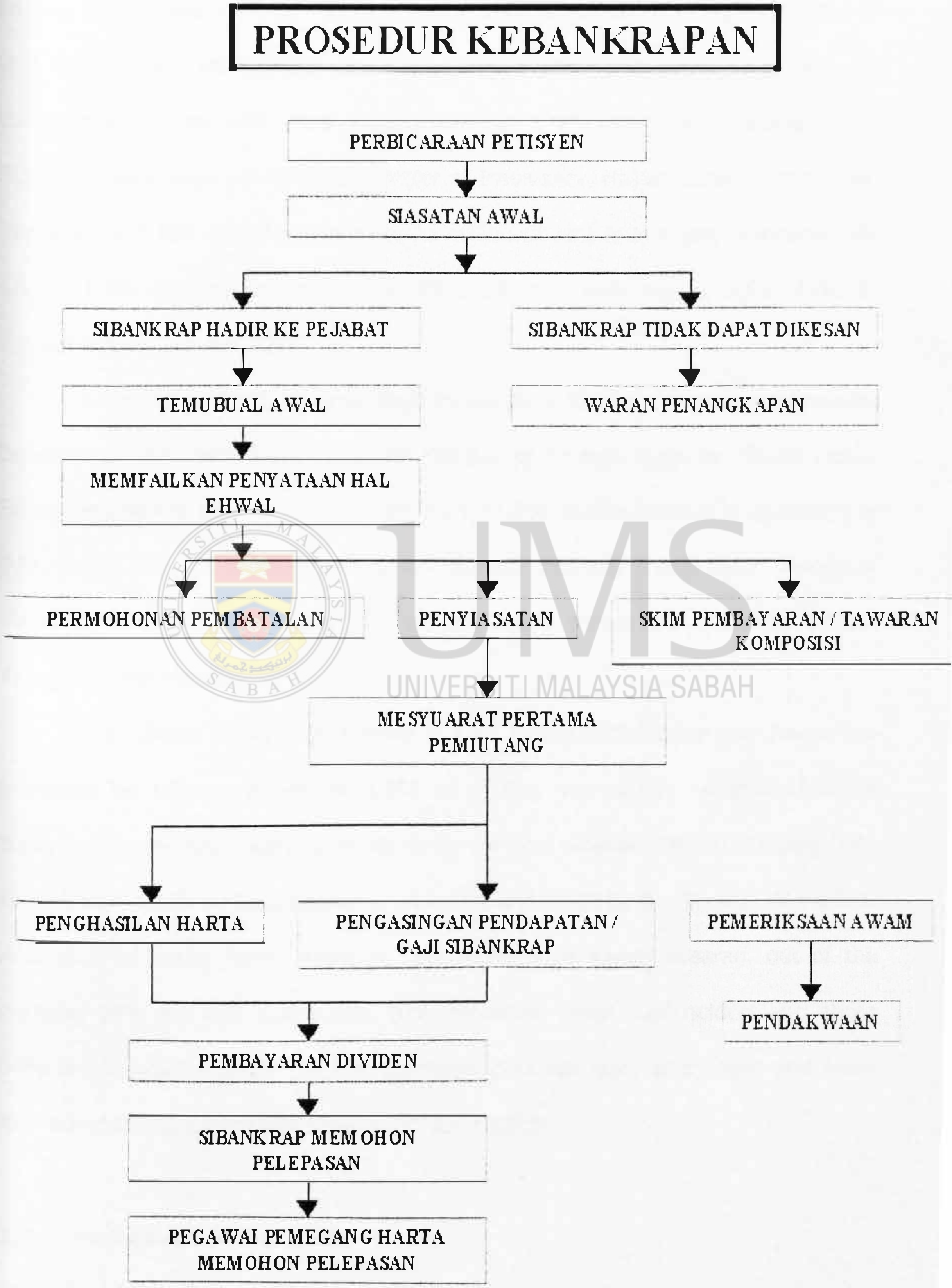
Source: Insolvency Department, Annual Repost 2004

Figure 1.3: Bankruptcy Cases in Kota Kinabalu, Sabah
(Year 2001 – 2005)



Source: Insolvency Department, Kota Kinabalu

Figure 1.4: Procedure of Going Bankruptcy



1.2 Problem Statement

In year 2004, there are 127, 707 bankruptcy cases accumulated in Malaysia. Out of this figure, there are 16, 251 new cases. More than 17,000 individual declared bankrupt every year with the average more than 1,000 person every month. This figure had been explored by Chief Director of Insolvency, Halijah Abbas to the press. There are 137,620 out of approximate 25 million citizens in Malaysia according with 14,276 firms declared bankrupt. This figure updated until August 2005. *(Source: Harian Ekspres, 11 Mei 2005)*

