Retirement Income
JOURNAL

Seven questions that reveal financial biases

By Editorial Staff *Wed, Oct 20, 2021*

'Understanding clients' underlying biases and mitigating suboptimal investment decisions is critical for advisors in a digitally pervasive environment," a Cerulli Associates report said.

US investors held nearly $55 trillion in financial assets as of year-end 2020, up from $46 trillion in 2019, according to Cerulli Associates. In its latest report, the Boston-based consulting firm suggests that advisers use behavioral finance techniques to help retain investor trust—and assets.

"As investors navigate perpetual unease resulting from the pandemic, advisors should pay increased attention to clients' emotional biases through the lens of behavioral finance to acquire, retain, and grow financial assets," said the report, *US Retail Investor Advice Relationships 2021: Navigating Perpetual Unease.*

According to the research, advisers most commonly see three so-called information-gathering biases among investors: availability bias (91%), confirmation bias (80%), and recency bias (71%).

"The fact that investors realize they rely on things that they just read, that were easy to find, and reinforce what they already think underscores the challenge with investor 'research,'" said Scott Smith, director of retail investor advice relationships, in a release. "Instead of seeking out a variety of inputs from independent experts, consumers are predisposed to choose the path of least resistance."

BEHAVIORAL FINANCE BIASES AND IDENTIFICATION QUESTIONS	
Ask clients, "How much do you agree or disagree with the statements on the right?"	
Confirmation bias	**I generally read articles, visit websites or watch TV shows whose information I agree with.**
Availability bias	**I tend to rely a lot on information that I read or heard recently.**
Overconfidence bias	**With my portfolio management skills, I'm sure I can outperform the market.**
Loss aversion bias	**I tend to feel really bad after a loss. Gains don't excite me much, however.**
Recency bias	**Sometimes I make an investment decision right after a big news event or emotional experience.**
Herding bias	**I find out how other people are investing and try to do something similar.**
Anchoring bias	**If I bought shares of stock at $160 and the price went down, I wouldn't sell until it reached $160 again.**
Source: Cerulli Associates, October 2021.	

Investors' behavioral biases evolve as they age, Cerulli found. Investors ages 40–49 report the highest incidence of acute behavioral bias—confirmation bias (47%) and overconfidence (42%). To advise an "emerging affluent" investor, advisers should "start early to help investors understand their biases and nudge them toward better outcomes," Smith said.

Investors with more than $5 million in investable assets report elevated levels of confirmation (39%) and availability (39%) bias. "These investors have frequently made long-term decisions about the direction of their portfolios and are reluctant to be swayed by new information.

"While they should not overreact to short-term changes, they should also be open to the reality that the landscape of finance is one of constant evolution and refinement, necessitating ongoing portfolio oversight," said Smith.

"Increased attention to clients' emotional biases through the lens of behavioral finance can be an impactful tool in helping set goals, maintain investment discipline, and reduce decision fatigue," he added.

"Advisors need to ensure that investment decisions are being optimized for the financial betterment of the investor. Understanding their underlying biases and mitigating suboptimal investment decisions is critical for advisors in a digitally pervasive environment."