BORN TO SPEND?

BY JESSICA HUBBARD

SOUTH AFRICANS SPEND ALMOST FOUR TIMES MORE ON ALCOHOL THAN ON OUT-OF-POCKET HEALTHCARE, AND ABOUT THE SAME ON DSTV SUBSCRIPTIONS AS ON RETIREMENT ANNUITIES.

WHY?

BECAUSE "RETIREMENT IS FREE AND RAs ARE NOT AS ENTERTAINING AS DSTV".

These were some of the findings (and conclusions) that consulting firm Eighty20 released last year in its *Conspicuous Consumption report*, which drew on data from Statistics SA's *Income and Expenditure Survey* and other sources. While some of Eighty20's sound bite-friendly claims raised eyebrows and caused many to question the validity of the numbers, the report nevertheless drew much-needed attention to our spending habits – and the drivers behind them.

According to Eighty20, households earning up to R3 500 a month spend 8% of it on clothing and footwear, and 2% on education while those with between R3 500 and R10 000 a month spend 7% on clothing and footwear, and 3% on education. The report points out that Edgars sold R25bn worth of merchandise in the 2013 financial year; and the retailer has over 3.8m store-card holders. Just over 50% of all sales are on credit.

A recent blog post by 22seven, the Cape Town-based personal financial management service, stated that its users spend about 10 times more money on their cars than on their savings.

If we take our lead from these findings, we can pretty much assume that, as a nation, we are a bunch of narcissistic spendthrifts. ■

1. VAIN OR... WELL, JUST HUMAN?

IN ITS REPORT, Eighty20 attributed some of this spending behaviour to 'status anxiety', and the need to be seen sporting certain labels and driving the right car. Others, when commenting on the way in which South Africans spend, look to the so-called 'Black Diamond' phenomenon and the emerging black middle class's need to brazenly display its newfound wealth. If you frequent Parkhurst in Johannesburg on a Saturday afternoon, you might well attribute it to pure hubris and a great deal of raging hormones.

However, what if making foolish decisions about how we spend our money, just as we make foolish decisions about what we eat and drink on a daily basis, is simply human nature – part of our genetic makeup?

Instead of pointing the finger at big, bad banks and conniving advertisers who dangle bargains and hot models in our faces, should we not just admit that we are human beings and woefully prone to impulsive, irrational behaviour – even when it comes to our money?

For the growing band of academics, financial professionals, policymakers and entrepreneurs worldwide who are ploughing into the ever widening field of behavioural economics (and one of its 'subsets', behavioural finance), getting to grips with our 'humanness' is a critical place to start when it comes to money matters. ■

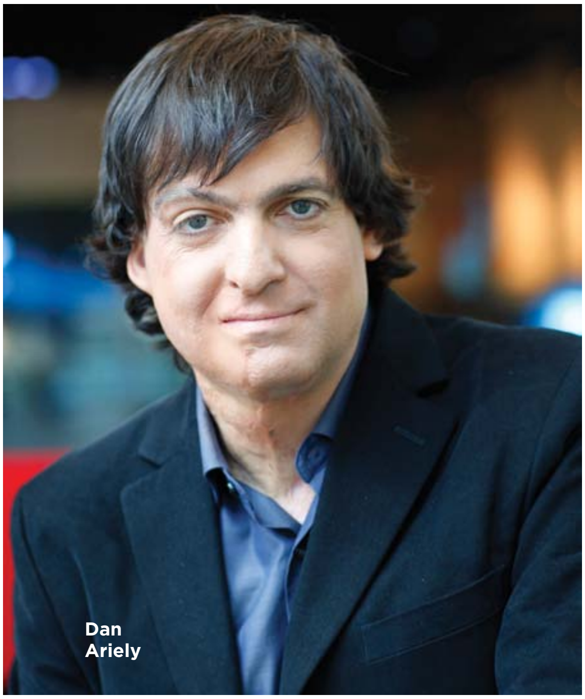
2. HARDWIRED TO BE HOTHEADED?

PUT SIMPLY, BEHAVIOURAL economics combines the fields of psychology and economics, and many within the financial and public policy realms are using it to figure out how our natural tendencies – or psychological 'blind spots' so to speak – prevent us from making sage decisions around our rands and cents, and ultimately, our futures.

