

Human-Centric Investing Podcast

January 2, 2018

Episode 12 – Breaking the Habit of Putting Off Hard Decisions

Host: Farnoosh Torabi, personal finance expert, Bloomberg Media Studios

Featured Guest: Professor David Laibson, Harvard University Economics Department

This podcast is brought to you by Hartford Funds.

Farnoosh Torabi: How can financial advisors improve their clients' satisfaction by truly understanding the psychology through which clients make choices? Welcome to a special edition of Hartford Funds Human-centric Investing Podcast. I'm your host, personal finance expert Farnoosh Torabi of Bloomberg Media Studios.

Today we're exploring what's called 'present bias.' It is the tendency to make choices that are biased toward whatever is easiest to do right now. We'll explore how you can help your clients overcome this very human inclination to put off the hard decisions. We're joined by one of the intellectual godfathers of behavioral economics, Professor David Laibson. He chairs the economics department at Harvard University and he leads the university's Foundations of Human Behavior initiative.

David, welcome to the podcast.

David Laibson: Glad to be here.

Farnoosh Torabi: I'm very happy to say that I worked out this morning. Isn't that great? I'm, I'm really proud of this, because there were probably-

David Laibson: That makes one of us.

Farnoosh Torabi: (laughing) There were probably a million reasons I could have come up with to not go to this class. And I think it does help that this particular workout class charges my credit card when I fail to show up without canceling in advance. So, that just gives you a little insight into me. That's what motivates me. Don't charge me and, uh, I'll happily show up.

David Laibson: There's seven billion people just like you.

Farnoosh Torabi: (laughs) Okay, good. I'm not alone. So, we're talking about present bias today, this human habit of putting off hard decisions, whether it's working out, saving more money. What has the research shown you?

David Laibson: So, it basically boils down to the following, uh, simple insight: What happens right now, we psychologically give full weight. What happens in the future, we psychologically give half weight, roughly speaking, which means that, if there's some unpleasant task that I need to do -- say, call my human resource office and sign up for a 401(k) plan, I don't want to do that right now. I'm gonna pay full psychological price for that half an hour of misery.

If I push it off till tomorrow, I'm only gonna pay, from today's perspective, a half psychological price, 'cause it's coming tomorrow. The effort and irritation of making that phone call, and spending that time, maybe on hold or talking with some representative, negotiating this process of enrolling in the plan, if I do it tomorrow, it's half as awful, at least as viewed from today's perspective. But you can see where this is going.

- Farnoosh Torabi: Mm-hmm (affirmative).
- David Laibson: When tomorrow arrives, once again (laughing), it's right in front of me. Now I'm gonna pay full price, and I want to push that unpleasant thing another day into the future. And in this way we postpone far too long many important things that we should be doing, and it flips on the other side. The pleasant things we pull out of the future and into the present. The bowl of ice cream. Why eat it tomorrow? Looking forward in time, it's only half as good as if I eat it right now.
- Farnoosh Torabi: So, what do you, uh, procrastinate on? I'm just curious. What's, what's something that you know you should do, but you really always push it off?
- David Laibson: Oh, I've got it all. So (laughing) ... I mean, my favorite example- Farnoosh Torabi: It happens to the best of us.
- David Laibson: (laughs) ... is the exercise one, where I went to a gym, gave the gym a thousand dollars for a one-year membership, thinking I was going to go at least two times a week, probably three times a week ... I was pretty confident ... at least two.
- So, that would be 50 weeks, a hundred visits, maybe a hundred and fifty visits. It was worth a thousand dollars for a hundred to a hundred and fifty visits to the gym. And over the next 12 months I went five times-
- Farnoosh Torabi: Yeah.
- David Laibson: ... at a cost of 200 bucks per visit. So, whether it's exercise, or cleaning my office, or grading exams, or eating well-
- Farnoosh Torabi: Mm-hmm (affirmative).
- David Laibson: ... it's all about, "Well, today I'm going to gorge myself and I'm gonna start the hard work in the future. I think I'm pretty typical relative to, uh-
- Farnoosh Torabi: Sure. You're human.
- David Laibson: ... the rest of the population. Farnoosh Torabi: Yeah.
- David Laibson: Exactly.
- Farnoosh Torabi: We've all been there. Uh, so, in my example, for me, what motivates me is knowing that there is potentially a financial ramification, a fi-, a financial, um, sort of pain point -- losing money -- in the event that I don't attend a wo-, a, a, a workout class, unless I cancel in, in, far in advance. That works for me. Is there science behind that?
- David Laibson: Absolutely. So, what's happening for you is something layering into this called 'loss aversion,' where you're feeling very badly about the loss of the money, because, "Hey, I didn't need to pay for this class that I'm not going to attend," and then that burns psychologically. And that kind of gives that extra push to get you to go.
- Um, there's many things that work to get people to actually attend the gym. Commitment is another important dimension, where people are willing to essentially sign up for something, tie their hands, whether it's maybe exercising with a friend or signing up for a class. That's kind of related to your example.

