ANITA VLAM

Customer First?

The Relationship between Advisors and Consumers of Financial Products

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Klant Centraal?

De Relatie tussen Adviseurs en Consumenten van Financiële Producten

Thesis

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Preface (Voorwoord)

Vanaf het moment van mijn afstuderen aan de Economische Faculteit in Rotterdam heb ik menigmaal gezegd: 'mijn studie is nog niet klaar, ooit maak ik mijn studie af door te promoveren, maar dat komt nog wel'. Na mijn economie studie wilde ik hetgeen ik geleerd had in de praktijk gaan brengen in het bedrijfsleven. Ondertussen gingen de jaren snel voorbij en gezin, werk en politiek namen alle tijd en aandacht in beslag. Toch bleef mijn voornemen kriebelen en groeien. Na het volgen van verschillende 'master of marketing' modules bij Tias/Nimbas, welke ik een aantal jaren geleden via mijn vorige werkgever mocht volgen, was mijn latent aanwezige academische honger aangewakkerd. Mijn behoefte aan verdieping en actualisering van academische kennis en vaardigheden was weer aanwezig.

In die periode vernam ik van het Mature Talent programma van de Erasmus School of Economics. Een unieke mogelijkheid om mijn werkervaring te gebruiken voor promotieonderzoek en nog wel bij mijn 'eigen' Erasmus Universiteit. Niet alleen het feit dat ik onderzoek kon doen, maar juist naar een onderwerp uit mijn werkpraktijk en welke mij na aan het hart ligt, waren voor mij doorslaggevend om de knoop door te hakken en het onderzoek te starten.

Inmiddels zijn drie jaar verstreken en ligt het resultaat van mijn onderzoek voor u. Terugkijkend heb ik dit als een enorm leerzaam, boeiend en bijzonder proces ervaren. Het schrijven van dit proefschrift was voor mij een project waarin ik alle rollen zelf moest vervullen. Nieuwe literatuur en modellen leren, statistiek weer onder de knie krijgen, de geheimen van Global Park ontrafelen en schrijven in het Engels waren een forse uitdaging en vereisten mijn volledige inzet. Terwijl de financiële dienstverlening te maken kregen met alle gevolgen van de economische crisis voor de bankensector, bekeek ik de financiële sector vanuit een andere hoek.

Dit proefschrift had ik niet kunnen voltooien zonder de hulp en inbreng van velen. Allereerst wil ik mijn collega's van de 11^e^, het Econometrisch Instituut, danken voor hun gastvrijheid en gezellige afdelingslunches. Als niet-econometrist op deze afdeling waren de onderwerpen van hun gesprekken af en toe onbekend voor mij, maar desalniettemin heb ik er van genoten. In het bijzonder dank ik Christiaan Heij voor zijn bijdrage en hulp bij het verzamelen van de data, welke ik gebruik in hoofdstukken 3 en 4. Ook dank ik de deelnemers aan het Econometrisch Instituut seminar, voor hun positieve en kritische reacties tijdens de presentatie van mijn bevindingen van hoofdstuk 3. Peter Neuteboom ben ik dankbaar voor zijn nuttige suggesties naar aanleiding van deze presentatie.

Een speciale plek op de 11e nemen mijn verschillende kamergenoten in. Met Bart Diris heb ik de eindfase van het proefschrift kunnen delen en ervaringen kunnen uitwisselen. De gesprekken met Kristiaan Glorie over onze onderzoeksonderwerpen waren heel leerzaam. En speciaal dank ik Liesbeth Noordegraaf-Eelens. Onze gesprekken over economie, bankdirecteuren en hun uitspraken, ontwikkelingen in de financiële sector en over ons gezin waren erg boeiend en aangenaam. Haar opmerkingen over mijn vragenlijst waren zeer bruikbaar. En haar enthousiasme en belangstelling voor communicatie van bankdirecteuren hebben mij geraakt en heeft zelfs geresulteerd in het citaat, welke ik in de inleiding van dit proefschrift gebruik.

Mijn onderzoek bij de financieel adviseurs en hun klanten was niet mogelijk geweest zonder de medewerking van verschillende bedrijven in de financiële dienstverlening. Heel veel dank voor Hans van der Pouw, Ronald van Aart, Haik de Jong en Peter van Klaveren voor hun bereidwilligheid mee te werken en zo dit onderzoek mogelijk te maken. Marinus Elenbaas en Pedro Gonzalez, Mirjam Giesbers en Martin Sebregts, Pieter Leeuw en Helfred Woortmeijer, Carola Sterk-Litjens, Edwin van Tricht en Frank Rutgers dank ik heel hartelijk voor hun medewerking en zinvolle opmerkingen tijdens de feedback. Ik hoop dat ik met de resultaten hen verder heb kunnen helpen met de continue verbetering van hun dienstverlening. En natuurlijk de financieel adviseurs die ik gesproken heb naar aanleiding van de vragenlijst, dank voor jullie bijdragen. Deze waren nuttig en verhelderend. Verder ben ik Guido Willems, Wiel Zentjens, Jack Bal en Hans Mellink en al die anderen die achter de schermen betrokken waren, dankbaar voor hun hulp bij het verzamelen van de data.

Het contact met mijn Mature Talent- collega's heb ik als zeer waardevol ervaren. Wij allen stuitten op de enorme verschillen tussen ons eerdere werk in het bedrijfsleven en het werken aan een proefschrift. Onze uitwisseling van ervaringen en wetenswaardigheden tijdens onze gezamenlijke lunches waren voor mij onvergetelijk.

Verder wil ik professor Philip Hans Franses, mijn promotor, bedanken. Hij heeft het aangedurfd om mij met dit onderzoek en proefschrift te begeleiden, terwijl mijn academische kennis en vaardigheden toch wel wat gedateerd waren. Zijn enorme enthousiasme, creatieve ideeën, kennis en inzicht hebben mij door dit proces heengetrokken. Veel dank hiervoor. Ook wil ik de leden van de Promotie Commissie danken voor het invullen van hun bijzondere rol. Tot slot dank ik professor Folke Ölander die mij met zijn nuttige suggesties mijn onderzoek een zetje in de goede richting gaf.

Verder wil ik alle vrienden, oud-collega's en bekenden, die de afgelopen jaren met belangstelling naar mijn bevindingen en resultaten van het onderzoek geïnformeerd hebben, danken. Alle belangstelling uit mijn omgeving was geweldig en welkom in het soms wel solitaire bestaan van een promovendus.

De mogelijkheid dit proefschrift te schrijven en mij daar ook volledig op te kunnen richten was niet mogelijk geweest zonder mijn familie. Mijn ouders, dank dat jullie mij na mijn middelbare school hebben laten studeren. Die studie vormde de basis waaruit dit proefschrift is voortgekomen. Henk Jan, Patricia, Miranda en Rutger, een studerende echtgenote en moeder is wel wat anders dan een werkende. Jullie hebben mij overtuigd dat ik ervoor moest gaan om mijn droom te kunnen volbrengen. Henk Jan, ik heb je steun enorm gewaardeerd en altijd gevoeld dat je achter mij stond bij dit traject. Jij bent een stuk handiger met editen en opmaken van teksten dan ik en ik ben blij dat je mij hierbij hebt geholpen. Dank hiervoor! Rutger, ik zie nog je opluchting dat ik voor deze studie niet op kamers ging wonen. Af en toe thuis werken, met de hond aan mijn voeten onder het bureau, vond ook jij heel prettig en ga ik zeker missen. Patricia en Miranda, jullie enthousiasme voor het onderzoek was mede bepalend voor mij om te starten aan dit project. Ik zie met vreugde dat jullie inmiddels jullie eigen weg gekozen hebben en studeren. Ik ben heel erg trots dat jullie beiden mijn paranimfen willen zijn en op deze wijze jullie steun aan mij laten zien. Met mijn dochters aan mijn zijde kijk ik vol vertrouwen uit naar de verdediging van dit proefschrift.

Na al deze woorden van dank kom ik toch echt aan de laatste woorden van dit proefschrift. Ik heb genoten van de verschillende fasen van dit project, maar zeker van de inhoud van het onderzoek. Mijn academische honger is, voor eventjes dan, gestild.

Anita Vlam
Nieuwegein, oktober 2011

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Chapter 1:
Introduction

"The recent crisis demonstrated the critical importance of financial literacy and good financial decision making, both for the economic welfare of households and for the soundness and stability of the system as a whole."

Ben S. Bernanke, Chairman,

Board of Governors of the Federal Reserve System,

April 12, 2011

In a recent speech to the Committee on Homeland Security and Governmental Affairs of the US Senate, Chairman of the Federal Reserve Board Ben Bernanke emphasized the importance of financial literacy of individuals and good financial decision making. He postulated that informed, educated individuals achieve better outcomes for themselves by a careful choice and use of financial products. He also emphasized that these conditions of financial literacy help to improve the performance of financial markets.

The Federal Reserve Board proposes to improve individuals' knowledge of household finances through life-long financial education. This includes financial education materials and programs that expose individuals to financial concepts at an early age. To achieve this, the Federal Reserve Board collaborates with many organizations and agencies, as well as stimulating research on this topic and supporting financial education programs for consumers.

Interestingly, Bernanke indicates in his speech that the Federal Reserve Board recognizes that financial education is a "critical first line of defense", but it does not substitute strong regulation to protect customers against "abusive and fraudulent practices."

This dissertation addresses issues of financial education, where it focuses on the relationship between a consumer of financial products and his or her advisor.

1.1 Background

The situation in the Netherlands in terms of financial literacy seems similar to that in the USA. Like their American counterparts, Dutch consumers also seem to have little awareness and understanding of financial products and of the consequences of decisions on financial products. Research in the Netherlands concerning financial awareness of and attitudes towards financial products as in, for example, Antonides et al. (2008) and CentiQ (2009a,b, 2010a,b) indicates that the Dutch public only has limited knowledge about household finances. Similar research on pension decisions in van Rooij et al. (2007) arrives at the same conclusion.

There is literature that describes that early education on the relevance and use of savings increases the amount of savings as an adult (Otto et al. 2006, Webley and Nyhus 2006) and that it reduces debt problems (Lea et al. 1993). Despite this evidence, formal education of individuals is limited in the Netherlands. There are only a few programs offered by Nibud, the National Institute for Family Finance Information (available at www.nibud.nl), which are designed for VMBO (low vocational) students and elementary school children.

While education is still at an initial stage, the number of legal regulations aiming to protect consumers of financial products by providing obligatory information has increased in recent years. Also, there is increased legislation on the quality of advice provided by financial advisors. The WFT ("Wet Financieel Toezicht" in Dutch, Financial Supervision Act) is just one example. Additional to the WFT there is also an institute called the Netherlands Authority for the Financial Markets (AFM) that provides suppliers and advisors of financial products with further information on the interpretation of legislation (AFM 2007, 2009a,b, 2010a,b). The AFM can "punish" those who fail to comply with the legislation by "naming and shaming" and by imposing fines on suppliers or advisors. Banks and financial institutions strongly dislike this type of punishment, so it seems that the AFM is rather effective (van Erp 2009).

These increased educational efforts and the various legal instruments can provide an individual with more and relevant information, so that he or she gains more "responsibility for making important and complex decisions involving risks that they had not to make in the past, are not trained to make in the present, and are unlikely to execute efficiently in the future, even with attempts at education" (Merton and Bodie, 2005). Notwithstanding the efforts, suppliers and advisors still face difficulties in providing customers with sufficient and adequate information to properly make their financial choices (Prast, 2007).

The recent worldwide financial crisis also hit the financial markets and financial health of customers in the Netherlands. A committee of the Dutch Banking Association, known as the Maas Committee, analyzed the banking situation in 2009 and recommended several measures to restore and improve trust in the Dutch banking system (Adviescommissie Toekomst Banken, NVB, 2009). At present, a special committee supervises the implementation of these recommendations (Monitoring Commissie Code Banken, 2010). There was also a Dutch Parliamentary committee (the De Wit Committee, Tweede Kamer der Staten-Generaal, 2010) that investigated the causes of the financial crisis in the Netherlands and evaluated the recommendations provided by the committee of the Dutch Banking Association.

These latter recommendations concern good governance and risk management, the public role of banks, and supervision and regulation. Good governance and risk management focus on the profile of the Supervisory Board members of banks and financial institutions and on the prevention of under-appreciated risks. The public role is about the fees and variable incomes that Executive Board members receive with their short-term investments and the role of shareholders. Further, the committee recommends initiating a more European-based regulation and supervision structure.

The Dutch Banking Association (NVB) translated these recommendations into the Banking Code (2009). One of the main recommendations concerns the relationship between financial suppliers and their customers and is coined “Customer First”. In the interpretation of the Banking Code, Customer First is associated with customer-friendly activities and improved customer satisfaction. However – and this is important for the rest of this dissertation – it is widely recognized that customer-friendliness and customer satisfaction are not the key issues that made customers lose their faith in the banking system (Mentoring Banking Code, 2010). The latter committee has observed that banks still have problems defining Customer First issues. Although they have noticed that banks have been implementing new business processes to improve customer-friendliness and processes to improve new product development, they suggest that more needs to be done to regain customer trust. In fact, it appears that the key issues of individual financial literacy and the quality of individual decision making concerning financial products are still not given enough attention.

With the speech of Bernanke (2011) in mind, we would argue that Customer First has to start with an increase in financial literacy and better abilities to make sound financial decisions. For financial decision making many individuals seek advice from a financial advisor, and it is now easy to understand that an individual's financial literacy determines the quality of the relationship between advisor and advisee as well as the perceived quality of the eventual advice.

In this dissertation we study aspects of financial literacy, along with the relationship between financial advisors and customers. Aspects of interest are (perceived) transparency and fee disclosure.

1.2 Outline of this dissertation

The focus of our study is on financial literacy and on decision making concerning financial products.