For example, behaviourists insist that we are hardwired for immediate, short-term gains (damn that dopamine!) and we are irrationally afraid of loss. In the oft-cited behaviourist experiment, subjects have to choose between a sure-fire R3 000 loss and an 80% chance of losing R4 000; or the 20% chance of losing nothing. The majority of people go for the second option, even though it's not the mathematically sound choice. (To spell this out, an 80% chance of losing R4 000 works out to an average loss of R3 200; so it's better to lose an even R3 000, right?)

Yet the thought of enduring a loss when there's even a vague chance of avoiding it runs against our caveman tendencies.

These instinctive responses to the 'real world' can easily lead us into some pretty hairy financial scenarios, ranging from monstrous credit card debt to, well, hairy debt collectors breaking down our front doors. ■



Dan Ariely

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3. MAINSTREAM ECONOMICS

FORTUNATELY, THERE ARE some really smart people who are now doing more than just publishing academic papers on the topic. Behavioural economics has undoubtedly progressed from being a cool-sounding concept bandied about in classrooms to a discipline that is attempting to fundamentally alter our approach to personal finance (and much more, like public policy... but let's stick to finance for now). Since its emergence as a formally recognised and respected field of scholarly inquiry in the Seventies or thereabouts, behavioural economics has firmly entered the mainstream – producing a Nobel Prize, a growing treasure trove of empirical research, and a remarkably consistent record (annoyingly so, for many) of turning traditional or neoclassical approaches to economics very firmly on their heads.

Predictably Irrational, a book written by Dan Ariely, a behavioural economist at Duke University, spent 11 weeks on *The New York Times* bestseller list and got many decision-makers worldwide interested in behavioural economics and its potential role in both personal finance and policymaking. ■

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U.S. President Barack Obama awards the Presidential Medal of Freedom to Daniel Kahneman

> "THE PROBLEM IS THE MARKET DOESN'T PROTECT US FROM OUR OWN FOLLY... IF WHAT WE WANT IS TO IMPROVE PEOPLE'S CHOICES WITHOUT ELIMINATING THEIR FREEDOM, THEN I THINK BEHAVIOURAL ECONOMICS IS VERY HELPFUL."
>
> **DANIEL KAHNEMAN**

4. 'PROTECTING US FROM OUR OWN FOLLY'

PSYCHOLOGIST DANIEL KAHNEMAN, who won the aforementioned Nobel Prize for his groundbreaking work on behavioural economics in 2002, has commented that "the problem is the market doesn't protect us from our own folly... if what we want is to improve people's choices without eliminating their freedom, then I think behavioural economics is very helpful."

Given the many real world applications of behavioural economics, this is quite the understatement. In the US, for example, Barack Obama has drawn on solutions put forward by renowned behaviourists Cass Sunstein and Richard Thaler to shape his retirement savings programmes.

In 2006, Barclays became the first bank to establish a dedicated Behavioural Finance division in its London office, and told *Vanity Fair* that this team became "an integral part not only of the service offered to the clients of the Barclays Wealth and Investment Management division but also of the overall strategy of the bank as a whole".

The British government even has its own Behavioural Insights Team, which hunts around for "policy tweaks that help our psychological quirks work for us", as *The Economist* elegantly described it. Dubbed the 'Nudge Unit', the Insights Team was inspired by the famous 2008 book *Nudge*, authored by Sunstein and Thaler, which reportedly made a big impression on David Cameron before he made it to 10 Downing Street. ■

5. PERSONAL FINANCE PIONEERS

WHILE WE CANNOT boast our own governmental 'Nudge Unit', SA has its own band of behaviourists who are drawing on the discipline to help people make better decisions around their finances. Given the reams of depressing evidence about our reckless spending habits – not to mention our dismal national savings rate – we clearly need the help.

Entrepreneur and founder of 22seven, Christo Davel is one of the local pioneers of the concept, and he explained to *Finweek* that behavioural economics is at the core of the thinking behind the personal financial management start-up that he launched in January 2012 (and was later acquired by Old Mutual).

Davel says that he was initially inspired by a TED Talks video that featured the behaviourist author and thought leader Dan Ariely, and later managed to get in contact with the celebrated professor. A trip to Duke University followed, during which Davel laid the groundwork for a working partnership between Ariely and the young 22seven.

"Ariely invited me to participate in seminars and discussions with his students, and there was so much great information flying around it was like trying to sip from a fire hydrant," recalls Davel.

Davel returned to SA with fresh ideas and inspiration for the application of behavioural theory – determined to create a service that would "be awesome for the end user", adding that in local financial services, "nobody had really played a hand in this space yet".

