Psychological Influences on the Retirement Investor

by Douglas Hershey, PhD

Certified Senior Advisors (CSAs)® working in the broad field of financial and retirement planning routinely find themselves across the desk from someone seeking advice on how to plan or save for retirement. That first encounter with a client is often a detail-oriented meeting, one in which earnings profiles and pension plans are discussed, portfolio figures are disclosed, and the client is asked a handful of critical questions about his or her age, marital status, family make-up, and occupation. It almost goes without saying that the quality of service the advisor can provide is limited by what is known about the individual. Unfortunately, for many advisors, the initial interview represents an opportunity lost when it comes to collecting pertinent psychological information about the investor.

This article focuses on the various dimensions that are important to consider when constructing a *psychological profile* of a retirement investor. It is written primarily for retirement advisors, gerontological counselors, and financial service professionals who may not have the opportunity or the inclination to read retirement and financial planning articles that appear in the psychological research literature. Over the past two decades there has been a noteworthy increase in scientific papers that describe the psychological basis of retirement planning and saving, and in this paper recent key findings are summarized. Many of the findings that are cited come from studies conducted at the Retirement Planning Research Laboratory, which I direct at Oklahoma State University. The reliance on my own research and that of my collaborators is largely due to the fact that there are still relatively few psychologists who specialize in this area. However, before turning to the topic of the psychological basis of saving and investing, a psychological model of life planning will be presented that has been specifically adapted to the area of financial planning for retirement.

