

Economic Psychology and Investor Education

Vera Rita de Mello Ferreira

Investor Protection and Education Going Forward

What does it take to change behaviour?

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ECONOMIC PSYCHOLOGY AND INVESTOR EDUCATION



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[some of] THE CHALLENGING PROBLEMS

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1. We don't have stable preferences – rather, we're context dependent



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**1. We don't have stable preferences –
rather, we're context dependent**



=



higher life satisfaction!

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2. We're **BLIND**



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2. We're **BLIND** to our **OWN blindness**

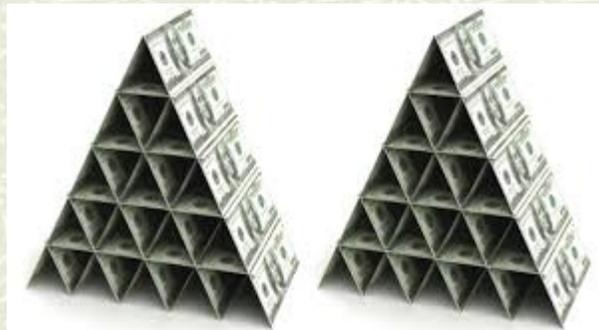


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3. We want to be fooled!

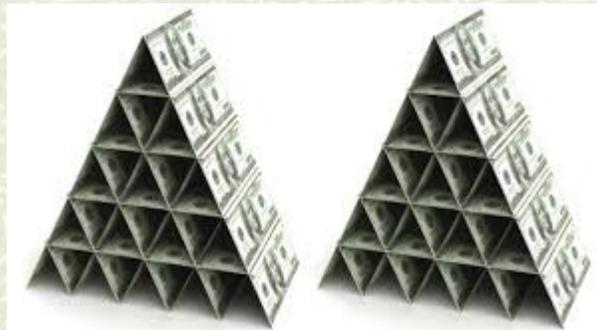


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3. We want to be fooled!



**If you don't fool me...
...I'll do it myself!**

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4. THERE IS A **LARGE GAP** BETWEEN **INTENTIONS... AND ACTIONS!**



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4. THERE IS A LARGE GAP BETWEEN **INTENTIONS... AND ACTIONS!**



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TROUBLE!!!

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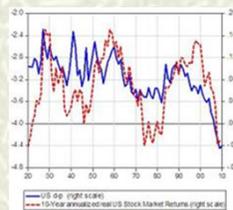
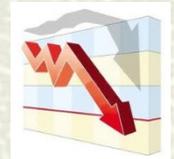
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On one hand,

Financial markets are rough...



- a **complex** world where **complex**
choices must be made



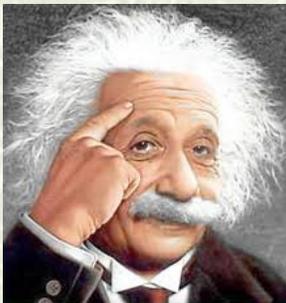
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On the other hand,

human abilities are **limited**



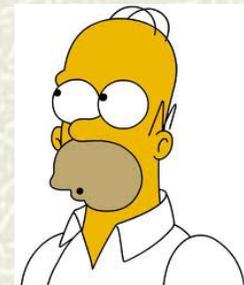
?



?



?



?

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So:

**ECONOMIC PSYCHOLOGY /
BEHAVIOURAL ECONOMICS**

+

FINANCIAL EDUCATION

=

**COMPLEMENTARY WITH
GREATER EFFICACY**

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ECONOMIC PSYCHOLOGY – 1881

[more recently **Behavioural Economics**, Behavioural Finance, Neuroeconomics, *Applied Behavioural Science*]

- interdisciplinary field – economic behaviour and decision-making
→ *anomalies*, distortions in perception, memory and judgment of data
- 3 Nobel Prizes in Economics:
 - 1978 – H. **Simon** → *bounded rationality* 
 - 2002 – D. **Kahneman** → *prospect theory* 
 - 2013 – R. **Shiller** → *financial markets and bubbles* 

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EMOTIONS and IMPULSES

are VERY powerful

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Not only
GREED and FEAR...