To gently nudge people into making smarter decisions around spending, 22seven seeks to gather users' financial data into one place, present it in such a way that a user can see exactly how much he spends (and where) every month, and inspire him to ultimately see, think, and do things differently.

"I cannot overstress how the in-your-face awareness works and how powerful it really is when you are presented with the data," Davel explains. "Once you can see what you spend and where, we ask you the question, is there any way you could do things differently?"

6. LONG-TERM PLANNING

WHILE DAVEL AND his team are looking to guide people in their day-to-day decisions around money, another passionate behavioural sciences advocate, Warren Ingram of Galileo Capital, draws on the discipline to help clients make the heftier decisions around long-term investments and retirement.

"We [Galileo Capital] built our entire business model and financial proposition around the principles of behavioural finance," Ingram explained to *Finweek*. "Both Theo Vorster [CEO of Galileo] and myself came from large financial institutions before we founded Galileo in 2005, and we were very aware of why the whole industry doesn't really work for people."

"Clients don't always get the full benefit [of financial services]," he adds, "because the industry is skewed toward benefitting the product providers".

To change this dynamic, Ingram says that he kicks off any client relationship by firmly anchoring clients with realistic expectations, and getting a feel for their attitudes toward money and the markets.

"We look at what your current situation is, and try to assess whether you can tolerate major losses, for example. Are you highly risk averse? Unfortunately, that is a conversation that generally doesn't happen in the industry, worldwide," says Ingram.

To gain insight into a client's tolerance

Christo Davel

"I CANNOT OVERSTRESS HOW THE IN-YOUR-FACE AWARENESS WORKS AND HOW POWERFUL IT REALLY IS WHEN YOU ARE PRESENTED WITH THE DATA. ONCE YOU CAN SEE WHAT YOU SPEND, WE ASK YOU THE QUESTION, IS THERE ANY WAY YOU COULD DO THINGS DIFFERENTLY?"
CHRISTO DAVEL

Gallo Images/Getty Images

for market risk and volatility, Ingram applies similar strategies to those used by the Barclays Behavioural Finance team.

He uses FinaMetrica, for example, which is a risk-profiling tool that he describes as "almost a psychometric test for clients…" So by gaining a more in-depth understanding of his clients and their tendencies around money, Ingram can tailor his investment and retirement plans to fit each individual.

7. DRAWING ON THE DATA

WITH THE INCREASING availability of these types of tools, as well as growing access to big data, the scope for behavioural sciences to further impact financial services and solutions is exciting.

Nicola Kleyn, deputy dean at the Gordon Institute of Business Science (Gibs), highlights the fact that this is really only the beginning for local application.

"The emergence of big data has resulted in increased awareness of the opportunities to concentrate not only on what consumers think, but also on their behaviour across all of their financial interactions," she explains. "Behavioural science focuses on understanding and explaining human choices and behaviour… unlike attitudinal research which focuses on asking what they think, the main thrust of data gathering in behavioural science is through the design of experiments – either in artificially created settings [the lab] or in everyday life [the field]. In my interactions with financial services providers, I'm hearing reference to behavioural economics more and more."

Kleyn adds: "Having said that, I think the focus on designing good data gathering procedures to test clear hypotheses is only starting to take off in South Africa."

8. DOWN TO YOU

FOR THE MAJORITY of South Africans, who don't have access to streamlined money-management tools and forward-thinking financial advisers, one of the most obvious and immediate solutions is straightforward financial literacy training and education. This is slowly becoming a priority on the corporate agenda, although we undoubtedly have a long way to go.

"While I firmly believe in the consumer's right to choose whether to spend today or tomorrow, it needs to be an informed choice," Kleyn says. "Given our low levels of financial literacy, business needs to partner with Government to invest in driving sustainable consumption patterns in order to not only avoid writing off significant bad debts that result in poor organisational and country performance, but to ensure that they play their role in building a 'tomorrow-focused' economy."

Yet while we can look to economists, advisers and policymakers to install what Duke Professor Ariely has termed 'guardrails' in the system to shield us from our own 'folly', we ultimately have to rely on our own wits and willpower to avoid getting lost in the financial wilderness. ■

WATCH WHAT YOU SAY – YOUR LANGUAGE COULD BE MAKING YOU POOR!

Keith Chen

IT SOUNDS A little funky, but let's face it – linguists have been telling us for years that the way we read, write, and talk shapes the way we see the world. So why shouldn't our language have an impact on our financial behaviour as well?