In Chapter 2 we present summary statistics of the amounts of consumer loans and consumer savings in the Netherlands and various other countries. These numbers should provide a first impression of the size of these amounts. We also give some figures on various credit products, like credit card limits and overdrafts on current accounts. Special attention is given to mortgages. The gross amount of money involved in mortgages in the Netherlands is relatively high, and this was already noticed by the IMF, which issued a warning. Next, we present some recent statistics about consumer savings as a fraction of GDP. Finally we present some numbers on life insurance in the Netherlands. Various figures are also put in a European context. The main conclusions of this chapter are that debts are substantial and are increasing over time.

One possible reason for having substantial debts at the individual consumer level is financial innumeracy. In Chapter 3 we focus on one interesting aspect of financial innumeracy, and that is the way individuals deal with interest rates. Indeed, consumers often have to make decisions involving computations with interest rates. The relevant literature describes that computations with percentages and thus with interest rates represent a difficult task. With empirical data we confirm this finding. Moreover, and this is new, with these data we document that consumers are too optimistic in the sense that they believe loans are paid off sooner than is actually the case. This self-serving bias may cause people to have too much debt.

One way to make people aware of the consequences of their decisions is to include warning signals on the products. In Chapter 4 we focus on the warning signal: "Borrowing money costs money" and we examine its usefulness. As we saw in Chapter 2, consumers have substantial debts, like mortgages but also debts for loans for boats or catalog homes, and it is believed that slogans like "Borrowing money costs money" should make consumers aware of the consequences of their borrowing money. With new empirical data we show in Chapter 4 that the campaign could be made more effective if the actual size of the debt is mentioned in monetary terms.

With the understanding that financial decision making involves difficult tasks, we turn to a potential consequence and that is that consumers seek help from advisors. Typically these advisors are the very same individuals who also try to sell a financial product. In the next three chapters we focus on the relationship and the perceived quality of the advice. For that purpose we analyze a unique data set where we have interviewed customers as well as their advisors.

In Chapter 5 we discuss the survey that we used to collect the data on consumers of financial products and on their advisors. We present the design of the survey and we give various summary statistics concerning the answers. The two financial institutions that allowed us to interview their advisors and customers provided feedback and were also involved in the design of the survey to check validity.

In Chapter 6 we address the relationship between a consumer, who intends to purchase a financial product, and a financial advisor, who gives advice and at the same time tries to sell that product, where we focus on the stated and perceived expertise of the advisor. So, is the advice of the advisor useful and relevant? The relationship may involve asymmetric information, where one of the two parties can feel to be better informed than the other on various aspects of the product. Also, the advisor has two roles, that is, giving advice and sales.

In Chapter 7 we also focus on this relationship where we now address the quality of the relationship itself. Stated satisfaction levels are compared, and we find that advisors are quite confident about the quality of their advice, more so than are customers. Additionally, we find that whether the advisor's fee is disclosed or not has no impact on satisfaction levels.

In the final Chapter 8 we present a summary of the main findings in this dissertation. We also discuss limitations and avenues for further research.

Chapter 2:
Consumer credits: Some facts and figures

Abstract

This chapter presents summary statistics on consumer credits and consumer savings in the Netherlands and several other countries. The main impression is that the amount of consumer credits has increased in recent years. We also present some figures for various credit products, including credit card limits and overdraft amounts on current accounts. Special attention is given to mortgages. The relatively high level of mortgage debts in the Netherlands motivated the IMF to issue a warning regarding this point. We then present recent statistics on consumer savings as percentage of GDP, which likewise reflects an upward trend. Finally, we present figures on life insurances in the Netherlands. In addition, various figures are also placed in a European context. The main conclusion to be drawn from this chapter is that consumer debt has increased over the last decade, at a rate exceeding that of GDP.

2.1 Introduction

This dissertation is about financial literacy and consumer behavior concerning financial products. Before we will reveal individual behavior, we first present some statistics in this chapter which give an impression of the sheer size of consumer debts. We will see that debt has increased over the last decade, and perhaps with a trend that is too steep. That is, perhaps there are too many debts.

In this chapter we will present some facts about the various credit products, like credit card limits and overdraft on current accounts. Special attention is given to mortgages, as, even though a mortgage is a consumer credit product, there is a collateral feature to mortgages and separate savings are possible to pay off interest-only loans. We abstain from a discussion on tax facilities concerning each of the products. Next, we present some statistics on consumer savings, where we will see that these savings have also grown over the last decade. This may be due to the recent introduction of financial products concerning consumer savings with some specific fiscal features. Life insurances are also important in the Netherlands, which may be associated with the specific pension program. Dutch consumers also have many savings in specific life-insurances with a combined savings account, which, mainly due to fiscal reasons, also have grown over the years.

In Section 2.2 we start with consumer credits. In Section 2.3 we discuss some figures on mortgages. In Section 2.4 we focus on consumer savings, and we deal with life insurances. We conclude this chapter in Section 2.5 with a few graphs that allows us to put the situation in the Netherlands in a broader, mainly European, context.

2.2 Consumer credits

The data on household credits are obtained from Statistics Netherlands. The data usually span 1998 to 2010 and are available at an annual frequency.

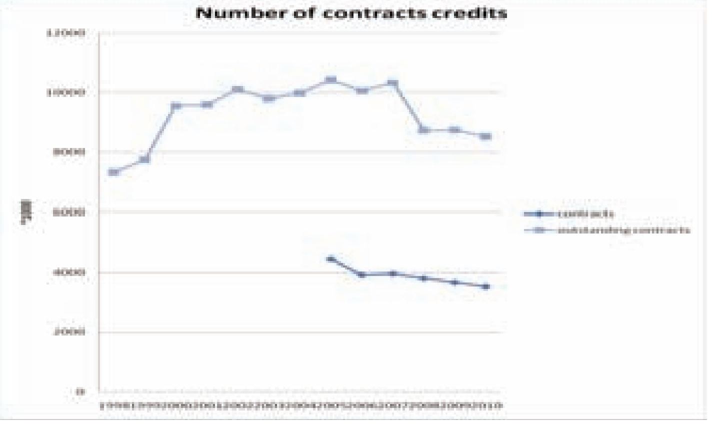

Figure 2.1: Contracts credits and outstanding contracts, *1000, per year, 1998-2010.

In Figure 2.1 we display the number of contracts credits. We notice an upward trend until 2008, the year of the outbreak of the financial crisis.

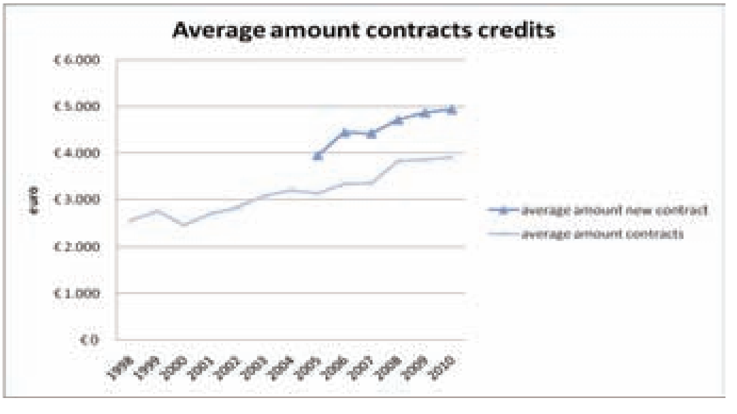

Figure 2.2: The average amount of euro involved in the contract credits. Figure 2.2 shows that the amount of euro involved in the consumer credits also has increased.

Figure 2.3 shows that during the first years of the 21th century the credit limits have grown rapidly. The amount of limits granted in 2010 is more than 41% higher than it was in 2000. In 2010 the total amount of household credits is more than 33.3 billion euro, while it was "only" 23.6 billion euro in 2000.

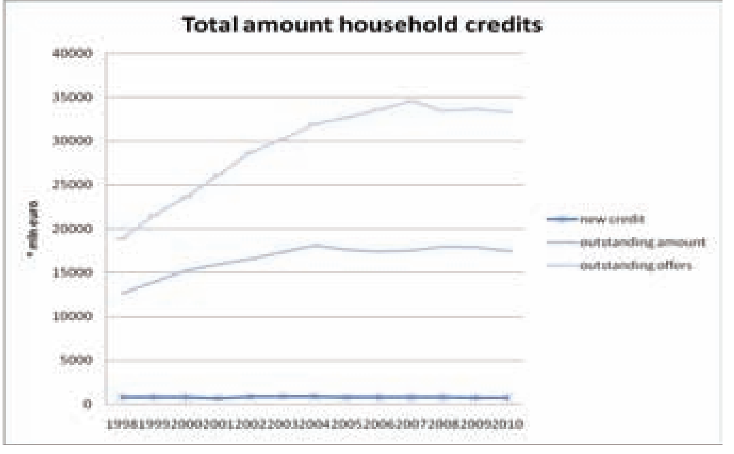

Figure 2.3: Household credits in the Netherlands, in millions of euro (current prices)

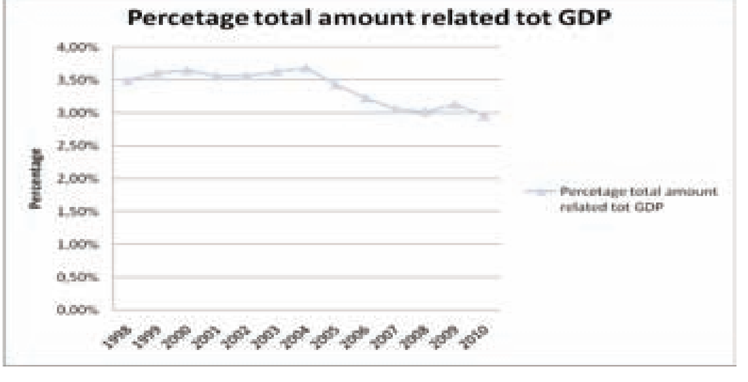

Figure 2.4: Total amount of credits relative to GDP

Figure 2.4 shows that, related to the level of GDP in the Netherlands, there is a downward change from 2005 onwards. Before that year the total amount of consumer credit was higher than 3.5% of GDP. After 2004 this has decreased. In 2010 the total amount of credits was less than 3% of GDP. In 2009 we notice a small increase, but this can also be due to the downturn in GDP.

When we turn to credit cards, we see quite a few interesting trends concerning fixed credits, revolving credits and credit card credits. The amounts of fixed credits and of credit card credits are growing faster than the amount of revolving credit, as can be seen from Figure 2.5.

Figure 2.6 shows that the growth of credit card loans is steep. The limits granted have grown with a factor 2.7 from 2000 to the end of 2010. In the year 2000 the amount of limits granted was more than 3.2 billion euro and in 2010 it has increased to 8.5 billion euro. Figure 2.7 shows that also the number of new contracts almost doubled from 2000 to 2010. That is, in 2000 453000 new contracts of credit card loans were issued, while in 2010 it has increased to 815000 new contracts. The amounts of credit card loans related to GDP in the Netherlands doubled from 0.12% of GDP in 2000 to 0.24% in 2010. In 2010 the average amount of credit card loans was just over 3000 euro.

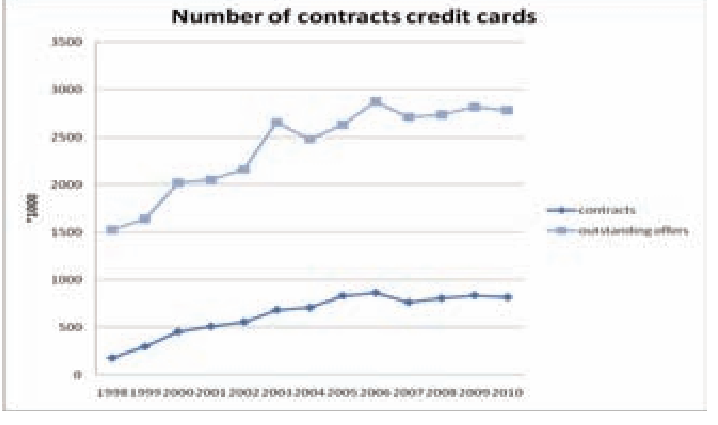

Figure 2.5: Total amount of credit card contracts and outstanding offers, * 1000

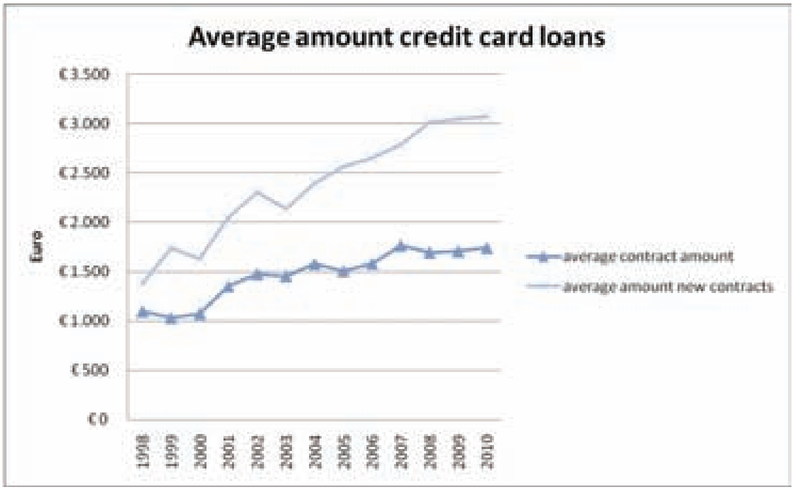

Figure 2.6: Average size (in euro) of loads due to credit cards.

