

"Consumer in Financial Crisis: Lessons Learned and Ways Forward"

# Financial Advice and Sales

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# Outline

- **The Basic Nature of Financial Products.**
- **Dangerous Framework of the Client's Financial Decision Making.**
- **Natural Conflicts of Interest in Selling Financial Products.**
- **Impartial Financial Advice Limitations.**
- **Who Should Improve the Financial Literacy of Consumers?**

# The Basic Nature of Financial Products

- **Intangible.**
- **Complex.**
- **Related to emotions.**

# Mass Media

*For bubbles to happen, information flow is the key. Media plays a significant role in disseminating information and **bubbles seem to have originated in recorded history after the advent of the print media.** In recent times electronic media particularly the television and the internet play a significant role in speeding up bubble formation and also the reversals. **Media needs a storyline and this story needs to be continued to retain customers on a daily basis.***

*Robert J. Shiller*

# Media and the Financial Bubbles

- **WSJ, 10th of March, 2000 (Nasdaq = 5000):** *"What could stop the Nasdaq's climb from here is anybody's guess... the sky seems to be the limit."*
- **Fortune, 6th of February, 2001:** *"Enron Corp. was named today the "Most Innovative Company in America" by Fortune magazine (6x)."*
- **T. Keenan, CNN FN (2001):** *"We've also tried, over the years, to find the bears to come out and give the opposite side of the story. Unfortunately, Wall Street fired a lot of the bears..."*
- **H. Kurtz, CNN (2001):** *"There's a symbiotic relationship here, television in particular, but also newspapers, need celebrity analysts, big names, because they've become a piece of programming. People want to see what they have to say."*
- **A. Murray, Wall Street Journal (2001):** *"Well, I think our job is to dramatize good stories and so I think it's no surprise that you got screaming headlines."*

# Financial Industry

*Being at once a salesman and a counselor is too much of a burden for most mortals.*

Albert Haas, New York Times, Sept 4, 1977

# The Art of Misselling

- A salesman wishing to sell a financial product:
  - misrepresents the product,
  - omits an important piece of information about the product
  - or presents the financial product as something which the client urgently needs, even though the objective analysis of the client's needs would show it doesn't hold.
- Key sources of misselling:
  - compensation based on the performance.
  - high cost of financial advice for the seller.
  - poor education of the sales channels.
  - intangibility and complexity of the financial products.

