

Discussion of

“Individual Judgment and Trust Formation: An Experimental Investigation of Online Financial Advice”

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Overview

Big Question: Why do individuals trust financial advisers who have been shown to give self-interested advice?

Fund level: Bergstresser, Chalmers, Tufano (2009), Christoffersen, Evans, Musto (2013), Del Guercio and Reuter (2014).

Individual level: Anagol, Cole, Sarkar (2012), Mullainathan, Noth, Schoar (2012), Hackethal, Inderst, Meyer (2012), Chalmers and Reuter (2014).

Authors run an “incentivized” online experiment to explore two possible sources of trust formation:

1. Strategic behavior by advisers.
2. Faith in professional credentials.

Empirical evidence is consistent with both possibilities.

Policy recommendation: Credentials based on rigorous exams **plus** advisers as fiduciaries.

Outline of Discussion

- Place paper into broader existing literature
- Possible tweaks to analysis given existing data
- Possible extensions for future iterations of the experiment
- Caveats to policy recommendations?

“Video advice, so hot right now”

- **Berg and Zia (2014):**

- Introduce storyline about the pitfalls of high-cost (store) debt into South African soap opera “Scandal!”
- Those invited to watch “Scandal!” exhibit better borrowing behavior than those invited to watch “control” soap opera.
 - *Approach is limited by the number of finance-based storylines that viewers (and advertisers) are willing to tolerate.*

- **Carlin, Jiang, Spiller (2014):**

- Produce “cartoon in which a TV viewer uses a ‘magic remote’ to uncover hidden messages while watching a credit card commercial”
- Version showing how to read list of credit card fees associated with better credit card choices (in the experiment)... *but less sharing.*
 - *Inherent tension between education and entertainment?*
- Participants who see through misleading claims are more likely to share. Others exposed to misleading claims are less likely to share.
 - *Authors worry that firms can take strategic actions to limit sharing.*

“Video advice, so hot right now”

- **Lusardi, Samek, Kapteyn, Glinert, Hung, Heinberg (2014):**
 - Create four online educational programs to teach participants about risk diversification and evaluate their effectiveness.
 - All programs are effective, but video is more effective than written narrative.
 - *Education is more effective when it is more engaging.*
- **These papers are more closely aligned with literature on financial education than literature on financial advice**
 - **Tension between education and entertainment—which I feel every semester—is missing from this paper.**
 - Authors purposefully minimize variation in advice delivery.
 - **Authors do not attempt to vary how advice or credentials are perceived by participants**
 - **Authors do not explore correlation between trustworthiness and learning; trust in adviser may crowd out learning/updating in the same way that defaults may crowd out active choice**

“Strong... To Quite Strong?”

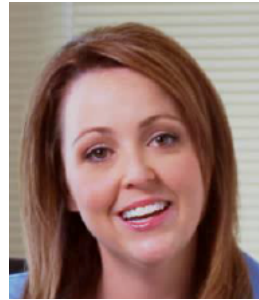
Big Question: Why do individuals trust financial advisers who have been shown to give self-interested advice?

Third possibility: Counterfactual choices would be worse.

- Chalmers and Reuter (2014): For some participants, bad advice is better than no advice.
- Gennaioli, Shleifer, Vishny (2014): Larger the gains from trade with trusted advisers, the higher the observed fees.
- Hackethal, Inderst, Meyer (2012): More trusting clients generate higher bank revenues.
- Georgarakos and Inderst (2011): Less literate are more trusting.

Suggest important interaction between financial literacy and trust formation that is not currently explored in this paper.