This is precisely what behavioural economist Keith Chen is proposing. Chen has published research that suggests speakers of languages without strong future tenses tended to be more responsible about planning for the future.

"After scouring many datasets with millions of records on individual household savings behaviour – along with a number of peculiar health performance metrics like grip strength and walking speed – I find that languages that oblige speakers to grammatically separate the future from the present lead them to invest less in the future," Chen explained on his TED Blog last year. "Speakers of such languages save less, retire with less wealth, smoke more, practise more unsafe sex and are more obese. Surprisingly, this effect persists even after controlling for a speaker's education, income, family structure and religion."

According to Chen, language could account for the fact that "Germans save 10 percentage points more than the British do [as a fraction of GDP] while Estonians and Chinese save a whopping 20 percentage points more than Greeks and Indians."

What then, does that say about South Africans? Eina! ■

APPLYING BEHAVIOURAL SCIENCES IN THE WORKPLACE

***Finweek* chatted with Erik Vermeulen, a behavioural economics strategist, to find out how the principles of behavioural economics can be applied in the workplace to achieve business goals.**

1. IN YOUR CORPORATE CONSULTING WORK, WHAT ARE SOME OF THE MOST COMMON BEHAVIOURAL PROBLEMS YOU ARE PRESENTED WITH?

» For the most part, I look at companies as a whole in terms of the behaviours that they would require in order to achieve strategic objectives.

Very often, I bridge the gap between marketing and HR. The disconnect exists because the marketing department comes up with great ideas about what the company promises, but somehow this seldom gets transferred into the behaviour of employees.

Yet the only way customers can gauge if a company lives its brand promise is through the consistent behaviours of employees at all touchpoints. The most common problems I have to resolve stem from the fact that brands change – and their promises to customers change – but employee behaviours seldom change along with them. ■

THE WAY TO MOTIVATE EMPLOYEES IN TODAY'S BUSINESS WORLD IS TO 'UPGRADE' TO AUTONOMY, MASTERY AND PURPOSE:

AUTONOMY: the desire to direct our own lives.
MASTERY: the urge to get better at something that matters.
PURPOSE: fulfilling the yearning to do work that serves something larger than us.

» Research shows that today's young employees (under the age of 35) do not rate money as the most important form of compensation. They look at a range of non-monetary factors ranging from 'a great team', to 'the ability to give back to society through work'. Essentially, they want four things to be present: a sense of progress; connectedness; control and meaning.

2. WHAT MISTAKES DO EMPLOYERS CONSISTENTLY MAKE WHEN TRYING TO CHANGE EMPLOYEE BEHAVIOUR?

» Not understanding the modern trends in motivation. Almost without exception, the companies that I come into contact with are still stuck on the 'carrot' way of motivating employees – which is the way we used to do it in the Nineties! ■

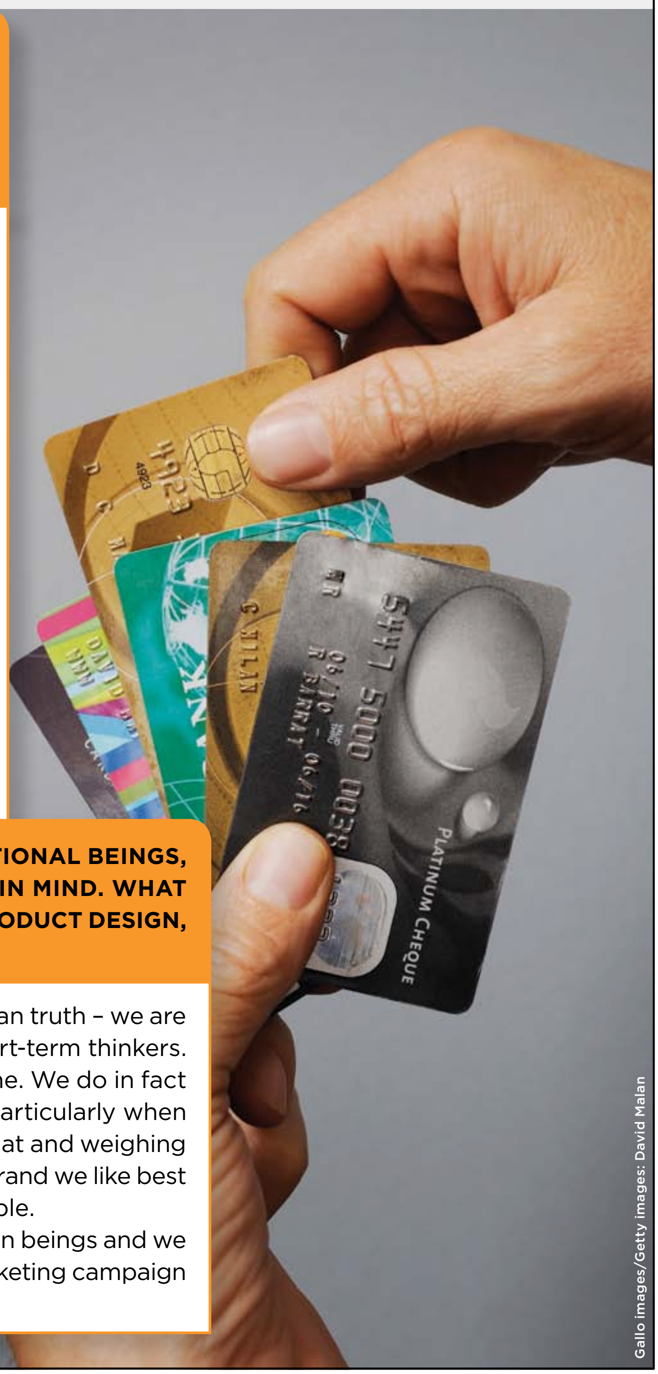
3. ARE SA BUSINESS LEADERS, BRANDS AND MARKETERS BECOMING AWARE OF BEHAVIOURAL ECONOMICS AS A CONCEPT AND BEGINNING TO LEVERAGE IT?