According to the Insolvency Department, Kota Kinabalu Branch, accumulated bankruptcy cases was 7,082. Deputy Minister of Finance Dato Dr. Shafie Mohd. Salleh also saying that there are more than 53,000 Malays involve in approximate 51% out of 104, 770 cases of bankruptcy incurred until year ended 2002. Among of them, 39% are Chinese while 9% are India and others 1%. *(Source: Utusan Pengguna, Mac-April 2004)*

The number of bankruptcy cases in Kota Kinabalu, Sandakan and Tawau has increased by 10% to a total of 8,878 as of May year 2003. A total of 6,168 bankruptcy cases have been administered by the Kota Kinabalu Official Assignee (OA) Department, 1,200 by its Sandakan counterpart and 1,510 by the Tawau OA' s office. According to Sabah Senior Assistant Official Assignee Kamin Kusaran, out of the number, 50% are loan guarantors, 20% defaulting credit card holders and about 30% are borrowers under the hire-purchase, personal loan, study loan and other loan schemes. (*Source: Daily Express, 30 June 2003*)

1.3 Objectives of the Study

Objective of this study is to measure the risk tolerance among individuals by focusing into willingness to become a guarantor since the bankruptcy cases of becoming a guarantor is 50% of the total bankruptcy cases involved. Becoming a guarantor does not have any financial return but have to bear the risk as borrower as explained previously. Therefore it is a question mark where will discuss more detail in later chapters. In addition, this research also exam the relationship of the three main dependent variables: demographic factors, socioeconomics factors and psychological factors with the dependent variable which is willingness to take risk or risk tolerance.

1.4 Scope of Study

The study focused on the determinants or factors influencing the public to take high risk when they choose to become a guarantor in Kota Kinabalu, Sabah on the effect of the increasing cases of bankruptcy. It is important to know the determinants such as demographic, socioeconomic and psychological factors to the risk tolerance and the willingness to take risk as a guarantor.

1.5 Significance of Study

The significance of this study is researching and finding the answers about the determinants of becoming a guarantor. Therefore it is important for the public to know the factors determinant the individuals to take high risk whereas zero return associated with. This study hoping that the result and findings can create awareness about the willingness to take risk as a guarantor and can be used as additional inputs for practitioners to determine the factors influencing the willingness to become a guarantor. The outcome might be useful for financial industry to predict and classify qualified loan guarantors.

1.6 Definition of the Key Variables

This section will explain the definition of guarantor, bankruptcy, insolvency, risk, demographic factors, socioeconomic factors and psychological factors.

1.6.1 Guarantor

A guarantor undertakes that he will repay a debt incurred by another person or company to a bank or other creditor and the bank or other creditor can require him to pay the outstanding amount if that person cannot or will not pay their indebtedness. Proprietors and directors of companies are often asked to give personal guarantees for their company's borrowings to provide additional security. A bank will commonly require the guarantee to be secured, for example a mortgage over a director's house. In the case of co-guarantors each guarantor will be fully liable for the outstanding amount - it is up to guarantors to resolve their respective obligations between themselves.

1.6.2 Bankruptcy

Bankruptcy is brought about when an individual or commercial organisation is no longer able to manage their debt. There are two distinct types of bankruptcy, personal bankruptcy and commercial bankruptcy. Personal bankruptcy is the bankruptcy of an individual, whilst commercial bankruptcy is the bankruptcy of a commercial organisation.

For a debtor or creditor to apply for a bankruptcy order, the debt must be at least RM 30,000 and not be disputed by either party. The purpose of bankruptcy is to convert debtor assets on a personal or commercial level into lump sum and installment payments for the creditors. In the Chinese mainland, the term bankruptcy refers to the winding-up of insolvent enterprises. In Hong Kong, the term bankruptcy is referring to bankruptcy of individuals, whereas liquidation is referring to the winding-up of business enterprises, no matter whether the cases are solvent or insolvent. (Christina Y.M. Ng, 2002)

The Malaysian Bankruptcy Act 1967 was amended in the year 2003 and came into force on 1 October 2003. Changes brought about by the new amendment include:

- A change in the title of the Official Assignee Malaysia to the Director-General of Insolvency Malaysia (DGI);
- Inclusion of a definition of 'social guarantor';
- A requirement for a petitioning creditor to prove to the Court that he or she had exhausted all avenues to recover debts owed to him or her by the debtor before he or she can commence any bankruptcy action against a 'social guarantor'.
- An increase in the minimum debt which enables a person to be declared bankrupt from RM10,000 to RM30,000;
- Enabling the DGI to give the creditor/s a notice of his or her intention to issue a certificate of discharge to a bankrupt without giving any reason;
- Stopping the calculation of the rate of interest on the date of the receiving order granted by the court in cases where the interest is not reserved or agreed upon;
- An increase from RM100 to RM1000 as the minimum amount that cannot be borrowed by an undischarged bankrupt without informing the person who gives the credit or loan that he or she is an undischarged bankrupt.