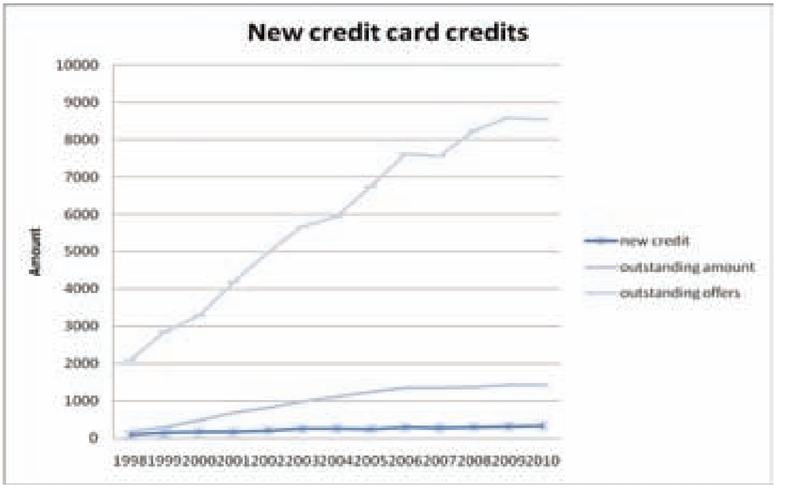

Figure 2.7: Amount of new credit card credits

When we discuss consumer credits, it is also noteworthy to study the size of overdraft on current accounts. This type of consumer credit has become more popular in recent years. Figure 2.8 shows that the number of contracts in 2010 has reached a level of more than 10 million, and that it almost doubled since 2000. Further, Figure

2.9 shows that the average amount of overdraft on a current acount has increased from 2158 euro in 2000 to 3538 euro in 2010.

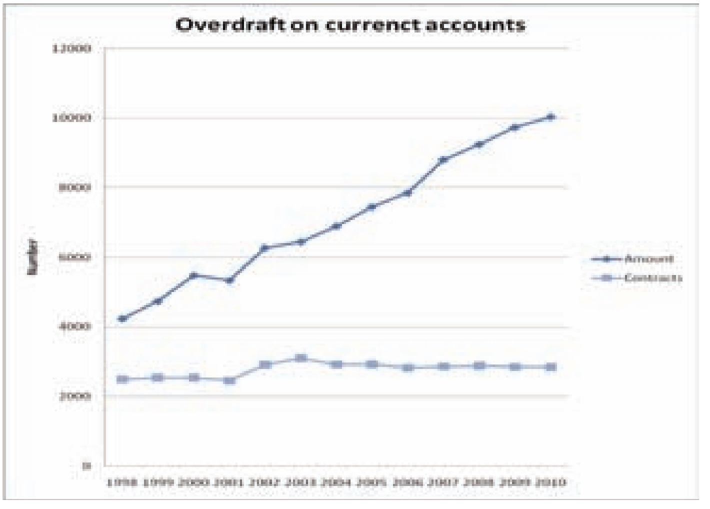

Figure 2.8: Amount of overdrafts on current accounts

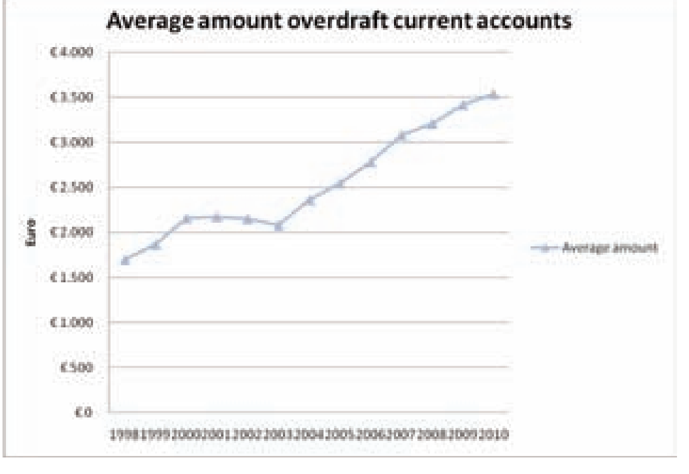

Figure 2.9: Average amount (in euro) in case of overdraft.

2.3 Mortgages

With a mortgage we define a loan that is issued to a homeowner, with specific payment arrangements. Usually, a mortgage is meant to finance the purchase of a house. In the payments arrangements the consumer gives the bank a guarantee for repayment. This guarantee is in most cases the house itself. There are several payment arrangements possible, and it seems characteristic for the Netherlands that there is such a wide variety of arrangements. Mortgages can be interest-only loans or loans with payment agreements. These payment agreements can concern payments by savings accounts or via a life insurance, or there can be payments by installments.

For the number and amount of mortgages in the Netherlands we use the statistics of De Nederlandsche Bank (DNB), where the sample starts in 1998. The data concern the number of registered mortgages, which involves the maximum amount of the mortgages. It contains no information on the savings necessary to pay off the mortgages. We will deal with those later on.

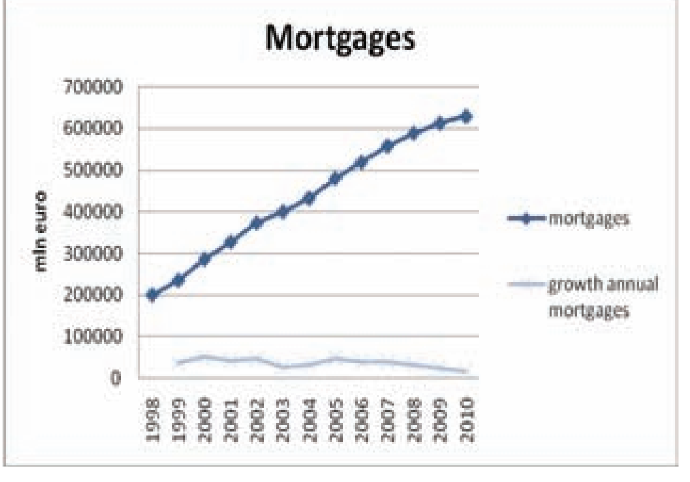

Figure 2.10: Outstanding amounts in mortgages

Figure 2.10 (bottom line) shows that in 2000 the Dutch households acquired new mortgages for an amount of 50.8 billion euro. The following years the amount of mortgages still increased, but not as fast as around 2000. In 2005 the increase was at a new peak with 47.5 billion euro new mortgages. After the financial crisis in 2008 the amount of new mortgages dropped very fast. In 2010 the number of mortgages grew with 16 billion euro, a third of the increase of 2005. The number of houses sold also decreased and therefore also the amount of new mortgages decreased. Nevertheless, the total amount of mortgages in the Netherlands is still almost 630 billion euro in 2010. That is 119% of the GDP in the Netherlands of 2010, which was 530 billion euro (current prices) in 2010.

Figure 2.11 allows for a comparison of these amounts of mortgages and of credits. Clearly, mortgages constitute the main part of the credits of Dutch households. Also, the growth of credits seems mainly due to the growth in mortgages.

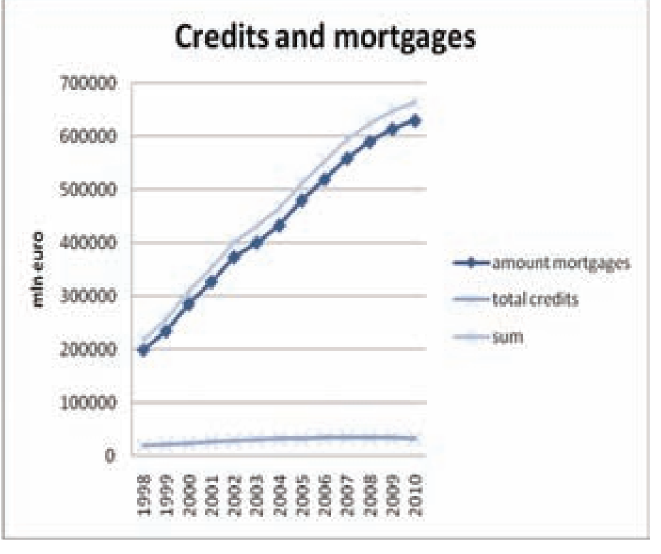

Figure 2.11: Mortgages relative to total credits

2.4 Consumer savings

The level of household savings in the Netherlands has grown in recent years, as evidenced by the data from Statistics Netherlands (CBS), presented in Figure 2.12. As at the end of 2010 Dutch households held more than 290 billion euro in saving accounts, representing 2.1 times the level of savings held by Dutch households in 2000. Each year during this period, the amound held in savings accounts grew by more than 15 billion euro on average.

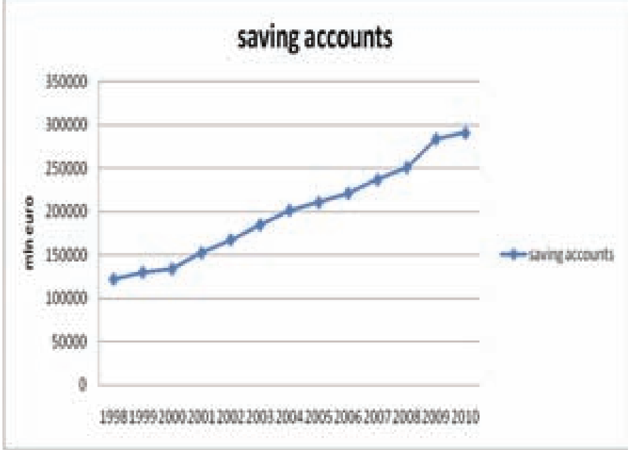

Figure 2.12: Total amount of euro in savings accounts.

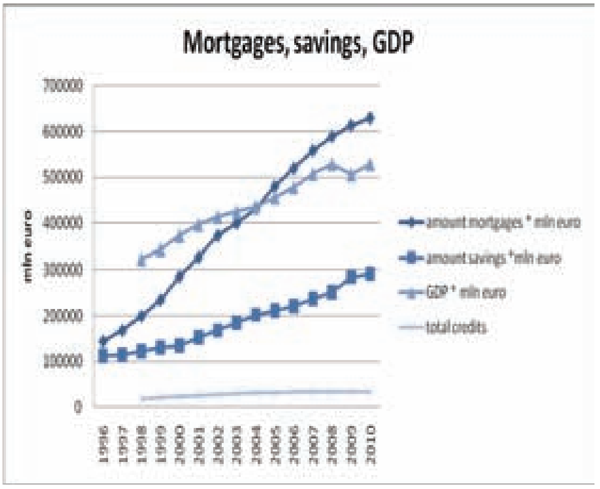

Figure 2.13: Mortgages relative to GDP

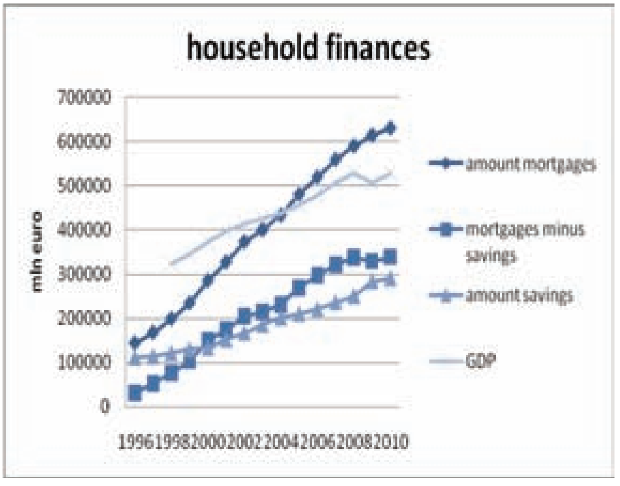

Figure 2.14: Mortgages versus savings

The sum of mortgages minus savings has grown the last years, see Figure 2.13. From the year 2000 onwards the amount of mortgages exceeds the number of savings. In 2009, for instance, the amount of household finances has decreased, due to the growth of savings, see also Figure 2.14.

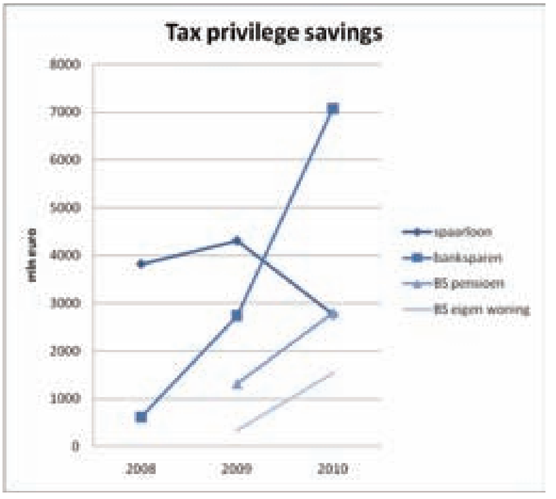

Figure 2.15: Tax privilege savings

In the Netherlands there are some financial products for savings accounts with tax privileges. One of these is called “banksparen / banksparen eigen woning” which is a blocked savings account, destined to pay off a mortgage after several years. At the end of 2010 these savings accounts for mortgages contained 1.5 billion euro. This same type of saving accounts is used to get some amounts of money to buy pension products called “banksparen (bs) pensioen”. More than 2.8 billion euro has been saved for pensions in this short period. Figure 2.15 gives this level of savings, and it is clear that these products have gained popularity. At the end of 2010 these saving accounts held 7 billion euro.

Another savings type is “spaarloon”, which is a tax facility to save money of gross income. It is limited to approximately 600 euro a year per person. These savings are blocked for four years, due to fiscal facilities. Only and uniquely in 2010 it became possible to withdraw money from these savings accounts in between. This withdrawal explains the decrease of the total amount of savings of “spaarloon” in 2010. At the end of 2010 2.7 billion euro was still held in blocked savings accounts for “spaarloon”.

In the Netherlands also life insurances are important. These are a type of saving accounts, which will pay when the insured person has died or will pay at a pre-arranged moment in time. Often the amounts are used to pay off mortgages or to buy pension products. For the number of life insurances we use the statistics of the Centre for Insurance Statistics (CVS). In 2008 the total capital sum insurance of life insurances, individual and collective, is 649.7 billion euro. The amount of new life insurances has grown over the last years. In 2005 the level of new capital sum was 46.9 million euro. After a minor decrease in 2007, in 2009 this amount has grown to 45.6 million euro. Figure 2.16 presents the total sum of capital insurance, individual and group insurance. Due to the financial crisis the amount in 2009 was a bit less than in 2008. In fact, in 2008 53.2 million euro new capital sum was issued. Figure 2.17 presents the amount of new insured capital of individual life insurances. The amount of unit-linked insurances has decreased, in favor of the amount of euro insurance.