» If brands are truly 'problem-solvers' – in other words, they see themselves as indispensable by providing a product or service that their customers cannot live without – they had better start taking notice of the irrational decision-making forces that shape the decisions of their customers. Understanding how and why customers and employees make choices is to the modern business what TV advertising was from the Sixties to the Eighties.

I find that SA companies are not yet fully grasping the significance of this understanding and if the marketing team gets it, often budgets get in the way of exploring the science and implementing key lessons. They are becoming aware of it, but they're a few years behind leveraging it the way that US and European companies are. ■

BRANDING AND BEHAVIOURAL SCIENCES

How do brands leverage behavioural sciences to tie in to our human folly? We chatted with Honore Gasa, Customer Insights Director at Yellowwood Future Architects, to glean insights from the 'other side'.



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1. BUYING CERTAIN PRODUCTS AND SERVICES IS OFTEN AN EMOTIONAL EXPERIENCE – AND IN FINANCE, ADVISERS WORK TO KEEP EMOTIONS OUT OF IT. IN BRANDING AND MARKETING, ARE YOU DOING THE OPPOSITE – I.E. TRYING TO KEEP EMOTIONS PART OF IT?

» Yes, in marketing we are (or should be) trying to do the opposite. Choosing and continuing to use a brand is very similar to choosing and continuing to be in a relationship with someone (see Dr Jan Hofmeyr's theory of commitment).

There is plenty of strong evidence that, even in supposedly fact-based product and service categories, emotions play an important role in brand or provider choice. For a start, whether or not we trust the very adviser who is giving us advice is largely an emotional reaction to the adviser.

There are myriad options for us to choose from in any given category. We may do extensive searches for information and facts, particularly in those categories where the investment or risk of making an incorrect decision is high. However, how do we go about choosing the institutions, brands or services that we are going to investigate more fully? The simple truth is that we assemble a 'competitive set' based on what we have heard and whether we think the brand could meet our needs or can be trusted. ■

2. BEHAVIOURAL ECONOMISTS SAY THAT WE ARE IRRATIONAL BEINGS, ACTING ON IMPULSE AND WITH ONLY THE SHORT TERM IN MIND. WHAT DOES THIS MEAN FOR BRANDS AND THEIR CAMPAIGNS, PRODUCT DESIGN, AND SO ON?

» The above suggests that we are emotional beings – a human truth – we are not robots. However, we are not completely irrational or short-term thinkers. This would be taking the 'emotional' argument to the extreme. We do in fact spend time weighing up the pros and cons of our choices, particularly when the investment is large or risky, and this does include looking at and weighing up the facts. We are quite capable of walking away from the brand we like best and moving to a substitute that is more prac-tical or affordable.

The truth is that we are both rational and irrational as human beings and we use a good dose of each to make any decision. Any good marketing campaign or product design will take both aspects into account. ■