1.6.3 Insolvency

Insolvency is the inability of an individual or a commercial organisation to meet its debts as and when they fall due. Insolvency does not have to end in bankruptcy, however, Individual Voluntary Arrangements and Administration Orders can provide protection against impatient creditors.

1.6.4 Risk

Risk may be defined in terms of variability of possible outcomes from a given investment. Risk is a central feature in everyday life. Risk can be defined as the appraised likelihood of a negative outcome for behavior (Zuckerman, 1994). Risk refers to a lack of predictability about the outcome of a problem, or to a lack of predictability about the consequences of a decision (Hertz and Thomas, 1984). Liles (1981) defined risk as the probability of a negative outcome occurring from some course of action. We all take risk all the time, often in a way that we do not recognize. In many cases, we underestimate the risk we encounter. However, risk-taking does not mean taking chances. Risk is inherent in choice and can be substantively affect the various decision made.

Risk averse is a people who are unwilling to take risk or in other word, try to avoid risk. Risk takers are those people willing to take higher risk compare to others while risk neutral are those medium person. Risk tolerance is more than a function of an individual's psychological makeup. Risk behaviour is conceptualized as individuals' decision-making behaviour in risky contexts, and may be characterized by the degree of risk associated with the decisions made.

Risk is generally believed to be a multi-dimensional construct (Sitkin and Pablo, 1992; Sitkin and Weingart, 1995; Williams and Narendran, 1999; Yates and Stone, 1992). Although the measurement of risk is complex, research suggests that risk comprises a number of perceptual dimensions: uncertainty, gains relative to losses, situational framing, and personal involvement (Williams and Wong, 1999).

1.6.5 Demographic Factors

Demographic factors including age, gender, marital status, working experiences, education level and etc related to the willingness to take risk. Dohmen *et al* (2005) analysis reveals that women are less willing to take risks than men, at all ages; increasing age is associated with decreasing willingness to take risks. Grable and Joo (1999) also state that singles are more risk tolerant than married persons.

1.6.6 Socioeconomic Factors

Socioeconomic consist of income level and financial knowledge that might influence the willingness to become a guarantor. Grable and Joo (1999) reveal that higher income is associated with higher risk tolerance; greater economic expectations are associated with higher risk tolerance; and lastly increased personal finance knowledge is associated with higher risk tolerance.

1.6.7 Psychological Factors

Psychological factors including birth order, locus of control, personality and etc. Walker (1996) indicates that psychological factors may be more important than economic ones in the process of getting out of debt. The psychological variables relevant in the context of this paper are lifestyle attributes, specifically, beliefs about credit and the importance of things in one's surroundings.

1.7 Organisation of Study

This research proposal comprises of three main chapters. Chapter 1 provides the introduction, problem statement, objectives, scope research, significance of the study and definition of key variables. Chapter 2 is mainly focused on literature review on the aspects of demographic factors, socioeconomic factors and psychological factors that influence the willingness to take risk. In this chapter the relationship between independent variables and dependent variables are discussed. Chapter 3 describes the research methodology of the study. It encompasses the research design, sample and population, research instrument, research location, procedures of collecting data and method of data analysis.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

Research on risk-taking behavior has taken one of three major approaches on how the entity being studied (whether an individual, a firm or a society) takes risks: the economic, the behavioral and the sociological. The economic perspective (von Neumann & Morgenstern, 1947; Arrow, 1971) which permeates much of the research in economics, finance and statistical decision analysis, essentially treats decision-making agents as unitary and free of contextual influences, whether they are individuals, firms or teams within firms (Zaheer Srilata A., 1997). The role of context in this perspective has been largely restricted to the interaction of individual wealth and risk aversion (Pratt, 1964; Arrow, 1971) and in the finance literature to portfolio effects (Markowitz, 1959; Ball and Brown, 1969).

The second approach is that of the behavioral decision theorists (Slovic, 1972; Payne, 1973; Kahneman & Tversky, 1979; Goldstein and Einhorn, 1987). These researchers tend to describe the actual risk-taking behavior of individuals in relation to their information-processing limitations. In this perspective, context begins to play a role in influencing risk-taking behavior, but it is largely the immediate decision context (for instance, the framing of the problem, the order of presentation or the salience of the alternatives) rather than the broader organizational or social context in which the decision-maker is embedded. As Tetlock (1985:300) puts it,

> *. . .the dominant research program on judgment and decision-making has clearly been the cognitive or information-processing approach. . . Thought and action are seen as products of the cognitive operations of the individual thinker, rather than as products of the social, organizational and technological settings in which the individual is embedded.*