Risk Profiling

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Risk Profiling

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The missing link

Professionalism = Going over and above regulation

Risk Profiling = The process where Financial Planners can stamp 'professionalism' loudest
Risk Profiling

The current situation

- Ethics
- Best Practice
- Professionalism

What you will get from this session

How to go over and above the regulation
Risk Profile discussion prompts
Risk Profile Questions
Access to a survey you can use with clients
Access to aggregate data from the surveys

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What you will get from this session

How to go over and above the regulation

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Risk Profile Questions

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Current Risk Profiling

AFSL - specific
Questionnaires
Philosophy
Inherently tied to asset allocation
Psychological Research

Self-Control
- Predictor of Financial Behaviour
  (more than Financial Literacy!)
- Impact on your processes

Optimism
- Optimism Bias > Inaccurate Forecasting
- Business owners are overly optimistic
- Lower fee sensitivity
- Impact on your processes

Financial Literacy
- Helps people in financial shock
- Financial literacy programs

Risk Tolerance
- Business owners are highly risk tolerant
- Female-headed households
- Irrational behaviour

Experience
- Train lower dilemma
- What does that teach us?
Experiments

Train Lever Dilemma

What does that teach us?
Self-Control

- Predictor of Financial Behaviour

(more than Financial Literacy!)

- Impact on your processes

Gathergood, 2012
Self-Control Surveys

Rate these Questions on a scale of 1 to 5 (1=SA, 5=SD)

A) I am impulsive and tend to buy things even when I can’t really afford them

B) I am prepared to spend now and let the future take care of itself

C) Financial services are complicated and confusing to me
Self-Control

- Predictor of Financial Behaviour

(more than Financial Literacy!)

- Impact on your processes

Gathergood, 2012
Optimism

- Optimism Bias > Inaccurate Forecasting
- Business owners are overly optimistic
- Lower fee sensitivity
- Impact on your processes
- High Optimism:
  
  Harder working
  More savings
  Later retirement
  Select short-term debt
  Overestimate future income
Optimism Surveys

Rate these Questions on a scale of 1 to 5
(1=SA, 5=SD)

A) I can make a positive difference to my life.

B) I have the ability to help people.
Optimism

- Optimism Bias > Inaccurate Forecasting
  - Business owners are overly optimistic
  - Lower fee sensitivity
  - Impact on your processes
Financial Literacy

- Helps people in financial shock
- Financial literacy programs

Financial Literacy Surveys

4) Suppose you had $100 in a savings account and the interest rate was 2% per year. After 5 years, how much do you think you would have in the account if you left the money to grow?
   - more than $102
   - exactly $102
   - less than $102

5) Imagine that the interest rate on your savings account was 1% per year and inflation was 2% per year. After 1 year, would you be able to buy more than, exactly the same as, or less than today with the money in this account?

6) Do you think that the following statement is true or false?
   “Buying a single company stock usually provides a safer return than a stock mutual fund.”

Survey # 200X
Financial Literacy Surveys

A) Suppose you had $100 in a savings account and the interest rate was 2% per year. After 5 years, how much do you think you would have in the account if you left the money to grow:
- more than $102 - exactly $102 - less than $102?

B) Imagine that the interest rate on your savings account was 1% per year and inflation was 2% per year. After 1 year, would you be able to buy more than, exactly the same as, or less than today with the money in this account?

3) Do you think that the following statement is true or false?
   “Buying a single company stock usually provides a safer return than a stock mutual fund.”
Risk Tolerance

- Business owners are highly risk tolerant
- Female-headed households
- Irrational behaviour
Objective Risk Tolerance Measures

Higher Risk Tolerance for clients with:
- More years to retirement
- More liquid assets
- Higher monthly investment earnings
- Male and couples
- Homeowners with mortgages

Sung and Hanna (1996)
How does this relate to how a professional risk profiling process looks like?

- Discussions
- Survey questions for clients
- Self-survey and reflect
Psychological Research

Self-Control
- Predictor of Financial Behaviour (more than Financial Literacy!)
- Impact on your processes

Optimism
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Financial Literacy
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Experiences
- Train, Learn, Decide
- What does that teach us?
Adding value

Investment Philosophy

Risk Profiling - Discussion and Survey

Break the investment return link to value

Investment philosophies
- Life-cycle vs Dynamic Strategies
- Asset allocation alignment
- One-size-fits-all (Default funds)
- Human capital
Investment philosophies

- Life-cycle vs Dynamic Strategies
- Asset allocation alignment
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Conclusion

Professionalism is ethics and client empowerment

Risk Profiling is the chance for Professionalism

Discussions around risk profiling issues

Alternative survey questions (additional)

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References