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EMOTIONS and **IMPULSES**
are **FAR MORE** **powerful**
than **REASON** is

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THINKING IS A RECENT ACHIEVEMENT!
AND STILL RATHER UNSTABLE!
IT MAY 'COLLAPSE' ANY TIME...



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It is *as if* there were **2** of us in our mind!

hot self

impulses – fast



VS.

cold self

ponderation – slow

automatic

VS.

reflexive

action

VS.

intention

doer

VS.

planner

short range

VS.

long range

PSYCHOLOGY

EDUCATION



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**THIS IS WHY IT IS RELEVANT
TO UNDERSTAND
THE INVESTORS' MIND**

**THUS, DESIGN
[MORE] EFFICIENT
FINANCIAL EDUCATION
PROGRAMS FOR THEM**

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btw, that includes **protecting** the
investor against **HIM/HERSELF**
as well!!!

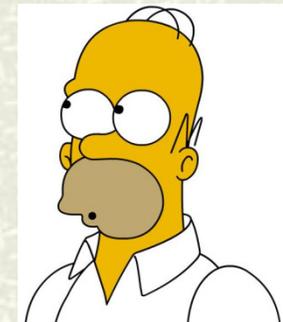
fraud, scams, Ponzi schemes are
not the only threats
to be addressed...

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The Homer Simpson* living [more or less] secretly inside us is always lurking...



*[or the chimp, or the baby – unfortunately, less often the Einstein...]



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It's a tough struggle!

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we need all the help we can get!

the fantastic quartet

psychological insights

+

financial education

+

consumer protection

+

regulation

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- investors are driven by major **psychological forces**
- and there are several **implications** resulting from these **tendencies...**

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- investors are driven by some major **psychological forces**:
- constant **search for comfort and relief**
[from tension,
distress, anxiety]



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- investors are driven by some major **psychological forces**

IMPLICATIONS

- constant search for **comfort** and **relief**
[from tension, distress, anxiety]



- If no **immediate** solution is to be found in reality → resort to **illusions**



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- investors are driven by some major **psychological forces**:

- enormous **loss** and
frustration **aversion**



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- investors are driven by some major **psychological forces**

IMPLICATIONS

- enormous **loss** and frustration **aversion**
- In order to try and **avoid losses** → run **more risks** in the name of *'attempting to recover what's been lost'* [or is in danger of being lost] – while **unaware** of it...



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- investors are driven by some major **psychological forces**:

- **uncertainty** and ambiguity
are equally **hated**



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- investors are driven by some major **psychological forces**

IMPLICATIONS

- **uncertainty** and ambiguity are equally hated 
- so **simple** perspectives and alternatives will be **preferred** – even when what they may yield does not amount to **much**
 - or worse, when they involve **risk** 

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- investors are driven by some major **psychological forces**:

- also **hated** → the very
act of **making decisions!**



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- investors are driven by some major **psychological forces**

IMPLICATIONS

- also **hated** → the very act of making decisions!
- then **procrastinate, do nothing, push** the final decision **to others** [later on, to be blamed if it doesn't work out...], or choose just about anything, **only to get rid of** [the distress caused by] the situation



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AS A RESULT...

bounded rationality

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AS A RESULT...

*and **emotions** riding again!*

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human abilities are limited

we're **VERY** suggestible

...and **gullible**

...and **vulnerable**



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human abilities are limited

selective attention



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human abilities are limited

**social pressure /
herding behaviour**



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human abilities are limited

EXCESSIVE

pessimism...

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human abilities are limited

EXCESSIVE

pessimism...

optimism...

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human abilities are limited

EXCESSIVE

pessimism...

optimism...

self-confidence...

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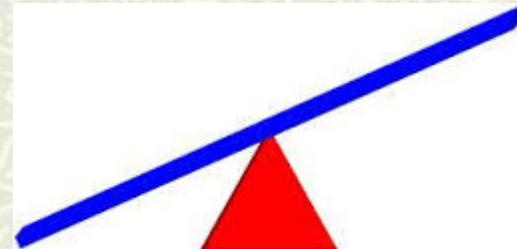
human abilities are limited

EXCESSIVE

pessimism...

optimism...

self-confidence...