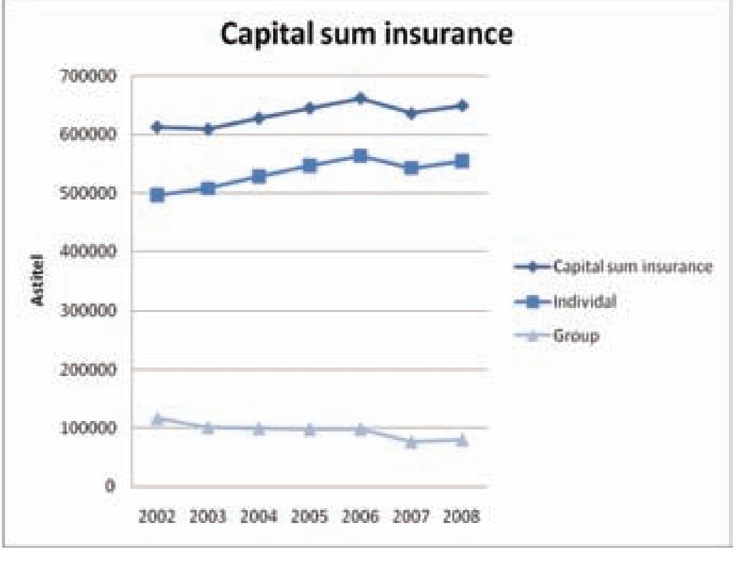

Figure 2.16: Capital sum insurance

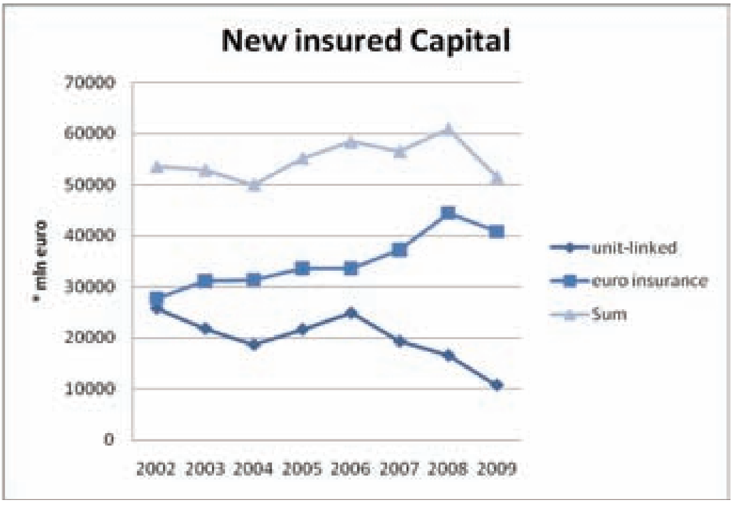

Figure 2.17: New insured capital life insurance

2.5 A comparison with other countries

In this final section of this chapter we compare the trends in the Netherlands with those in other (mainly European) countries. For this purpose we collected and analyzed various data from ECRI, the European Credit Research Institute, about Lending to Households in Europe (1995-2008). The difference of this data with those of Statistics Netherlands is that it contains credits and savings of individuals, as consumers and as entrepreneurs (sole proprietorships and partnerships). Therefore, credits contain household credits but also credits for for example education purposes. To allow for a proper comparison we only use the statistics of the countries who participated in the euro from the start of the euro in 2002. These countries are Austria (AT), Belgium (BE), Germany (DE), Greece (EL), Spain (ES), Finland (FI), France (FR), Ireland (IE), Italy (IT), Luxembourg (LU), Netherlands (NL), and Portugal (PT). For illustration, we also analyse the data of the United Kingdom (UK) and the United States (US), when relevant and insightful.

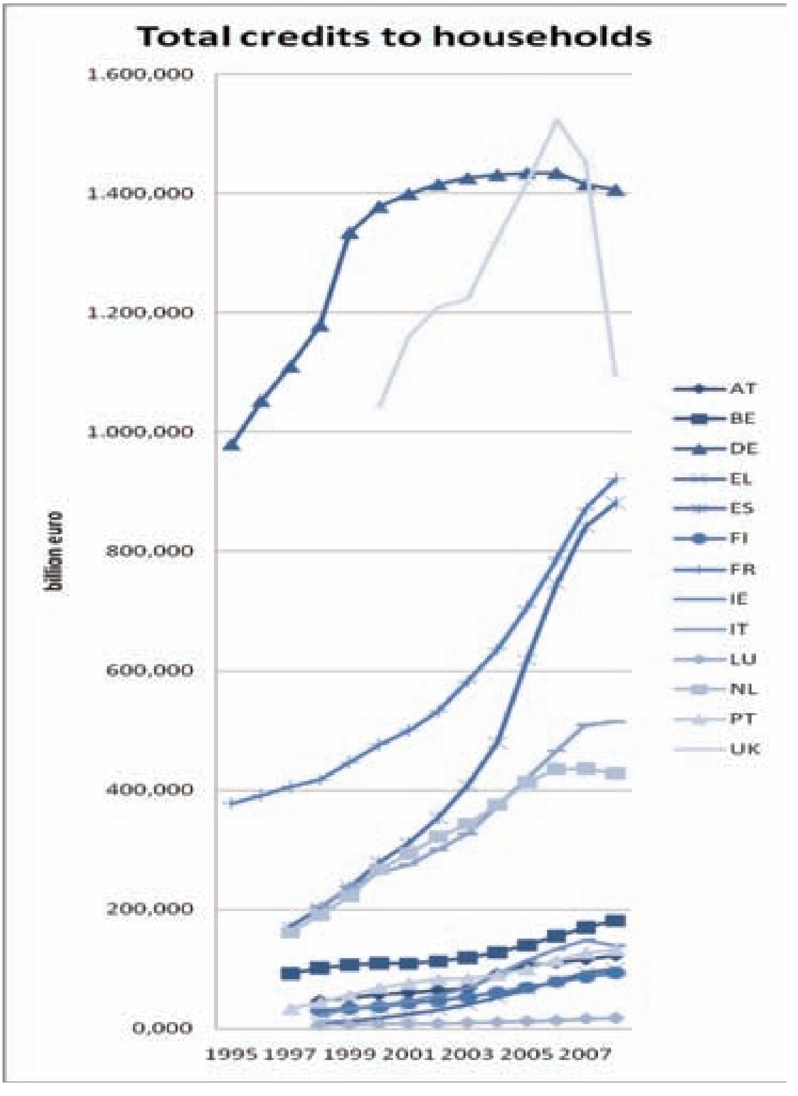

Figure 2.18: Total credits to households

Figure 2.18 presents the amounts of total credits, where we see that the Dutch number of total credits has increased until 2007. Maximum credit is associated with Luxembourg, followed by Ireland and the US. The Netherlands appears to attain rank 4, which puts the Netherlands at the top of the total amounts per capita, presented in Figure 2.19.

Related to the GDP of a specific country, in 2008 the amount of total credits is higher in the US, Portugal, Spain and Ierland, than in the Netherlands, shown in Figure 2.20. Note that the three European countries currently (2011) all face substantial financial problems. In a European context, the position of the Netherlands can be viewed as rather alarming. The large amount of mortgages as part of the total credits is the most important reason for this position, although we must stress that these figures are not adjusted for the number of savings associated with these mortgages.

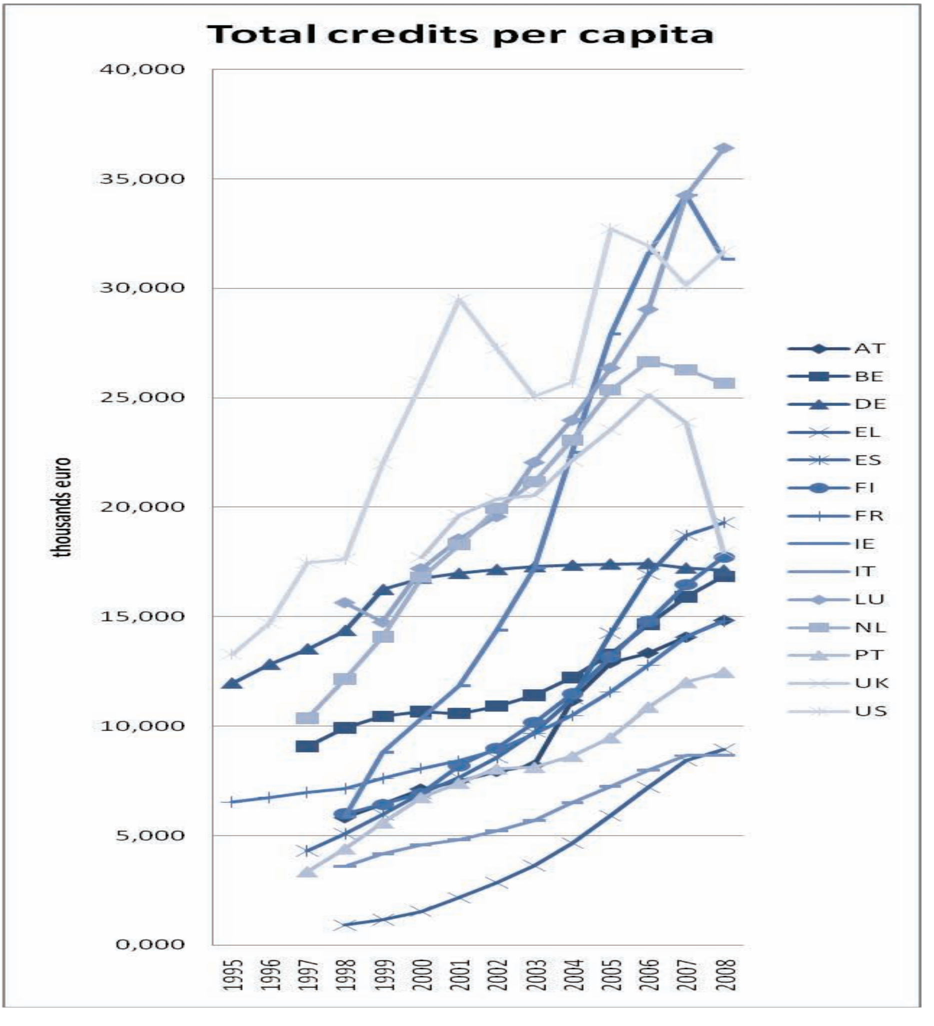

Figure 2.19: Total credits to households per capita

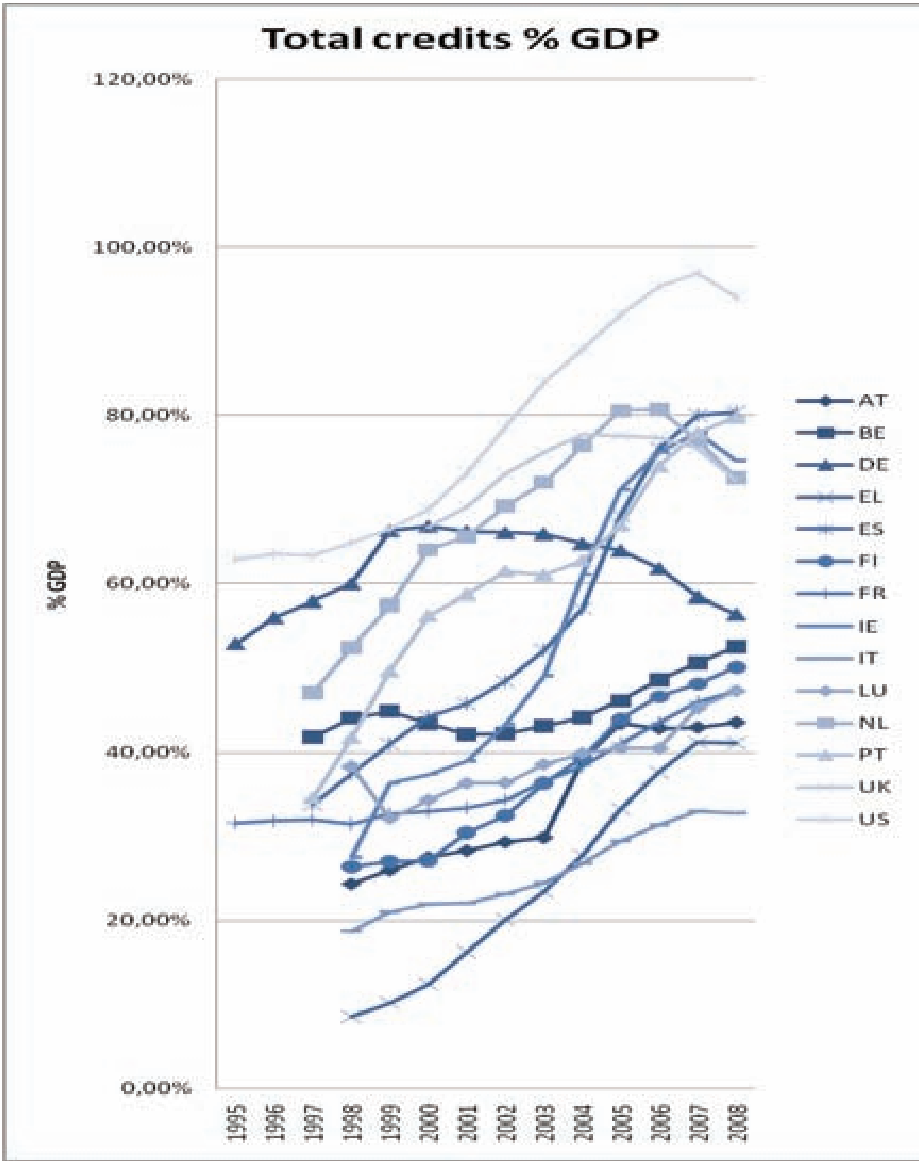

Figure 2.20: Total credits as a percentage of GDP

Figure 2.21 shows that consumer credit per capita is also on the rise for many countries. This also holds when it is presented as a percentage of GDP, presented in Figure 2.22. Countries like the UK, Germany and France have substantial consumer credits per capita or GDP, much more than the Netherlands.