# The Client and the Psychology

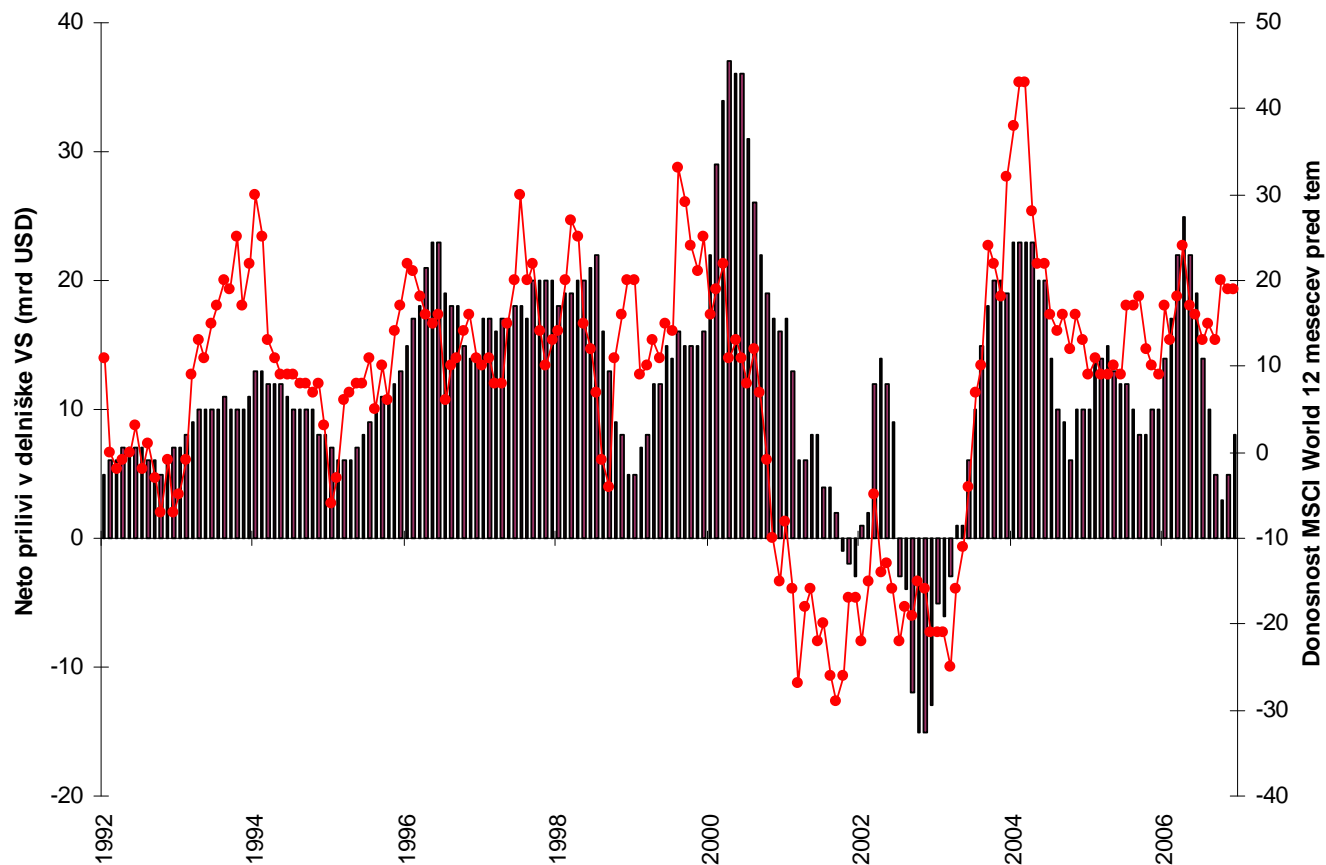
- **Financial investments in particular are strongly based on emotions:**
  - Greed, hope, fear, panic, ...
  - Mass psychology.
  - Ignorance, self confidence, illusion of control.
  - Greater fool theory.
  - ...
- **Shooting the Messenger.**

# What Does the Average Man Wish?

*The average man doesn't wish to be told that it is a bull or a bear market. What he desires is to be told specifically which particular stock to buy or sell. He wants to get something for nothing. He does not wish to work. He doesn't even wish to have to think."*

*Jesse Livermore*

# Investors' Behaviour In Practice (USA)



Source: Investment Company Institute.

# Natural conflicts of interest in selling financial products

- **Compensation formulas.**
- **Sales plans.**
- **Peer pressure.**
- **Specific interests of the financial institution.**
- **Limited product offer.**
- **Time is money.**
- **Subjective judgement & the psychology of the seller / financial institution.**

# Impartial financial advice limitations

- **The amount of time the client is willing to invest.**
- **The truth hurts.**
- **“Over the street promise.”**
- **Impartial financial advice can turn out to be “badly wrong”.**
- **Good times: “Who needs a financial advice?”**
- **Bad times: “The financial industry is spoiled anyway.”**

# Independent Financial Advice

- **Independent vs. “Independent” financial advice.**
- **Are the clients willing to pay for the independent advice?**

# Who Should Improve the Financial Literacy of Consumers?

- **Kursk tank battle vs. savings and investments.**
- **The role and limitations of consumers' associations and regulators.**
  - The minimum standards of financial advice.
  - Resources & financial innovation.
- **The responsibility of the financial institutions, media and the client itself.**
- **The lessons of the crisis: will it ever be the same?**