Advisers on the couch

***Richard Tomlinson** discusses the growing debate about whether applied psychology can improve the quality of financial advisers and the advice they dispense*

A recent survey of 130 investment and pension advisers for Quilter Financial Planning measured five key personality traits required to do the job well: emotional stability, agreeableness, conscientiousness, intellect and extraversion. Such research helps reinforce the caricature that, these days, personal financial advisers (PFAs) need their own session on the psychiatrist's couch before they are qualified to analyse index tracker funds, and certainly before they meet that bundle of neuroses and long-buried impulses formerly known as the client. In the US, for instance, an online seminar organised in January this year by the Financial Therapy Association offered financial advisers the chance to learn about "the volatile coefficient of sex and money" and the "underlying themes that fuel these precarious dynamics".

What this psycho-babble obscures is a serious and growing debate about whether applied psychology can improve the quality of financial advisers and, separately, the advice they dispense. "Don't assume that people understand how to manage their money just because they earn £250,000 per year and drive a flashy car," says Simonne Gnessen, founder of Brighton-based Wise Monkey Financial Coaching. "Underneath they may have all sorts of secret anxieties and even shame about money, which they are not discussing with their partner or even a therapist."

A central element of the debate concerns whether "robo advice" can assist PFAs in identifying a client's often subconscious biases when making financial decisions about savings, investments and pensions. The case against robo advice is that it is just a fancy name for online tick-box questionnaires that save PFAs the trouble of filling out forms about a client's personal circumstances (age, job, children and so on) and the financial products they are interested in buying.

"Robo advice is not advice, it is digital implementation of purchasing investments," says Julie Lord, a former president of the Institute of Financial Planning. "A digital advisory service is not going to hold your hand when the markets crash."

The alternative case is put cautiously by Stian Reimers, a psychologist at City University in London who has studied the impact of robo advice on financial decision-making. Reimers suggests that robo advice questionnaires can be designed that provide a "decent, if not perfect" service for people who cannot afford to consult a PFA. But the algorithms that underpin robo advice soon enter a maze of complexity in adapting analytical tools from psychology to assist a person's savings and investment decisions. "The more you look at robo advice, the harder it is to fathom how you get at people's preferences, which are so malleable and context-sensitive," says Reimers.

At the heart of this problem is the fact that the human mind is extremely good at performing mental short cuts, or what psychologists call heuristics, to solve practical problems in everyday life. For example, you decide to drive a car to work rather than taking a bus because you remember there are road works on the bus route that might delay you.

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As Reimers explains, this rule-of-thumb approach works much less efficiently in the complex world of financial decision-making, which academic psychological research suggests can be influenced by more than 150 heuristics and biases.

Biases and herding

One example is the tendency known as "herding", where people choose a pension plan or an index tracker fund not because it is objectively the best option for them but because it is popular; or, even more subjectively, because they know of several friends who are "sensible" about money and have bought the same product. A similar bias, demonstrated by psychological tests, involves picking the middle option on a list of investment strategies, regardless of the stated risk, simply because it is in the middle and therefore looks "safe" or consensual.

There is a further layer of complexity because not all biases necessarily reflect a poor understanding by someone of their own best interests. In 2018, the Behavioural Insights Team (BIT), a UK government policy unit, commissioned a survey of 200,000 adults by the polling company Ipsos MORI to measure their financial decision-making capability. The starting point for one scenario was research by the government's Money Advice Service showing that around 70 per cent of people experience an unexpected and costly event each year, such as a broken boiler or a leaking roof. "To our surprise," BIT reported, "we found that, when prompted, people either accurately estimated or overestimated the probability of financial shocks rather than underestimating them."

It gets even more complex because in the world of psychological testing, where all questions seem to lead to another conundrum, there could have been an in-built "framing effect" that made the respondents think more about financial shocks than normal because they had been asked to do so.

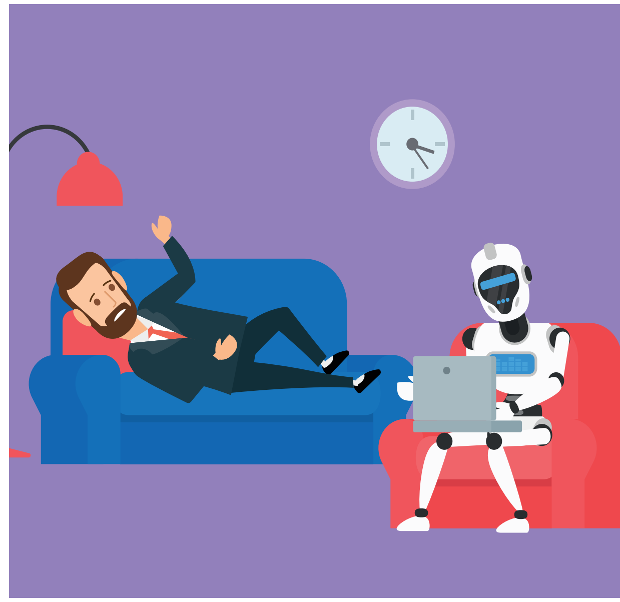
The real picture

According to Reimers, the challenge of financial advice is making people see their future life in concrete terms, rather than as an almost abstract proposition: the difference between knowing that you need a pension and visualising what it would look and feel like to be old without a sufficient retirement income. "There are psychological tricks you can use to get people to think more about their futures, which PFAs could certainly learn from," says Reimers. One such trick, invented by the retirement planning division of Bank of America, is to take a photograph of a client and then retouch it digitally to show them what they will look like when they are older.

> *Advisers are often less inclined to explore what a client needs financially to enjoy their idea of a good life*

Assume that such psychological tricks work, since there is no clear evidence either way. The spotlight then turns back to PFAs, who are naturally biased, as professional advisers, to telling clients what they require in terms of financial products in order to deliver measurable returns. Often, however, PFAs are less inclined to explore what a person needs financially to enjoy their idea of a good life.

It is easy to mock the idea of financial "wellness" as another mushy import from US psychotherapy. Yet it has always been true that some people can be miserable with large amounts of money, such as Shylock in *The Merchant of Venice*, while others can remain happy while teetering on the brink of financial ruin, such as Mr Micawber in *David Copperfield.* According to Lord, the only way a PFA can gauge where a client sits between these two fictional extremes is to spend



time getting to know them. In her opinion, this in-depth approach is in the PFA's financial self-interest as well. "Clients will be clients forever if you have listened to them and will then become an ambassador who recommends you to their friends," she says. "Ultimately, you'll make a heck of a lot more money than the money you would save by being quick."

At first glance, this focus on financial "wellness" and the client as a person sounds like an updated version of the proverbial visit to your friendly local bank manager, before the branch was shut down and head office rolled out its latest cost-cutting robo advice website. Yet this same bank manager was himself a mass of subconscious heuristics, biases and framing effects. These began with the fact that he was usually a man who, back in the 1960s, might still have insisted that a wife needed her husband's signature before she could open a savings account. Seen in this dismal historical light, Quilter's attempt to pinpoint and measure the most important psychological characteristics for a good PFA looks like sound common sense. ■

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