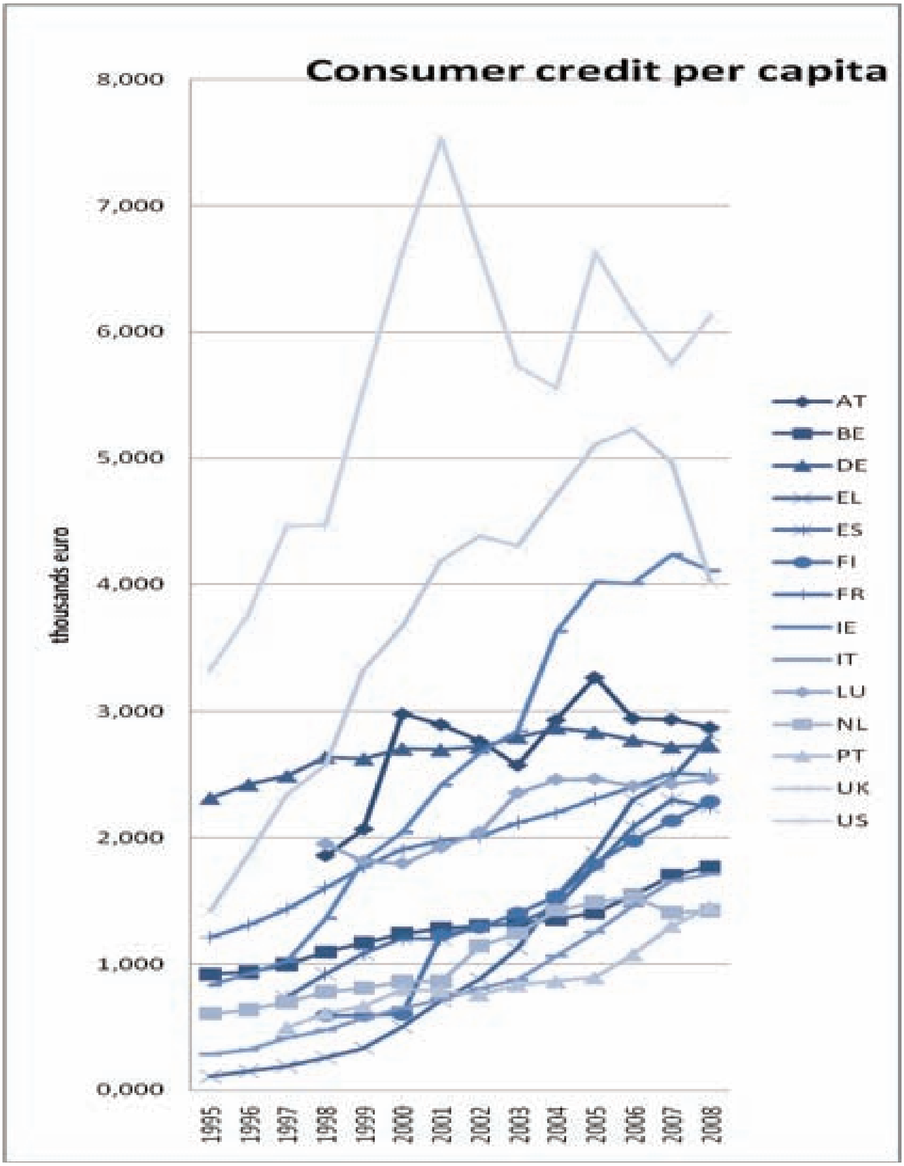

Figure 2.21: Consumer credit per capita

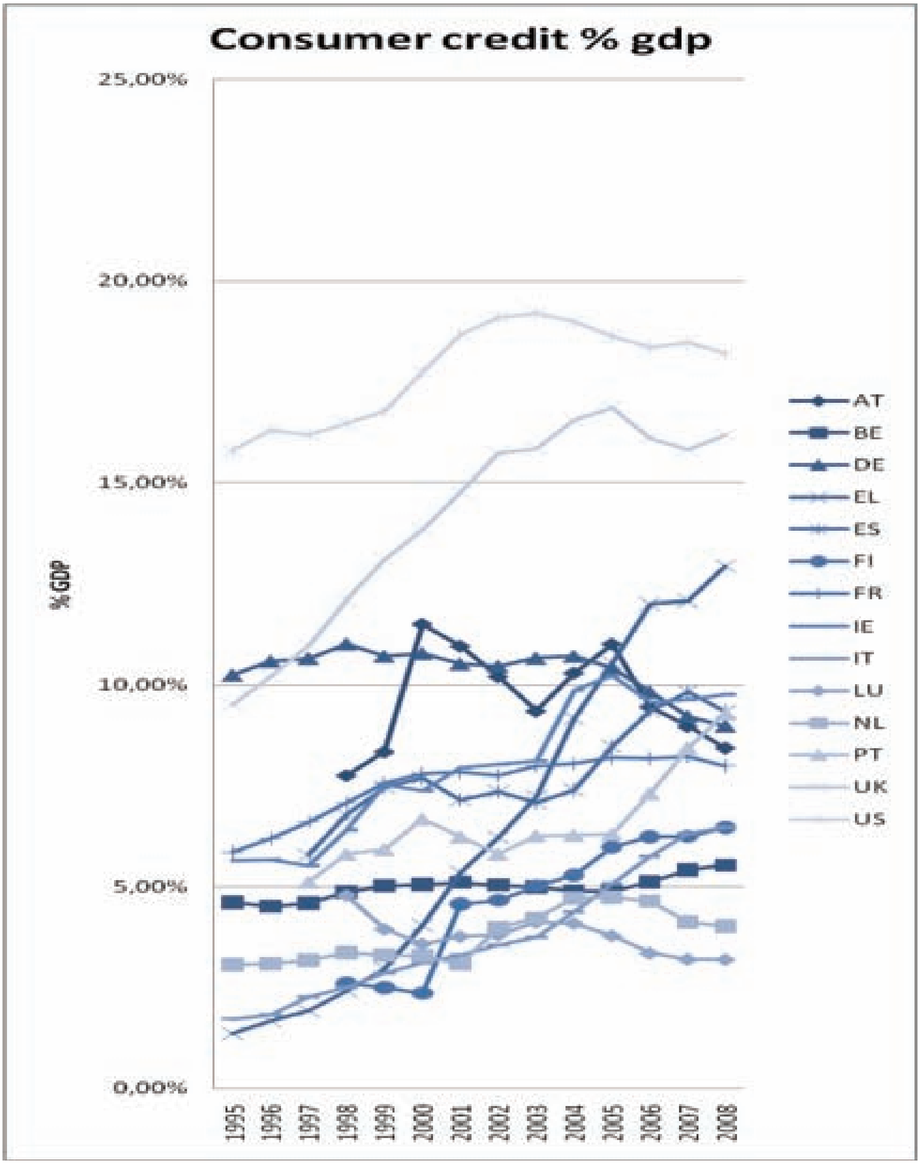

Figure 2.22: Consumer credit as a percentage of GDP

Finally, the development of housing loans (mortgages) over time has different features than consumer credits, as presented in Figures 2.23 and 2.24. The number of housing loans in Germany is the highest, although it is declining. Spain is the runner up, and there we see that the amount of housing loans, related to GDP, is increasing.

The Netherlands seems to be a specific case. Per capita the rate of housing loans is high, and only outnumbered by Luxembourg, Ireland and the US. But as a percentage of GDP it is relatively low, in contrast with Germany and Greece.

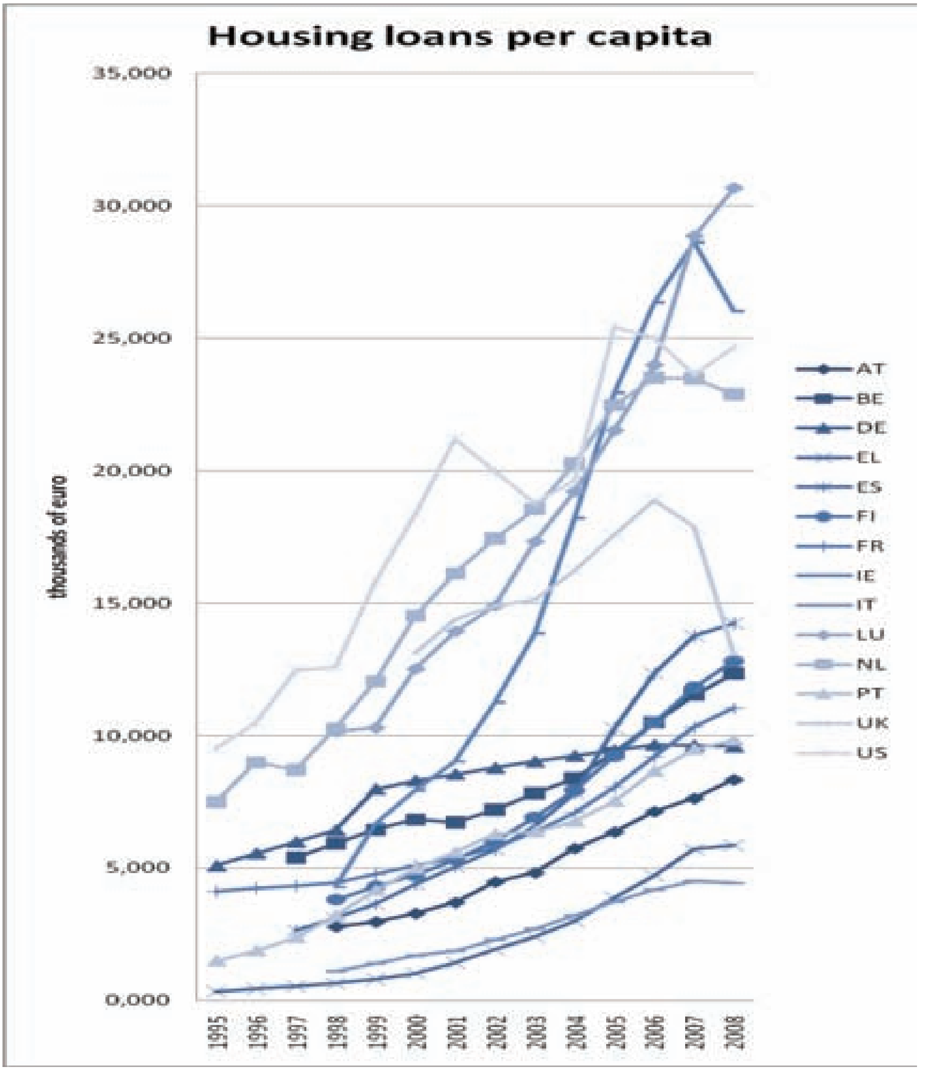

Figure 2.23: Housing loans per capita

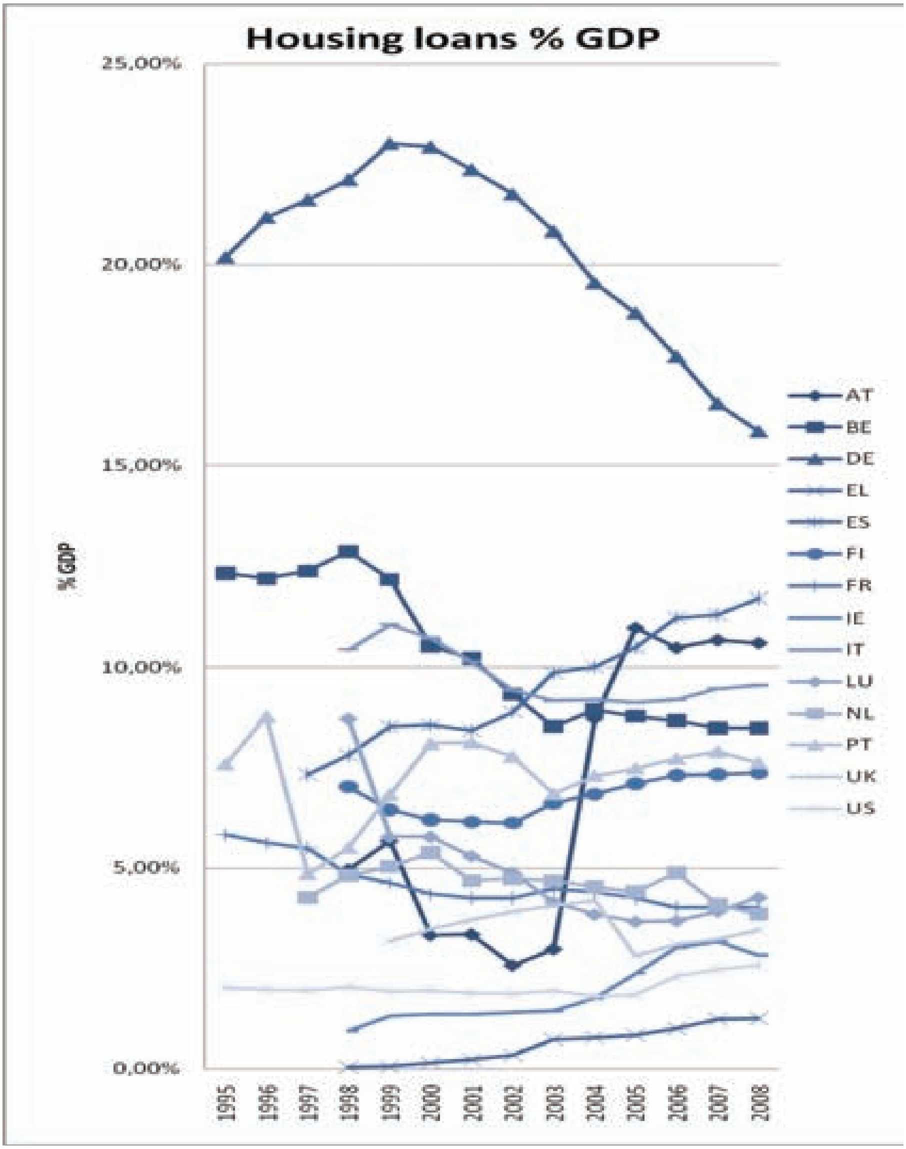

Figure 2.24: Housing loans as a percentage of GDP

2.6 Conclusion

This chapter has illustrated that consumer credits in the Netherlands are substantial. Relative to other countries, some types of consumer credits are exceptionally high, although countries like Spain, Ireland and Portugal seem to rank highest in various dimensions. We also saw that trends in consumer credits are almost without exception positive, meaning that there still is an increase in money that goes around in financial products of individual households. At present, in 2011, we know that the financial situation in Spain, Ireland and Portugal is far from good, and if trends continue, such situations may also prevail in countries like Germany, the Netherlands and the UK.

