<u>‘Nudges’ – Marketing Synopsis / Taster Piece</u>

Can Nudges be used for improved financial wellbeing?

Introduction

This report aims to address a recognised research gap by providing a comprehensive literature review by focusing on financial wellbeing of decision-makers. Specifically, this report concentrates on how nudges have been embedded into the repertoire of policy tools employed by government and institutions to facilitate better financial decision making of individuals.

Over the past two decades nudges have attracted considerable interest from policy makers and researchers, who continue their examination of the impact that nudging has in the financial arena, with the focus on the welfare effects.

Executive Summary

- While behavioural biases, heuristics, and rules of thumb facilitate the decision-making process, they often lead to suboptimal choices

- Policy makers exert significant efforts to help individuals make better financial decisions, aiming to improve their financial wellbeing

- One of the most prominent and popular nudges is a default rule

- The design of default rules often embeds the influence of behavioural biases particularly the status quo bias, loss aversion and regret aversion in order to conquer people's tendency to procrastinate

- Indeed, default rules and nudges more generally, are characterised by high effectiveness, low cost and wide public support

- In addition, alternative policy tools can lead to similar outcomes to those achieved by nudging

- In some cases, when people hold antecedent preferences and counter-nudges are at work, default rules may fail

- It is important to use nudges in combination with other policy tools and sludge to enhance people's financial wellbeing

Synopsis

A move away from the status quo takes effort. A nudge is therefore utilised to make change to the status quo, thereby using loss aversion to force the individual to take action (e.g. "this will happen within 30 days unless you tell us otherwise"). This could be used for example when rebalancing portfolios

Most changes to finances require the client's direct agreement, therefore loss aversion is limited in its use in this way. However, is there an opportunity for Advisers to make more use of Automatic Rebalancing, which would not require agreement as long as there is no change of funds as this exercise does not require agreement beyond the initial one.

Only 50% of people only have life assurance. The *ability* to cope with financial shocks is important. There is wellbeing from knowing that protection is in place. Many people are forgoing this

From a financial coaching point of view, there is the suggestion that people who potentially need more assistance with their finances are more likely to respond to nudges.

Highlighting the relevance of the financial plan as when there are too many choices, fewer decisions are taken and the want for immediate satisfaction (hyperbolic discounting) provides further evidence of procrastination.

How/whether to use nudges:

Nudges are an important tool because they respect the freedom of contrary choice, avoiding regret aversion. Accordingly, nudges must be transparent

People even approve of a nudge if they feel it is in their best interest. Nudges should be a choice between options, none of which could cause regret.

Nudges are more favourably viewed when instilled by someone who has the client's best interests at heart.

A combination of informative nudges (blogs, reminders, warnings etc) and action nudges (defaults, etc) would seem to be the best approach.

An alternative to nudging could be to reduce choices; "Would you like portfolio A, B or C?" is more likely to get a commitment than; "We have the ability to use any fund in the market in your portfolio."

Conclusion

It is important to note that nudging is about helping clients to achieve their own objectives and NOT the objectives of the firm. To assist and support a client to 'know thyself'. Helping clients to achieve their 'clear path to identifiable objectives', and NOT a method of convincing clients to buy products and invest more into the funds under management.

Nudging can (rather obviously) be used to sell products and services, rather than create better financial decisions. Any Advisers using nudging should make sure their nudges are open and transparent in order that they can easily be demonstrated to be in the client's best interest, and not the firm's. This is important for reputation, as well as the effectiveness of the nudging.

If making use of nudges, tell the client. Don't' make it a secret.

To read the full report, download the whitepaper here .....