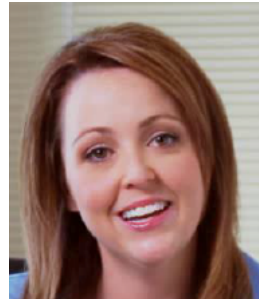
Range of Experimental Variation



Topic	Easy or Hard	Claire Harris <i>Young Female</i>	David Forbes <i>Old Male</i>	Elizabeth Turner <i>Old Female</i>	Michael Adams <i>Young Male</i>
Topic 1		G B	G B	G B	G B
Topic 2		G B	G B	G B	G B
Topic 3		G B	G B	G B	G B
Topic 4		G B	G B	G B	G B

*Advice on Topic # can be **Good** or **Bad***

Example of Advice Received



*Both give same quantity of **G** and **B** advice, but Claire's **B** advice is easier to detect*

Topic	Easy or Hard	Claire Harris <i>Young Female</i>		David Forbes <i>Old Male</i>		Elizabeth Turner <i>Old Female</i>		Michael Adams <i>Young Male</i>	
		G	B	G	B	G	B	G	B
Debt	E	G	B	G	B	G	B	G	B
Diversification	H	G	B	G	B	G	B	G	B
Fees	H	G	B	G	B	G	B	G	B
Consolidation	E	G	B	G	B	G	B	G	B

1st Set of Findings: Credentials

- After each set of videos, participants are asked to pick the advisor who offered the better advice to them.
 - **4.5 pp** more likely when labeled “Certified Financial Planner”.
 - **62.7 pp** less likely when advisor gives bad advice.
 - **Effect should vary across Easy and Hard topics.**
 - **4.3 pp** less likely when above median financial literacy... but only significant at 10-percent level and there are more than 10 participant characteristics.
 - **Interactions between adviser and participant characteristics?**
 - Evidence in Table D.2 that same advisor chosen across topics
→ Differential effect depending on whether initial advice was good (or good and easy)? **Good 1st impression limit updating?**
 - **Weight placed on credentials decrease from 1st to 4th topic?**
 - **Effects stronger for subset most likely to seek out adviser in real life?**

2nd Set of Findings: Strategery

- After all four sets of videos, participants are asked to choose which advisor is more trustworthy, competent, attractive, etc.
 - Figure 3 exploits variation in sequencing of of **Good** versus **Bad** advice interacted with sequencing of **Easy** and **Hard** topics.
 - Holding advice sequence constant, better for advisers to give **G** initial advice on **E** topic and **B** initial advice on a **H** topic:

$$\begin{bmatrix} \text{GBBG} \\ \text{EHHE} \end{bmatrix} > \begin{bmatrix} \text{GBBG} \\ \text{HEEH} \end{bmatrix} \quad \& \quad \begin{bmatrix} \text{BGGB} \\ \text{HEEH} \end{bmatrix} > \begin{bmatrix} \text{BGGB} \\ \text{EHHE} \end{bmatrix}$$

- Implication that when advisers give good advice on easy topics, they can give bad advice on hard topics without damaging trust
 - Strategic behavior consistent with Mullainathan et al (2012)
 - Expect weaker effects for participants who correctly answer literacy questions about diversification (Hard topic)?
 - Caveat: $\text{Pr}(\text{Correct}) \gg 50\%$ for all topics in pre-test.

Limitations & Extensions

There are significant differences between short, online interactions and longer, face-to-face interactions

- Limited opportunities for—or analysis of—learning.
- No portfolio outcomes that might reveal bad advice.
- No opportunities for advisers to increase trust through good listening skills or birthday cards.

Simple Extensions:

- Does explaining “Certified Financial Planner” certificate to random subset of participants increase its impact?
- Does showing an advertisement that is implicitly giving bad advice (Putnam: “Mercedes Benz of Funds”) benefit advisers giving the same bad advice?

Policy Implications

Finding:

1. Clients are more likely to listen to advisers with credentials
2. Trust not harmed when advisers give bad advice on hard topics

Leads authors to recommend:

1. Rigorous exams to become certified financial adviser
2. Advisers held to fiduciary standard

Caveats:

- Ignores potential strategic responses.
- DOL proposal to apply fiduciary standards to IRA rollovers strongly opposed by industry. One or more claims that they could not serve small accounts as fiduciaries.
- Pre-testing implies “Master Financial Planner” (fictitious) almost as trustworthy as “Certified Financial Planner” (actual).

Conclusion

- Very interesting and creative paper on an important topic.
- Experiment variation in advice quality may be the only practical way to study the impact of advice quality on perceived trustworthiness.
 - No one is willing to let me experiment on actual investors!
- Findings are completely believable.
- I look forward to seeing how the authors extend the experiment in future papers.