The numbers in this chapter lead us to conclude that perhaps there are too many consumer credits around. Of course, for mortgages there are physical entities like houses, but for overdraft on current accounts there may not be such counterparts.
A key topic in this dissertation concerns the issue that consumer credits have gone up so fast. The increase of the amount of consumer credits can be the result of several conditions. One of the premises taken here is that perhaps these positive trends are due to the fact that consumers find it hard to exactly understand the key aspects of financial products. In fact, as we will address in the next two chapters, it may well be that consumers lack basic skills for such an understanding. And, if so, then the relation between a consumer and a financial advisor becomes extremely important. Chapters 5, 6 and 7 will deal with these relations, where aspects as trust, quality and comprehension are important.

Chapter 3: Financial innumeracy: Consumers cannot deal with interest rates[1]

Abstract

Consumers often have to base decisions on calculations involving interest rates. The literature clearly shows the difficult time people have with calculations involving percentages (like interest rates). We survey a large group of consumers, and ascertain that questions involving interest rates are answered correctly about 20% of the time, which in our setting amounts to random guessing. In addition to the available literature, we also demonstrate that consumers are overly optimistic in belief loans will be paid off sooner than is actually the case, offering empirical evidence of a self-serving bias. We further determine that this optimism can be reduced by increasing the amount of euro of the monthly payments. The results are robust to corrections for general numeracy.

[1]This chapter is a revised version of: Franses, Philip Hans, and Anita Vlam (2011), Financial innumeracy : Consumers cannot deal with interest rates, Econometric Institute Report 2011-01, Erasmus University Rotterdam.

3.1 Introduction

Today it is very common to purchase products now and to pay later. This can be done by using credit cards, for example, or via loans. These loans can be taken from a bank, but today also many companies offer financial products. For example, car dealers have their own financial offers when a consumer purchases a car. When agreeing upon a loan, a consumer has to decide on the amount to be borrowed, and the consumer has to consider the interest rate, monthly payback amount and therefore the time it will take to pay off the debt. An important figure in the computations that a consumer needs to do are calculations involving interest rates. Usually, an interest rate is quoted as a percentage, and when it comes to loans to be paid off in the future, the consumer needs to perform calculations concerning its impact on future amounts of money. In this paper we address this consumer task in more detail.

At present it is also well acknowledged that many households face problems while keeping their personal finances, or make mistakes in household investments (Campbell, 2006). At the heart of the 2008 credit crisis was the large fraction of households, particularly in the United States, with substantial debts due to personal mismanagement of for example credit cards. Individual homes had to be sold as households could not pay the mortgage anymore.

It is of substantial interest to study the potential causes for the financial problems of so many households. Recent studies in for example Hilgert et al (2003), Lusardi and Mitchell (2008), Lusardi and Tufano (2009) go in-depth as regards the potential causes of over-indebtedness and financial literacy. Indeed, it may well be that consumers do not have financial literacy and are simply not able to perform the computations that are necessary to manage personal finances. A recurrent example is that many individuals fail to understand that stock markets can go up but also can go down, which is associated with the processing of gains and losses, see for example Chatterjee et al. (2000).

In the present chapter we focus on the computations that individuals have to make and in particular on the computations that involve interest rates. Interest rates are percentages, and it is well known that consumers find it difficult to perform computations with interest rates, see for example Paulos (1988) and recently Chen and Rao (2007). What is unknown, however, is to what extent consumers make mistakes and also whether there is any bias in these mistakes. That is, do consumers make computations such that the results are in their (believed) favor, instead of correct?

To this end, we carry out a simple survey amongst a large group of bachelor students, taking courses on Methods and Techniques in their second bachelor year. Additional to a range of questions concerning interest rates, we also have questions concerning innumeracy in order to single out whether mistakes on interest rates are perhaps due to general problems with calculations.

Our main findings are quite striking. First we find that the probability of choosing the right answer from K answer categories is about 1/K. This holds for the total sample and for the sample where we focus on those students (about 60%) with all other more general questions on calculations correct. A second finding is in correspondence with the literature on self-serving bias and it is that consumers have a tendency to underestimate the consequences of interest rates. More precise, they believe that debts are paid off earlier than is true. We put forward that this self-serving bias could be one of the factors that causes people to have problems with debts. The third finding is that higher monthly payment amounts reduce this bias, and we propose that this can be translated into a simple recommendation.

Our paper is structured as follows. In Section 3.2 we review the relevant literature (without claiming to be exhaustive) and we put forward a few hypotheses. In Section 3.3 we discuss the survey and in Section 3.4 we present the results. Section 3.5 concludes this chapter with a few recommendations.

3.2 Literature

There are three areas of literature of interest to our study. The first deals with personal financial management. One observation, which holds true in many countries all over the world, is that many households have a difficult time managing personal finance. There are countless examples of individuals falling prey to pyramid schemes and losing substantial sums of money. In addition, there are the countless individuals who have lost large sums of money on the stock markets due often simply to a lack of knowledge and an overly strong belief they will always benefit from a bullish market. Some financial product brochures of financial products never mention the possibility that the stock markets can also go down – quite precipitously sometimes. This is also an issue about which consumers apparently ask very few questions. Some households take out mortgages for an amount they are ultimately unable to pay several years down the road. There is, of course, the issue of supply-side responsibility (for example pyramid schemes are illegal). However, it is now also generally acknowledged that consumers also share in this responsibility.

The interesting aspect of this latter presumption is to what extent households are anyhow able to perform financial management in a proper way. Recent studies of Hilgert et al. (2003), Lusardi and Mitchell (2008) and Lusardi and Tufano (2009) among others seek to shed light on to what extent consumers are actually able to perform proper management of personal management. Exemplary findings are that individuals face difficulties with financial planning when it concerns further-away horizons (van Rooij ea, 2007) and that individuals can behave quite different from what they actually planned. For example, Lusardi and Tufano (2009) demonstrate that debt literacy is low.

One important issue that is touched upon in these studies concerns numerical skills. Indeed, a basic premise of the ability to perform proper financial management is that consumers can perform basic computational tasks. One of these tasks is concerned involving percentages, and hence a second relevant literature concerns dealing with percentages and interest rates. Examples are Chatterjee et al. (2000) and Chen and Rao (2007). Subjects in these studies were found to face difficulties in computing with percentages and in particular mistakes were made concerning the asymmetry that is involved. That is, the difference between N% gain and N% loss is often misunderstood. Lusardi and Tufano (2009) also document that "only one-third of their population does seem to understand interest compounding".

The third area of literature deals with a self-serving bias, that is, a tendency for people to evaluate ambiguous information in a way, that is beneficial to their interests. We propose that one potential cause for households to end up in financial problems is that if they make mistakes with interest these are also made in the wrong way. That is, costs of loans are estimated as lower that they really are. Tversky and Kahneman (1974) summarized a range of heuristics and biases that individuals can have, and some of these are translated to the issue of handling price changes in Heath et al. (1995). Also consumers are more overconfident about their knowledge and expertise (Alba and Hutchinson, 1987, 2000).

Taking a few key results in these three literatures together, we postulate

Hypothesis 3.1: *Consumers face difficulties with calculations using interest rates*
This hypothesis follows from many studies, and our findings will most likely support earlier results, although to which extent is yet to be investigated.

The second hypothesis follows from the literature on cognitive bias, and reads as

Hypothesis 3.2: *Consumers have a tendency for self-serving bias when it comes to paying back loans*
If we find support for this hypothesis, then we could have an indication of one of the sources of debt literacy. In our analysis we will also seek for moderators of this bias, if there is any.

Finally, based on Paulos (1988) and the like, we do not have any strong thoughts about whether general numerical skills are beneficial to skills concerning interest rates. We do postulate however

Hypothesis 3.3: *Findings are dependent on general numerical skills*
In the next section we discuss the survey that we use to examine these three hypotheses.

3.3 Design of survey

Our questionnaire basically has one single question, which we repeat seven times. It deals with an amount Y that one borrows with an interest rate of x% per month. Also known is that monthly payment M to pay back the loan, and the very basic question concerns the number of months that it takes to pay back the full Y. Additional to these questions, we ask a few general numeracy questions and a few demographics. The general idea of the first seven questions appears in Appendix 3A.

The survey was set out at the start of the class on Methods and Techniques for second-year bachelor students at the Erasmus School of Economics. These students all should have general computational skills. Also, students are used to borrowing money to pay for tuition, accommodation and general expenses. Even, most students additionally borrow money to afford driving a car or to have mobile phones and many other electronic gadgets. In sum, we can see these students as regular consumers who also make decisions concerning interest rates.

The survey was supervised by the author of this dissertation, and it was stressed that students could not use a calculator. The whole survey took less than 15 minutes and after that, we had collected 433 questionnaires, which were almost all complete. We display the survey in Appendix 3B. The amounts Y are either 10000 or 20000 euro. The interest rates are either 0.6% per month or 0.8% per month. And, the monthly payment M is either 200 or 250 euro. Prior testing of the survey revealed that these numbers match with numbers that these consumers (in this age category) can encounter.

The general numeracy questions are taken from a range of questions that were all tested at other occasions to measure numeracy. Of course, these questions should be such that people can answer them quickly, and also such that at least a sizeable fraction of the respondents has all answers correct. Prior testing on another set of students revealed that the four questions N1 to N4 in Appendix 3B would work well.

In Appendix 3C we give the correct answers to the seven questions on interest rates and on the four general questions. The method in Appendix 3A is used (as it is available in Excel using PMT) to compute the correct answers. In Appendix 3D we re-iterate the survey settings so that we can use these later on to see if they have a moderating role in the empirical results.

3.4 Results

Our focus is on examining the relevance of hypotheses 3.1 to 3.3, and hence we summarize the empirical results such that conclusions can be drawn easily.

Table 3.1 indicates that, on average (and also if we take the median), in only about 20% of the times the correct answer is given. If we were to excluding the two extreme categories (a) and (g), which were rarely selected, then this 20% matches with the level of a random guess. This low level of correct answers seems to provide strong support for Hypothesis 1, and is also in accordance with the findings in the literature.

Table 3.1: Frequency of answers to questions Q1 to Q7

Question	Sample size	Too low	Correct	Too high
Q1	432	0.382	0.256	0.362
Q2	431	0.244	0.197	0.559
Q3	429	0.548	0.148	0.268
Q4	428	0.484	0.178	0.339
Q5	428	0.266	0.231	0.509
Q6	429	0.795	0.205	0.000
Q7	428	0.381	0.154	0.465
Mean		0.443	0.201	0.357
Median		0.382	0.197	0.362

Table 3.1 further indicates that the average fraction of "too low" answers, meaning that the number of months is estimated smaller than the actual number of months, is larger than the average fraction of "too high" answers. This finding is robust to using the median instead of the mean, although now the difference becomes smaller. The median is used to meet the possible effects of Question 6 for which the correct answer is (g).

In sum, Table 3.1 suggests support for hypothesis 3.1 and for hypothesis 3.2.

Table 3.2: Regression results of fractions in Table 1 on the variables in Appendix 3D p-values on parentheses, based on HAC estimates of variance)

	Dependent variable is fraction		
Variable	Correct	Too low	Too high
Intercept	0.232 (0.005)	0.517 (0.028)	0.252 (0.200)
Amount	-0.025 (0.357)	0.059 (0.615)	-0.032 (0.812)
Rate	-0.039 (0.249)	0.080 (0.531)	-0.043 (0.774)
Payback amount	0.010 (0.741)	***-0.268 (0.061)***	0.259 (0.106)
P-value of F-test	0.464	0.212	0.354

In Table 3.2 we report on the regression results where we relate the fractions in Table 3.1 with the experimental settings in Appendix 3D. From the second column we learn that the fraction of correct answers is independent from the amount *Y*, quoted interest rate *x*% and monthly payments *M*. The same holds for the fractions "too high". Interestingly, the fraction "too low" does depend on the payment amount M. When the value M gets larger, then the fraction of "too low" gets smaller.

This finding is interesting as it can suggest at least one simple instrument to reduce the size of self-serving bias. When people get offered higher monthly payments, they may perhaps be less likely to underestimate their debts.