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human abilities are limited



euphoria

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human abilities are limited



panic

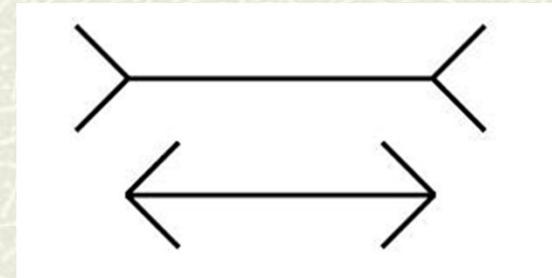
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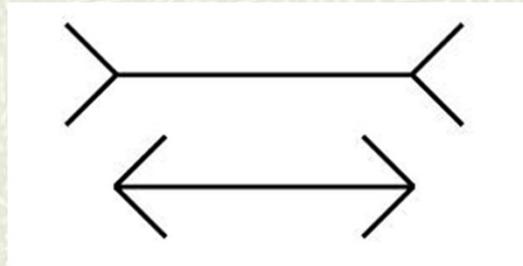
human abilities are limited

problems **perceiving**
and **assessing** data



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And we don't have only optical illusions!

We also have **cognitive** and **emotional**
illusions → they interfere with the
ability to **judge** data

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HOW DO INVESTORS HANDLE ALL THAT?

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HOW DO INVESTORS **HANDLE** ALL THAT?

- they **simplify** – all they can – and some more too, while perceiving and assessing data, perspectives, options

→ but... over the process of simplifying,

precision is lost!

→ and **inadequate choices** may follow...



though their single **wish** is to always have
everything work out as **fine** as possible!

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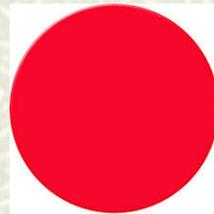
And the **root** of all
simplification is...
emotional!

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because this is the **first step** to judge all kinds of data: an **EMOTIONAL *stoplight!***



if seems **unpleasant** = good-bye!
[disregarding consequences]



if seems **pleasant** = welcome!
[even when only an illusion...]

And this **automatic**, unconscious and rudimentary '**assessment**' considers only the **short range!**

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So, all these **actual** features
of the **investor's mind** ought to be
considered when the **goal** is
to **change behaviour** towards
enhanced **decision-making skills**
and **better choices**

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AND HOW CAN EFFECTIVE BEHAVIOURAL CHANGE BE ACHIEVED?

- ✓ **psychological limitations** must be considered
- ✓ **accuracy** in mental operations **can't** be taken for **granted**
 - but **emotions** should, because they're always **present!**
 - **preferences are not consistent**
- ✓ the **hot self** and **groups** [**herding** is powerful!] are the **targets**
 - since they're the actual **doers** most of the time
 - however, they're **not** too **good** as far as **learning** goes...

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FINANCIAL EDUCATION + ECONOMIC PSYCHOLOGY: 'DO'S'

1. **clear** language ✓
2. examples and **narratives** ✓
3. different delivery **channels** ✓
4. relevant, tailor-made and timely info on the psychology of **economic behaviour** and **decision-making** ✓
5. warnings against **fraud** ✓
6. careful **maintenance** and constant updating ✓
7. **checklists** ✓
8. **multidisciplinary** approach ✓
9. **exchange** experience ✓
10. specific formatting for **different segments** ✓
11. good timing – **learning opportunities** ✓
12. **coherence** ✓
13. **crowdsourcing** – investors ✓
14. **internet** and **social media** ✓
15. **choice architecture** ✓
16. '**MANTRA**': **KEEP IT SIMPLE** ✓
[a.k.a., the **HUGE** challenge here...]