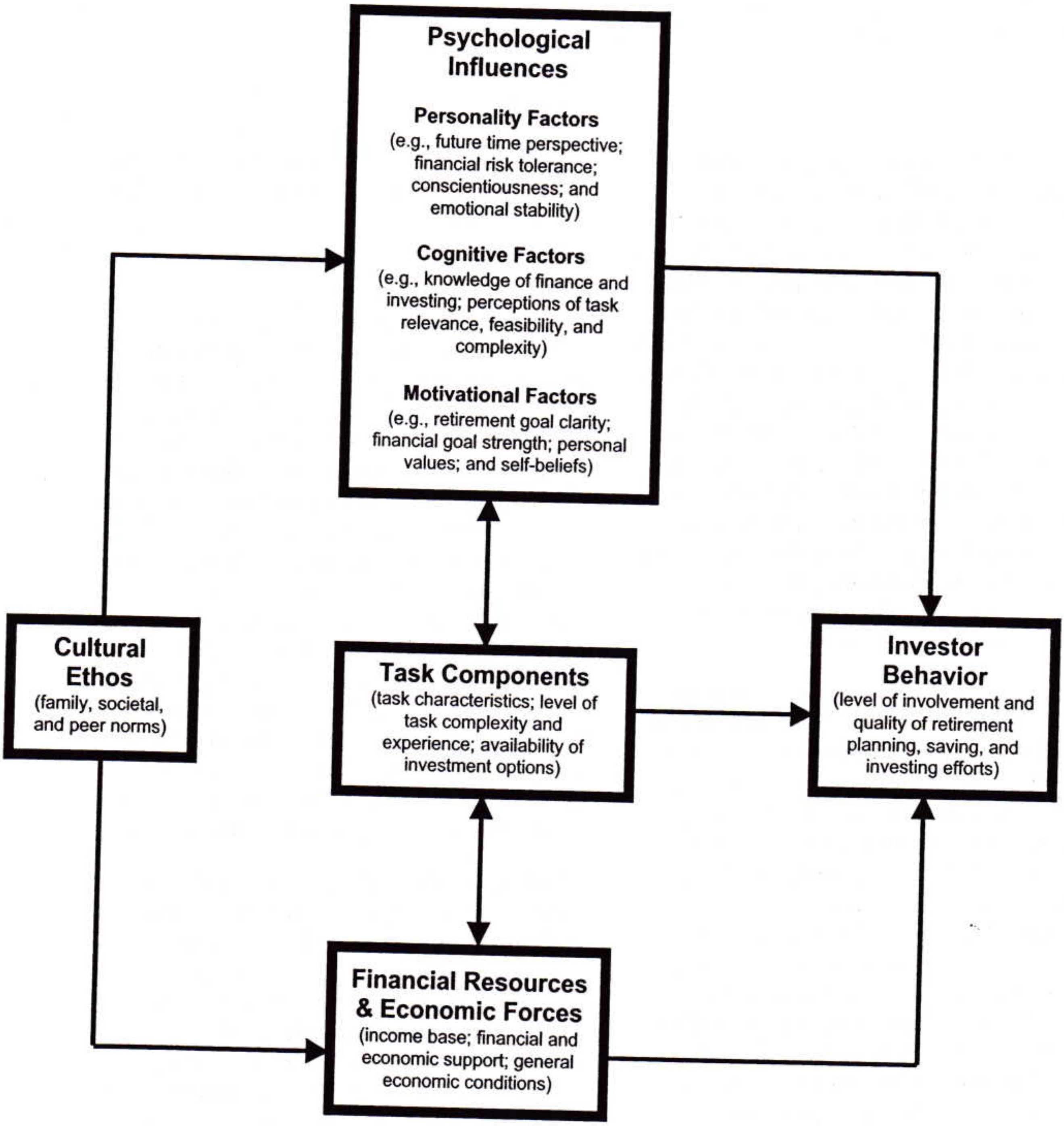
Conceptual Model

A recent model of life planning advanced by Friedman and Scholnick (1997) suggests that planning decisions and behaviors are made on the basis of four contributing factors: psychological influences, cultural influences, environmental influences, and task considerations. For the purposes of this article, elements of Friedman and Scholnick's model have been modified and recast in order to adapt them to the area of financial planning for retirement (see Figure 1). As shown in the diagram, psychological influences, such as personality traits, cognitive characteristics, and motivational factors, are all proximal determinants of investor behavior (shown on the right side of the figure). This particular dimension of the model (the psychological basis of investor behavior) will be discussed in greater detail in the following section of this article.

Task components constitute a second major influence on the planning and decision processes of the investor. Examples of task components include the availability of investment options, availability of employer pension plan options, and the complexity of the planning, saving, or investing task (which, as it turns out, is typically related to one's prior level of financial planning experience, itself a task component). Task-related issues include activities that are long-range in nature, such as considering the tax planning implications of an investment, as well as day-to-day activities such as monitoring one's portfolio.

Financial resources and economic forces (which correspond to environmental influences in the

Figure 1: Conceptual model of the factors that influence investor behavior.



Friedman and Scholnick model) represent a third factor that has a direct impact on investor behavior. Financial resources include, among other things, an individual's income base, current savings and assets, and discretionary income. Also included in this category are sources of support for the investor, such as information and advice gained from other persons (e.g., financial advisor, friends, spouse), educational materials (e.g., books, pamphlets, newsletters), and technological resources (e.g., computer programs, Internet resources). At much a broader level, this factor includes relatively long-term economic patterns and trends, changes in tax legislation that open up new forms of investment opportunities, and dynamic shifts in financial markets that may temporarily stimulate or dampen investor enthusiasm.

Represented on the left side of the diagram are a variety of sociocultural influences that are collectively referred to as the *cultural ethos*. The cultural ethos is a rich collection of social forces that stem from family, societal, and peer group norms. Taken together, they represent cultural forces that shape not only an individual's psychological tendencies and predispositions, but also the availability of financial resources and to some extent the nature of prevailing economic forces.

Collectively, the four factors shown in this conceptual model represent the "pushes" and "pulls" that determine whether or not one will plan, save, and invest for retirement. Among those who already have established a retirement portfolio, these same four factors presumably influence perceptions of gains and losses, and they largely dictate how resources will be allocated and manipulated on an ongoing basis. One point worth mentioning about the model is that the four factors interact with one another (note the pair of double-headed arrows, suggesting reciprocal influences) in a dynamic fashion.

In general, sociological researchers have focused their attention on the relationship between the cultural ethos and investor behavior (a direct link not shown in the model), and economists have focused on the link between financial/economic resources and investor behavior (the arrow shown in the bottom right corner of the figure). Psychologists, who, compared to sociologists and economists are relative newcomers to this research area, have focused the majority of their attention on the way in which psychological and task characteristics influence investor behavior. Members of the former two disciplines have focused a great deal of attention on the way in which demographic variables are related to investor behavior. In general, findings from this work indicate that financial advisors could benefit by obtaining a complete set of demographic information (as well as psychological data) when working with clients.

Demographic Profiling

As suggested in the introduction to this article, much can be learned about a client from answers to a few well-chosen demographic questions. Sketching a quick *demographic profile* of an investor allows the advisor to make a variety of probabilistic assumptions about the individual's financial needs, goals, and long-term plans — many of which will likely hit the nail on the head. However, demographic profiling is useful only to the extent that individual demographic indicators provide insights into the investor's *psychological* planning and saving predispositions. In other words, demographic markers serve as "proxy" variables when it comes to predicting the psychological basis of an investor's predilections. By buttressing a demographic profile with a brief psychological assessment, the advisor will gain a better understanding of the client and, on that basis, be able to fine-tune long-range strategic goals and plans. Fortunately, formal training in psychology is not a prerequisite to conducting a psychological assessment, which can be carried out quickly, efficiently, and in a non-invasive manner. The following sections of the article describe a number of dimensions that are worth exploring when developing a psychological profile of a client.