Table 3.3: Frequency of answers to questions Q1 to Q7, computed for those respondents who gave the correct answers to all N1 to N4 questions

Question	Sample size	Too low	Correct	Too high
Q1	260	0.338	0.274	0.338
Q2	260	0.212	0.177	0.612
Q3	259	0.510	0.189	0.305
Q4	259	0.432	0.193	0.375
Q5	259	0.247	0.243	0.510
Q6	259	0.768	0.232	0.000
Q7	259	0.367	0.174	0.459
Mean		0.411	0.212	0.378
Median		0.367	0.193	0.388

Table 3.3 presents the same fractions as in Table 3.1, but now only for respondents who got gave all correct answers to questions N1 to N4. It appears that there are not many differences across the fractions in Table 3.1 and Table 3.3, and hence we are tempted not to support Hypothesis 3.3. We also ran the same regressions as in Table 3.2 for this subset of the sample, and we find qualitatively the same results.

In sum, also for the numerically gifted, we document that they underestimate the number of months it takes to pay back the full amount (although slightly less so than the full sample). And, again, higher monthly payments reduce the degree of underestimation.

Table 3.4: Some summary statistics

Correct answers to questions N1 to N4		
N1	0.942	
N2	0.737	
N3	0.907	
N4	0.812	
To all questions	0.596	
Demographics		*Correct answers, all four*
Men	0.613	0.630
Women	0.387	0.370
Age		
<19	0.026	0.023
19	0.313	0.335
20-21	0.339	0.323
22-23	0.202	0.202
> 23	0.120	0.117

Table 3.4 provides a few summary statistics on the other questions in the survey. We see that about 60% of the students had all correct answers to N1 to N4. Not reported is that the fraction of students with all questions wrong is 0%. In terms of gender and age, we see no differences in numerical skills, and this further supports the aggregate analysis in Tables 3.1 to 3.3. Finally, there was no consumer with all seven questions on interest rates correct. And, there are 58 consumers who gave always “too low” answers and 55 of the consumers gave always a “too high” answer. These results also motivate looking at the full sample, as is done in Table 3.1 to 3.3.

3.5 Conclusion

This survey is about the numerical skills of second year bachelor students. These students are also consumers of financial products, for example by borrowing money for tuition fees. Hence, the results of this survey may hold for consumers in general..

The main conclusions that can be drawn from the survey results are that consumers have a difficult time dealing with interest rates. Not only are they generally unable to correctly estimate the number of months it takes to settle a loan, they also systematically underestimate this number of months of payments. This can be seen as a fundamental reason why households run into financial problems. After all, they believe the loan will be paid off earlier than is really the case; and may consequently opt to accept new loan offers prematurely. This pattern will inevitably lead to financial problems. We also found that these results hold true irrespective of the strength of the consumer's numerical skills.

A final important finding is that the monthly payment serves as a moderator. When this amount increases, then the size of self-serving bias decreases. To us this seems to suggest a simple instrument to reduce potential future financial problems. When loans come with higher monthly payments, consumers will make less biased mistakes. Indeed, if consumers believe it will take longer to pay off, then this is beneficial for personal financial management.

Appendix 3A: Calculation

Computing the number of months within which a loan of size Y is paid off, given a monthly interest rate of x% and a monthly payment of M euro.

	Amount left
Month 1:	$(1+x)Y$
Month 2:	$(1+x)Y-M$
Month 3:	$(1+x)[(1+x)Y-M]-M$
Month K:	$(1+x)^K Y-\sum_{i=0}^{K-1}(1+x)^i M$

Appendix 3B: The questionnaire

Example question: If you borrow 10000 euro at a MONTHLY interest rate of 0.6%, and pay back 250 euro per month, how many months (that is, the number of payments) do you approximately need to pay back the total loan with interest?

Panel 1: Seven questions about interest rates

Q1: The loan amount is 10000 euro, the monthly interest rate is 0.6% and the payback per month is 250 euro. The number of payments is

(a) < 40
(b) 40-45
(c) 45-50
(d) 50-55
(e) 55-60
(f) 60-65
(g) > 65

Q2: The loan amount is 10000 euro, the monthly interest rate is 0.8% and the payback per month is 250 euro. The number of payments is

(a) < 40
(b) 40-45
(c) 45-50
(d) 50-55
(e) 55-60
(f) 60-65
(g) > 65

Q3: The loan amount is 10000 euro, the monthly interest rate is 0.8% and the payback per month is 200 euro. The number of payments is

(a) <40

(b) 40-45

(c) 45-50

(d) 50-55

(e) 55-60

(f) 60-65

(g) > 65

Q4: The loan amount is 20000 euro, the monthly interest rate is 0.6% and the payback per month is 200 euro. The number of payments is

(a) < 100

(b) 100-120

(c) 120-140

(d) 140-160

(e) 160-180

(f) 180-200

(g) > 200

Q5: The loan amount is 20000 euro, the monthly interest rate is 0.6% and the payback per month is 250 euro. The number of payments is

(a) < 100

(b) 100-120

(c) 120-140

(d) 140-160

(e) 160-180

(f) 180-200

(g) > 200

Q6: The loan amount is 20000 euro, the monthly interest rate is 0.8% and the payback per month is 200 euro. The number of payments is

(a) < 100

(b) 100-120
(c) 120-140
(d) 140-160
(e) 160-180
(f) 180-200
(g) > 200

Q7: The loan amount is 20000 euro, the monthly interest rate is 0.6% and the payback per month is 200 euro. The number of payments is

(a) < 100
(b) 100-120
(c) 120-140
(d) 140-160
(e) 160-180
(f) 180-200
(g) > 200

Panel 2: Questions about general numeracy

N1 One chair costs 75 euro. When you buy 4 chairs, you get a 5% overall discount. How much do you need to pay when you buy 8 chairs?

- ☐ Less than 600 euro
- ☐ 600 euro
- ☐ More than 600 euro
- ☐ I do not know

N2 You buy 5 chairs for each 100 euro, Again, you receive 5% discount. However, you have to pay 19% tax over the total amount. How much do you need to pay, approximately?

- ☐ 425 euro
- ☐ 595 euro

☐ 565 euro

☐ I do not know

N3 There is a promotion in the supermarket for detergents. Each second package is half the price. How much do you need to pay if you buy 4 packages and each of them costs 5 euro?

☐ 7,50 euro

☐ 12,50 euro

☐ 15 euro

☐ 20 euro

☐ I do not know

N4 The weather forecast says that the average temperature for the next 3 days is 30 degrees Celsius. Tomorrow and the day after are predicted at 28 and 29 degrees. What will be the forecasts for the third day?

☐ 30 degrees

☐ 31 degrees

☐ 32 degrees

☐ 33 degrees

☐ 34 degrees

☐ I do not know

Panel 3: Demographics

G1 Gender

☐ woman

☐ man

G2 Age

☐ < 19

☐ 19

☐ 20-21

☐ 22-23

☐ > 23

Appendix 3C: The correct answers to the questions in Appendix B

Question

Q1	c (46)	N1	a
Q2	c (48)	N2	c
Q3	f (64)	N3	c
Q4	d (153	N4	d
Q5	b (109)		
Q6	g (202)		
Q7	c (128)		

Appendix 3D: The experimental setting

Question	Amount	Rate	Payback amount
Q1	0	0	1
Q2	0	1	1
Q3	0	1	0
Q4	1	0	0
Q5	1	0	1
Q6	1	1	0
Q7	1	1	1

Chapter 4:
"Borrowing money costs money": Yes, but why not tell how much?[2]

Abstract

Consumers have substantial debts. They have mortgages but also debts for loans for boats or catalogue homes. One of the reasons of facing difficulties is dealing with percentage computations. Campaigns like "Borrowing money costs money" should make consumers aware of the consequences of borrowing. We argue that the campaign would be more effective if the actual size of the debt is mentioned in monetary terms. We support our argument using new collected experimental data.

[2] This chapter is a revised version of: Franses, Philip Hans and Anita Vlam (2011), "Borrowing Money costs Money": Yes, but why not tell how much?, Econometric Institute Report 2011-02, Erasmus University Rotterdam.

4.1 Introduction and motivation

Consumers in industrialized countries often have credit debts. There is a large literature on the potential sources of those debts, see for example Lusardi and Mitchell (2008) and the literature cited therein. One aspect that has gained attention recently concerns the concept of financial literacy, of which a sub-aspect concerns the ability of consumers to perform basic and relevant computations.

Indeed, one of the potential sources of over-indebtedness is the notion that consumers face difficulties performing the actual calculations when they decide to purchase on credit. Also there is great confusion about the impact of interest among young adults with no experience in debts (Lewis and Van Venrooij, 1995). For example, consumers may find it hard to compute what the exact final amount is when they have to pay off a loan of 10000 euro with a 0.6% interest rate per month over 72 months. In Chapter 3 it was demonstrated that consumers not only lack the skills to perform these tasks, they also show a tendency to underestimate the eventual debt size. Similarly, subjects in the experiments were found to believe that debts are paid off earlier than that they really are.

To warn consumers of consequences of borrowing and against too high a debt, in the Netherlands (and similarly elsewhere) campaigns have been initiated to increase awareness. The punch line in the Dutch situation is "Borrowing money costs money"[3]. Despite its apparent success in creating such awareness, we believe that this campaign could be made even more effective if the money lender would be forced to precisely say how large exactly these borrowing costs are. Exact information about the total amount paid instead of information in terms and small print make people more aware of total costs of the loan. Hence, one would then read for example that a television set costs 338 euro, but if a consumer decides to borrow the money and pay back in monthly terms, the costs increase to 384 euro.

In the present paper we put this conjecture to a simple empirical test. We run two rounds of experiments, with the first where consumers face payment options that also involve buying on credit and where the second round only concerns monetary

[3] http://www.afm.nl/en/professionals/afm-actueel/nieuws/2009/dec/kredietwaarschuwingszin-succes.aspx

amounts. Our experiments show a clear support for the conjecture, and hence we conclude that we recommend money lenders to precisely quote the debt size in euro.

4.2 Research design

The research design is based on the familiar and rather basic version of a conjoint experiment. We ask individuals to choose between two choice options. Each choice option involves values for attributes and also for the method of payment. We have two runs of our experiments. First, we issue the survey where the payment options involve cash payments as well as payments in monthly terms (with interest). We do not create additional difficulties by forcing people to calculate with percentages, so we simply let people evaluate, say, a cash price of 338 euro against 59 monthly payments of 8 euro. In the second run of our experiments we simply translate the first-round credit payments into the actual monetary value, that is, following the same example, it then becomes 338 euro versus 472 euro (472 = 59 times 8).

An example of the survey is given in the Appendix, where we give the questions for hypothetical LCD television sets. We spent substantial time to make sure that the hypothetical products looked realistic. This also involves the payment amounts. Indeed, large screen sizes and more Hertz should also come with higher prices. So, whereas Brand, Screen Size and Hertz only have two levels per attribute, the payment seems to have many more. A closer look reveals that for the prices there are effectively three levels, the first is cash, the second is 24 months with some amount per month and the third is the maximum number of months with a somewhat smaller amount per month. We tested the survey on a few sample individuals and we consulted internet retail stores selling those television sets to confirm that these hypothetical products actually make sense.

A similar research design was implemented for couches. We chose this second product as we were about to hold the survey amongst undergraduate students at the Erasmus School of Economics. Some prior experimentation learned that these two products were actually considered by students, where also the three different levels of payment methods were considered as realistic. Additional to the indicated choices, we also asked to reveal their gender, age and income level.

On the first day of data collection, November 8 2010, we surveyed 375 students, which thus results in 4500 (is 375 times 12) answers of which 2250 are 1 for "preferred" and 0 for "not preferred". On the second day, November 25 2010, we surveyed 285 students giving 1710 values of 1 and 1710 of 0. The students were following different bachelor courses, so there is no overlap between the individuals in the two samples.

The data are analyzed by the familiar binary logit model, where the explanatory variables take values of 1 or 0, where 1 denotes the occurrence of that particular level. Because the payments can take three levels, each time we consider two logit models, each with a pair of potential levels of payment.

What would we expect a priori from the experiments? First, we would see that cash payments would be preferred over credit payments. So, we would expect that consumers would prefer to pay 338 euro over payments in 24 months (which is 384 euro). Second, we would expect that when the actual monetary amounts are given (in the second round of experiments), the differences in preferences would become even larger. We have two settings, one concerns the prices 338, 384 and 472 and the other is 439, 504 and 657. Clearly, the differences between the first two is much smaller than between the first and the last, so we would expect that most prominent differences in preferences would appear for the cash price versus payments with the maximum amount of months.

4.3 Results

In this section we first present the results for the survey concerning LCD television sets, and next we see if these results are corroborated by the results for the couches.

4.3.1 Results for LCD television sets

Table 4.1: Estimation results for LCD television sets (all data 4500 and 3420 analyzed)

Variable	Estimate (standard error) Survey of 8 November 2010	Estimate (standard error) Survey of 25 November 2010
Intercept	-1.733 (0.111)	-1.331 (0.109)
LG (not Samsung)	0.994 (0.132)	0.648 (0.124)
Screen 94 (not 81)	0.661 (0.145)	0.749 (0.132)
Hertz 50 (not 60)	2.453 (0.105)	1.563 (0.098)
24 months (not cash)	***-0.641 (0.095)***	***-0.299 (0.089)***
McFadden R-squared	0.301	0.156
Intercept	0.788 (0.159)	1.321 (0.174)
LG (not Samsung)	-0.163 (0.152)	0.224 (0.168)
Screen 94 (not 81)	1.223 (0.164)	1.934 (0.178)
Hertz 50 (not 60)	1.069 (0.109)	-0.589 (0.129)
Maximum months (not cash)	***-3.706 (0.121)***	***-4.211 (0.135)***
McFadden R-squared	0.514	0.475

The estimation results for the two logit models for LCD television sets appear in Table 4.1. Students appear to favor LG, Screen size 94 and Hertz 50, as their associated parameters usually take a positive and significant value. Payment in 24 months is less preferred over cash and payments in the maximum amount of months are even less preferred, which can be seen from a comparison of the absolute values of the parameter estimates. When we compare the results for November 8 versus November 25 of 2010, we see differences across the parameters, but, as these estimates are correlated, we resort to an alternative method to highlight the differences across the results for the 8 and 25 November surveys.