- Farnoosh Torabi: When it comes to our finances, I think inherently working with a financial advisor keeps you accountable. My husband and I initially when we got married hired a financial advisor. One of the reasons was because we wanted someone to keep us on track and to not allow us to procrastinate. And we almost felt, you know, almost accountable to this person, you know, that they're on our team, and they want, they want, uh, us to do well, and we want to, you know, follow the, the rules, and, and be good clients. And, but sometimes that's not enough, you're saying. Right?
- That advisors sometimes need to also be aware of the psychological phenomenon called procrastination. And so how can they, you know, get their clients to, um, do the work, essentially, you know, on their own and be more proactive as well?
- David Laibson: So, I think the same thing that makes a personal trainer work to get someone to exercise. You can imagine an advisor as a personal trainer in the financial domain.
- Farnoosh Torabi: Right.
- David Laibson: It's the appointment. It's the regularity. It's not just saying, "Great. I'll think about this," but rather saying, "Hey, I've got something on the calendar two- and-a-half weeks from now, and we'll sit down and we'll think about rebalancing the portfolio, or think about some estate planning questions, or getting to work on some tax efficiency." So, it's, I think, often a commitment that comes in the form of an appointment where the actual work gets done, as opposed to, "Hey, here's some advice. Go home and think about it."
- Farnoosh Torabi: "Let me know what you think at some point." (laughs)
- David Laibson: Yeah. Whenever that happens, nothing gets done. So- Farnoosh Torabi: Right.
- David Laibson: ... you know, for me, an example of that is when one of my financial advisors gave me some documents with, with regard to estate planning and said, "Hey, read these through, make comments, and then call me back (laughs)." And it took nine months for me to call him back. And it was, the mistake was trusting me to actually prioritize that. Now, of course, every day for those nine months I sat around thinking, "Boy, this is really important. I need to get these documents revised, and back to my lawyer, and signed. And every day it got postponed again.
- And we see that in the research. So, another example, uh, some work by Ned Augenblick, Muriel Niederle and Charlie Sprenger. They give people tasks and they ask them when they want to do these tasks. And people say, "Yeah, I'm com-, I'm, I'm planning to do this task in two weeks. And then when the two weeks pass, and the moment for action comes, these researchers go back to those same people say, "Okay. You said you were gonna do the task now. What is your-
- Farnoosh Torabi: (laughs) "Where are you at?"
- David Laibson: ... What is your (laughs) follow-through?" And, uh, the people, of course, tend to postpone the task yet further into the future. And we see that in study after study.
- Farnoosh Torabi: So, perhaps a good question for advisors as they're sitting down with their clients initially in the initial phase ... You know, they're getting to know them and they're asking them about their financial goals. And maybe it's worth asking, you know, "Tell me a little bit about your tendencies." Like, you can say, "From start ..." The advisor could even start and say, "I'm, I tend to procrastinate, or I tend to have a hard time with X, Y, and Z. What about you?" Because ultimately you want to make, create a relationship that makes sense, that works, that isn't maybe overly annoying, or not proactive enough, not handholding enough. You need to know where your client lies on the spectrum.

David Laibson: Yeah, though it's hard for some people to say, "I have a procrastination problem." Other people, like me, are happy to admit it.

I think one way to have that conversation implicitly is to ask people how comfortable they are setting up regular appointments.

Farnoosh Torabi: Right.

David Laibson: So, that doesn't require me to say, "The reason we're doing this is because I have a self-control problem (laughs) because I procrastinate." Maybe I'm just setting up a regular appointment. So, I think often we have these social systems that help us get the job done without being explicit, but it's helping us get the job done, because without them we would fall apart. (laughs) So, for me, I need the appointment.

Farnoosh Torabi: Mm-hmm (affirmative).

David Laibson: I need the thing on my calendar. I need the commitment

Farnoosh Torabi: Well, David, any time you want to hit the gym, I can be your accountability partner. Okay?

David Laibson: (laughs) Excellent.

Farnoosh Torabi: Let's make a date. Thank you so much. Um, and for listeners who want to learn more about the topics that we've discussed or about other ways in which psychology affects investors and their financial decisions, visit humancentricinvesting.com. Until next time, I'm Farnoosh Torabi, and this has been the Hartford Funds Human-centric Investing podcast.

Disclosure: Hartford Funds has engaged Farnoosh Torabi to conduct this interview.

Farnoosh Torabi is not an employee of Hartford Funds. David Laibson is the chair of the Harvard University Economic Department, which is not affiliated with Hartford Funds.

The views expressed herein are those of the speakers, David Laibson and Farnoosh Torabi. Hartford Funds is not responsible for, and does not validate, any information, opinions, assertions, or statements expressed in this podcast, which are for informational purposes only, and are subject to change based on prevailing market, economic, and other conditions. The views expressed may not reflect the opinions of Hartford Funds. They should not be construed as investment or fiduciary advice nor should they be considered an offer or solicitation to buy or sell any security.

Disclosure: Hartford Funds has engaged Farnoosh Torabi to conduct this interview. Farnoosh Torabi is not an employee of Hartford Funds. David Laibson is the chair of the Harvard University Economic Department, which is not affiliated with Hartford Funds.

The views expressed herein are those of the speakers, David Laibson and Farnoosh Torabi. Hartford Funds is not responsible for, and does not validate, any information, opinions, assertions, or statements expressed in this podcast, which are for informational purposes only, and are subject to change based on prevailing market, economic, and other conditions. The views expressed may not reflect the opinions of Hartford Funds. They should not be construed as investment or fiduciary advice nor should they be considered an offer or solicitation to buy or sell any security. Individual results discussed herein may not be representative of the experience of other individuals and are not a guarantee of future performance or success.