‘Field Research’ in Behavioral Finance

By Editor Test *Tue, Feb 21, 2012*

Real scientists scoff at the value of "anecdotal evidence." But you can learn a lot about the psychology of money at a garage sale, or when you're buying clothes.

Late last month, feeling flush after shaving $500 from the cost of a future business trip, I tempted myself by taking a long-cut on my way to the Port Authority Bus Terminal through the red light district of conservative men’s fashion in Manhattan.

I mean those sleek storefronts near Grand Central Station where *Brooks Brothers*, *Paul Stuart*, *Charles Tyrwhitt*, *Allen Edmonds*, *and JoS A. Bank* wait to prey on well-heeled males walking from the Harvard and Cornell Clubs (or from Citibank and Bank of America) to the Metro-North trains.

“SALE,” read the big red letters in *JoS A. Bank’s* window at the corner of 46th St. and Madison Ave. Inside, a matter-of-fact salesman (a Wall Street trader until 9/11) made this offer: Buy a sports coat at the “regular” price and receive two casual shirts, two dress slacks, and two sweaters *free*.

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JoS A. Bank isn’t *Barney’s* or *Brooks Brothers*. But then, neither am I. After estimating the average weighted price per garment in my head, and selecting my clothes, and finally standing on a carpeted platform while a tailor chalked my pant cuffs, I took the trade.

Later I reflected on my own behavior. Or rather, my participation in an act of *behavioral finance*. And I began to remember similar moments, involving myself or others. Check out these anecdotes and decide whether they count as evidence of anything:

Buyers’ club beware. As new homeowners, my spouse and I were once seduced by an “exclusive” direct-mail invitation to join a “buyers’ club” whose members enjoy discounts of 10% or more on a “vast” selection of wholesale furniture, carpets, kitchen cabinets, etc. We drove to the address on the invitation–a warehouse in a desolate industrial park.

Once inside, we were more less committed to watching a time-share-style video and an equally vapid live presentation. Then we and other couples were led, one pair at a time like creatures boarding Noah’s Ark, to a desk in a cubicle where a carefully scripted but otherwise clueless salesperson finally made the pitch.

We were offered the golden opportunity to pay $5,000 up-front to join the “club” and—for a single year—save 10% on purchases of big-ticket items *from certain selected catalogues*. We were not allowed to inspect the catalogs before joining.

Invoking my junior-high math, I calculated the minimum amount ($50,000) we would have to spend in a year simply to recoup our annual “membership fee.” Before I could start ridiculing the salesperson in a loud voice, my spouse hooked my arm and hustled me out.

Target-date mirage. A relation of mine, a very trusting single person of about 50, recently started a new job. Her 401(k) plan sponsor, an omnipresent Internet retailer whose name you can easily guess, defaulted her into a target-date fund whose target date indicated that she would retire in 15 years. When visiting us for dinner one Sunday, she marveled at her new employer's confidence that she could afford to retire in 15 years.

For some reason her naiveté reminded me of the time I and my young daughters saw a man in a cowboy hat buying lottery tickets from a cashier in a mini-market. Always ready to torment them with a teaching moment, I asked the girls, then ages 7 and 10, to guess that person's chance of winning the lottery in the next day's drawing. "Fifty-fifty," said my oldest. How so? "Simple," she said. "He wins or he doesn't win."

'Unfair' subsidies. People don't necessarily appreciate a subsidized price if someone else gets a free pass on the same item. I've observed this twice.

In the first instance, a friend of mine complained that, while he paid full tuition for his child at the state university (about $16,000), one of his children's single-parent friends was able to go tuition-free as a hardship case. Now, my friend could afford the $16,000 (plus $9,400 for room and board, $3,000 for fees and $1,400 for books). But the unfairness of it bothered him.

For argument's sake, I reminded him that he was the beneficiary of an in-state discount (non-resident tuition is $28,000) and an implicit discount for choosing a taxpayer-supported university over a private one, where the typical all-in sticker price is now $54,000. It was "all relative," I told him. But he didn't buy my argument.

In the second instance, a money manager for a family office firm in New York told me about indigent people living in her building on the Upper East Side who paid only $150 a month for spacious two-bedroom apartments, while she paid $4,000 a month for a similar apartment on the other side of the building. I was vaguely familiar with New York's rent control laws, but this particular wrinkle was new to me.

The money manager herself also enjoyed a subsidy: She paid $1,000 below-market because her landlord participated in a city-sponsored housing program that allowed a few of her neighbors to live there for next to nothing. But that didn't change the way she felt. What really annoyed her was that the City of New York apparently provided a car and a driver to chauffer any two people in the program anywhere in town on a day's notice—for free. I wondered if Mayor Bloomberg knew about that.

Herding. One of the couples in my neighborhood recently held a garage sale to get rid of a lot of bric-a-brac before moving to Florida to retire. They called it an "estate sale" to try to attract a crowd with deeper pockets than the usual flea market mob. Curious, I wandered over to gawk. Strange cars were parked up and down the lane.

Inside the house, an antique blanket chest caught my eye. A dozen other shoppers ahead of me had walked right by it. The tag said $125. I offered $100. The agent of the company that managed the sale swiped my credit card through an attachment to her smartphone and marked the chest "Sold." I rationalized the purchase as a memento of my soon-to-be-former neighbors.

An hour later, when I came back with a van to collect my little white elephant, the agent said, "As soon as you took the chest, a half-dozen people asked me about it. That's how it always works. Once one person gets interested in a piece, suddenly everyone wants it. I had lots of offers for it after you left. You could have *tripled* your money."

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But let me finish explaining the significance of my visit to *JoS A. Bank*.

As I said, I didn't agree to their deal immediately. First I had to see if any of their sportcoats appealed to me. Generally, the selection of jackets or suits in my size on any retail rack is meager at best. In fact, I order my suits from a reliable Tsim Sha Tsui tailor who has kept my vital statistics in a handwritten ledger since 1994.

As it turned out, I found a versatile tweed jacket that fit perfectly. At $500, it cost more than I generally pay, but the price included (as mentioned above) two slacks (tagged $165 each), two shirts (up to $90 each) and two sweaters (up to $100 each). Several round-trips to the changing room later, I had chosen all seven items.

Now, exactly what was I thinking, financially? Not for a moment did I pretend that I was getting $1,200 worth of clothes (which might have cost as little as $10 to manufacture in South Asia) for $500. But I was satisfied to think that I was paying about $250 for the jacket and getting the rest for $250. (And how much, really, was my $500 "worth"? These days I have a habit of dividing prices by 10 to see what they would have been before August 1971, when Nixon took the U.S. off gold to get re-elected.) So I bought the clothes.

Ultimately, money wasn't the issue. What mattered was whether the clothes were stylish enough and durable enough to serve me long enough to make the cost basis irrelevant. Clothes are not like stocks or bonds. I didn't need to sell them for a profit to realize their value. I just needed to wear them long enough. Indeed, given my age and their quality, the clothes and I might reach the ends of our lives simultaneously.

In that sense, the clothes were comparable to an income annuity. Will the income from the annuity meet your needs? Will it last? Will it make you feel more comfortable and secure? These are the most important considerations. When you are 91 years old and you continue to receive monthly checks from an insurance company, you'll probably have forgotten what you paid for the contract back in 2000-something.

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