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FINANCIAL EDUCATION + ECONOMIC PSYCHOLOGY: 'DON'T'S'

1. getting carried away with **jargons** and abstractions ☒
2. **too much** information ☒
3. **too many** options ☒
4. excessive **complexity** ☒ → *HUGE challenge here...*
5. 'loose' – i.e., **out of context** – recommendations & warnings ☒
6. solely **logical** explanations ☒
7. 'one size fits all' ☒
8. **obsolescence** ☒

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**BUT ONE THING IS FOR SURE:
IN ORDER TO ACHIEVE EFFECTIVE
BEHAVIOURAL CHANGE...**

**...different strategies must
be devised to move beyond the
simple presentation of technical
information and advice**

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CHOICE ARCHITECTURE → **NUDGE**

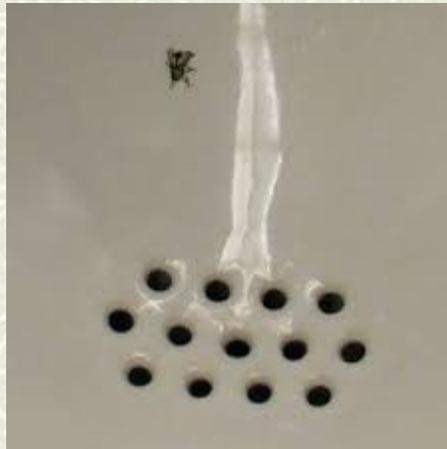
- recent research line
- designing policies to help make those choices more successful → **NUDGES** → *fool proof* contexts
- strategies to encourage better decision-making by turning limitations into advantages – **not** compulsory! – with **opt-out**
- to qualify as **NUDGE**
 - low cost
 - simple
 - mass scale

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famous ***NUDGE*** to keep male public
bathrooms more decent...



[Schiphol airport, Amsterdam]

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CHOICE ARCHITECTURE → ***NUDGE***

What would your meal be like if it started like this?



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CHOICE ARCHITECTURE → ***NUDGE***

And what if it started this way?



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CHOICE ARCHITECTURE → ***NUDGE***

Or this??



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CHOICE ARCHITECTURE → *NUDGE*

If the goal is to stay healthy and/or lose weight...



the *nudge*, here, has been to start with healthy options – though one could always skip them, and go straight to the greasy fattening stuff!

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CHOICE ARCHITECTURE → *NUDGE*

Choice architecture is everywhere – and has been around forever...

- **novelty:**

**CAN IT BE USED TO BENEFIT
THE DECISION-MAKER?
i.e., **investors****

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CHOICE ARCHITECTURE AND INVESTOR EDUCATION

For instance:

- In light of behavioural findings, start by **analyzing** the **current choice architecture** used by the industry and regulators
 - **what have investors been 'nudged' towards doing regarding practices, norms etc.?**
- then, afterwards, discuss, test and consider **what** and **how** things could be **changed** wherever necessary

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CVM – Behavioural Studies Center – new! **[NEC-Núcleo de Estudos Comportamentais]**

- team of **behaviour** specialists: **economic psychology, behavioural economics, neuroscience, cognitive and social psychology, education**
- in light of **behavioural** studies, provide insights, suggestions, criticism, recommendations and technical support towards **enhancing efficiency and efficacy of educational policies**, as well as information and guidance for **investors**

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VERA RITA DE MELLO FERREIRA

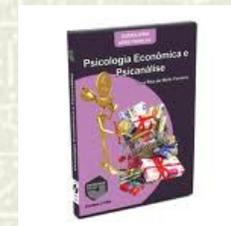
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VERTICE PSI *Economic Psychology – a psychological outlook for perspectives, decision-making, choice architecture and policy*



THANK YOU!

- **Ph.D. in social psychology** (PUC-SP), **Economic Psychology independent consultant** (policy-making: **Behavioural Studies Center-NEC**, at **CVM**, **ENEF-National Strategy for Financial Education**, **NUMIP**-Economic Psychology and Financial Education Interactive Center at the **Brazilian Central Bank Money Museum**, and other organizations), Lecturer (**FIPECAFI**), **Psychoanalyst** (Inst. Sedes Sapientiae)
- **Speaker; Coordinator of economic psychology study and work groups**
- Member of **ICABEEP**-*The International Confederation for the Advancement of Behavioral Economics and Economic Psychology* **Executive Committee** and **IAREP**-*International Association for Research in Economic Psychology* **Representative in Brazil**
- **Author of articles** published in Brazil and abroad, and the **books**:



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