Table 4.2: Estimated probability of purchase for LCD television sets (all data 4500 and 3420 analyzed)

	Survey of 8 November 2010	Survey of 25 November 2010 (With actual monetary value)
Type		
LG, Screen 94, Hertz 50		
Cash	0.915	0.836
Versus 24 months payments	0.850	0.791
Cash	0.949	0.947
Versus maximum months payments	0.313	0.211

Table 4.2 gives the estimated probabilities from the logit model for the cases where the LCD television sets are of the type "LG, Screen size 94 and Hertz 50", across the three levels of prices. The probability of purchasing this product using cash money is 0.915 while it reduces to 0.850 when one can pay using a 24 month period. This is not a very large difference, that is 0.065, and also for the 25 November survey, where the respective probabilities are 0.836 and 0.791, the difference 0.045 is not large. Matters change dramatically for the comparison of cash payments with the maximum amount of months. The purchase probability now reduces from 0.949 to 0.313 (is a 0.636 reduction) when only monthly terms are used, and it reduces from 0.947 to 0.211 (is a 0.736 reduction) when actual monetary values are mentioned. Comparing 0.313 to 0.211 entails about a 30% reduction of probability of purchase.

4.3.2 Robustness checks

So far, we relied on a logit model where are individuals were analyzed jointly. When we estimate the parameters of the same models for males and females separately, we do not find any noteworthy differences for the numbers in the current Table 4.2. The same holds when we consider the models for younger and older students and for different income levels. Hence, at least for these samples, we find that demographics do not matter much for purchase preferences versus payment methods.

To see if the results in Table 4.2 are robust, we had a second product evaluated, parallel to the television sets, and this concerned couches. Couches could be beige or gray, have seat size 45 or 46 and have normal or special comfort, and again, three levels of payment (methods). The key results appear in Table 4.3. Again we see not very large differences between cash and 24 months (from 0.761 to 0.685 in the first experiment and from 0.741 to 0.726 in the second). But, like in Table 4.2, the differences in preferences become salient when we evaluate cash payments against the maximum amount of months. There the reduction in preferences is from 0.271 to 0.146, which is about 50%.

Table 4.3: Estimated probability of purchase for couches (all data 4500 and 3420 analyzed)

	Survey of 8 November 2010	Survey of 25 November 2010 (With actual monetary value)
Type		
Color gray, seat size 46, normal comfort		
Cash	0.761	0.741
Versus 24 months payments	0.685	0.726
Cash	0.873	0.882
Versus maximum months payments	0.271	0.146

4.4 Conclusion

We conjectured that actually mentioning the price that one has to pay would make consumers less prone to opt for credit payments. More precise, when one would have consumers to evaluate a cash price of 338 euro versus 472 euro we would expect less preferences for the 472 euro product then when one would have consumers evaluate 338 euro against 59 months with only 8 euro per month. Even though this is a very simple computation, our experiments show that this happens indeed. In fact, the reduction in the preference ranges somewhere around 30% to 50%.

So, our recommendation is rather straightforward. We recommend the punch line “Borrowing money costs money” will be completed by the following: “When you purchase this television set it costs you 338 euro if you pay with cash now and the costs will be 472 euro when you pay 8 euro per month in 59 monthly terms”. We also recommend that product proposals consist of not only the amount in cash but also the total amount involved when you pay in terms.

Our research in this chapter can be extended in various directions. In our study we actually included rather basic computations. Indeed, consumers only had to multiply 59 with 8 to get the 472 euro. In more realistic settings, consumers face statements like "0.6% interest per month for 59 months"; and have to compute the 8 euro themselves, or alternatively, have to compute the number of months. A second issue concerns the products themselves. After 24 months one may expect that the television, say, still works, but perhaps after 59 months, or earlier, one needs to buy a new one. Hence, experiments could somehow include a deterioration of quality. Finally, we considered hypothetical products, and it would thus be even more interesting to see how our findings translate to natural experiments, where consumers may evaluate actual products on actual websites.

In chapters 3 and 4 we have seen that individuals can face financial innumeracy, and that they need help to make better financial decisions. In the next chapters we will deal with that help, when we focus on the relationship between consumers and their financial advisors.

Appendix 4A: The questionnaire

The first wave of data was collected on November 8 2010 and the second wave on November 25 2010.

The text for the survey reads as:
We kindly ask you to cooperate with the following survey. This survey is about making choices in the purchasing process of a durable good, like television sets, audio equipment and other household appliances. In each question you can choose between two different products. The features of each product differ from each other, like brand of the product, screen size or price. For each question we ask you to draw a circle around the product you prefer.
Many thanks for your kind help.

LCD-TV

You want to buy an LCD-TV and on the internet you see various offers. Each question displays two products between which you can choose. For each choice set we ask you to draw a circle around the product you prefer.

Choice set 1

	# 1:	# 2:
Brand	Samsung	LG
Screen size	94	81
Hertz	50	50
Payment	€ 338,00 in cash	59 monthly payments of € 8,00

Choice set 2

	# 1:	# 2:
Brand	Samsung	Samsung
Screen size	94	81
Hertz	50	60
Price	€ 338,00 in cash	24 monthly payments of € 16,00

Choice set 3

	# 1:	# 2:
Brand	LG	Samsung
Screen size	81	94
Hertz	60	50
Price	24 monthly payments of € 16,00	59 monthly payments of € 8,00

Choice set 4

	# 1:	# 2:
Brand	LG	Samsung
Screen size	81	94
Hertz	50	60
Price	€ 439,00 in cash	73 monthly payments of € 9,00

Choice set 5

	# 1:	# 2:
Brand	LG	Samsung
Screen size	81	94
Hertz	50	50
Price	€ 439,00 in cash	24 monthly payments of € 21,00

Choice set 6

	# 1:	# 2:
Brand	LG	LG
Screen size	94	81
Hertz	50	60
Price:	24 monthly payments of € 21,00	73 monthly payments of € 9,00

On November 25 2010 we circulated the survey that is similar to the above, except that the order of choice sets has changed and that the prices are now all in Euro's.

Choice set 1

	# 1:	**# 2:**
Brand	LG	Samsung
Screen size	81	94
Hertz	50	60
Price	€ 439,00	€ 657,00

Choice set 2

	# 1:	**# 2:**
Brand	Samsung	LG
Screen size	94	81
Hertz	50	50
Price	€ 338,00	€ 472,00

Choice set 3

	# 1:	**# 2:**
Brand	LG	Samsung
Screen size	81	94
Hertz	50	50
Price	€ 439,00	€ 504,00

Choice set 4

	# 1:	**# 2:**
Brand	Samsung	Samsung
Screen size	94	81
Hertz	50	60
Price	€ 338,00	€ 384,00

Choice set 5:

	# 1:	# 2:
Brand	LG	LG
Screen size	94	81
Hertz	50	60
Price	€ 504,00	€ 657,00

Choice set 6

	# 1:	# 2:
Brand	LG	Samsung
Screen size	94	81
Hertz	60	50
Price:	€ 384,00	€ 472,00

Chapter 5:
The results of the questionnaires

Abstract

In this chapter we describe the surveys we used to collect the data on consumers of financial products and on their advisors. We present the design of the survey and we give various statistics concerning the answers. We presented these statistics to the participating companies as a validity and reality check.

5.1 Introduction

This chapter deals with the survey that we used to elicit statements and opinions of consumers of financial products as well as the financial advisors who assisted them to make their choices. Various aspects of the survey will be used in the subsequent two chapters, when we put forward a range of hypotheses that are derived from the available literature. In this chapter the data will be described and various salient features will be addressed.

It is important that we interview customers of companies which sell financial services and their respective advisors. Due to privacy reasons we were not able to collect one-to-one relationships. In contrast, we have data on customers of two different firms and we have data on the financial advisors of these firms. So we do not have pair-wise data, and our results are based on the average scores. As we will see, these data are already rather informative and useful. We will also see that various unexpected outcomes are obtained.

We created a survey with a range of questions, and we distributed the survey via the internet. We also interviewed various managers of the participating companies to check whether our questions made sense, and, later on, to inform them about the outcomes.

In section 5.2 we provide more details on the survey. In Section 5.3 we present various statistics of the answers. The answers to each question are already quite interesting and noteworthy to discuss separately. In Section 5.4 we conclude with a discussion of our experiences when communicating the outcomes with the managers.

5.2 Survey design

In this section we first describe some general aspects of the survey. Next, we turn to more specifics on the surveys of the consumers and on those of the advisors.

We designed two internet-based surveys, which prove to be a useful tool (Cooke and Watkins, 2009). One survey concerns customers of financial companies and of financial advice. The second survey was distributed amongst financial advisors who give advice to individuals about their financial plans. There are various questions that overlap in the two surveys, and particularly these are of interest to evaluate the match between consumer and advisor.

The surveys contain a range of statements, and the respondents are asked to indicate on a scale of 1 to 7 whether they strongly disagree (1) or strongly agree (7). We did not use the option ‘I do not know’ to force respondents to have an opinion about each statement. At the end of the survey we asked personal information, like gender, age, education level for the consumers and, additionally, the years of experience for the financial advisors.

The statements are based on important issues of financial advice, which are described in recent legislation, such as WFT (“Wet Financieel Toezicht”) en NRFD (“Nadere regeling financiële dienstverlening”). These issues concern disclosure, quality of advice, understandability of advice and the relevance of the prospectus (which may include statements of risk and uncertainty).

The surveys are in Dutch, but for this thesis the text has been translated into English. We chose for Dutch as the addressed group of respondents concerns customers of Dutch financial companies and Dutch-speaking financial advisors of these Dutch financial companies. During the preparation of the questionnaire, we were in close touch with the participating companies about the tone of voice of the questionnaire and about the number of people who should receive the questionnaire. Also, there has been interaction on the appropriate presentation of the questionnaire to the group of customers and financial advisors. The exact timing of the distribution of the questionnaire to the group of customers was in accordance with the companies’ customer contact moments and other customer campaigns. As some items in the questionnaire deal with topics that were very relevant at the time, receiving much media attention, and as some of the companies claimed to change their strategy to improve advice and to comply to legislation about this financial advice, it was important that we adhered to a strict planning for sending out the questionnaires.

5.2.1 Survey amongst the consumers

For the survey of the customers we selected those who purchased a financial product in the most recent two years. In total 7000 customers received an invitation to participate in our research, and these were randomly selected provided their recent purchase. A customer received an email or a letter of the related company with an invitation to join the research. The companies informed their customers that they think customer information is of great value to the company and therefore they encouraged the customers to fill in the questionnaire. Customers were however free to participate in the survey. The group who received the invitation via the internet could find the questionnaire directly by clicking on the hyperlink in the email. The group who received the invitation by letter could find the questionnaire using an internet connection at home. Due to the internet facilities, all data were collected easily and they were also unambiguous and anonymous. The participants did not receive any kind of reward or payment for their cooperation. The customers, who received an invitation by email, received a reminder after two weeks. The customers who received an invitation by letter did not receive a reminder.

The survey of the customers is divided in four paragraphs. At first there are statements about the need of financial advice. These questions were included to check if a customer had purchased a financial product recently. Second, there are statements on the knowledge of customers about the financial products and about the choices they make in the purchasing process. The third set of questions and statements is about the quality of the received advice. The last questions are some general questions concerning age, gender and education.

5.2.2 Survey amongst the advisors

The addressed financial advisors are employees of the participating companies. They are all trained as retail advisors and advise customers of financial products. The two participating companies sent an email to all their employed advisors of financial products and asked these advisors to participate in our survey. In total 640 financial advisors received an invitation to participate in this research project. The email included a hyperlink to the internet survey. By clicking this hyperlink, the internet survey started. The advisors were not obliged to fill in the internet questionnaire, and they were allowed to participate during working hours. Again, also these participants did not receive any reward for their cooperation.

The survey of the advisors consists of six paragraphs. First, we ask on which products they give advice. The next paragraphs have questions in the form of statements. Again, participants could answer with (1) as strongly disagree to (7) strongly agree. The first set of statements concerns the transparency of advice and the knowledge of customers about the financial products and about the choices they made in the purchasing process. The next set of questions and statements is about the (own perceived) quality of the given advice. Then we ask about the presumed perception of the customer of the quality of the advice. Next we ask questions about the time schedule of the advisor and the relative importance of advising and administration. The final set of questions concerns age, gender, education, and the number of years of experience. We code these last questions as zero-one dummy variables and use them in a regression of the scores on the dummies to see if demography's matter.

Internet surveys can have their limitations, and therefore we also held a few personal interviews. These interviews were held with eight senior financial advisors of the participating companies, who all have ample experience in providing financial advice to retail customers. The questions asked were approximately the same questions as in the internet survey. Their answers were useful to put the work of the advisors in perspective, and as such we also obtained a check for the validity of the survey questions.

5.3 Results

The internet survey was prepared and executed in a period of instability in financial markets worldwide. Several banks went bankrupt and many individuals lost much in the stock market. In the Netherlands the DSB bank collapsed. This actually happened only one month before our first internet survey among the customers was held. This DSB bankruptcy marked the peak of the financial crisis in the Netherlands. Various insurance products were also vulnerable those days. In general, customers had low confidence in suppliers of financial products and in their advisors. Our participating financial companies did not have problems with their solvency or image, but we might expect slightly different answers to some questions than one would have obtained in non-crisis times. Financial advisors themselves could notice the changing climate. Many of them worked like 'business as usual', but they all felt the uncertainty in the market and were seeking for new ways to give their advice. They all had to face new legislation and strongly regulated supervision.

The survey was carried out in two periods. The first period started in December 2009 and ended by the end of January 2010. The second period was from April 2010 until the end of May 2010. Out of the 7000 customers, only 313 customers completed the internet survey. This is a response rate of 4.47%, which seems reasonable. Also, the very amount of 313 should allow us to draw some generalizing conclusions. We were more successful with the advisors, as in total 266 advisors completed their internet survey. This is a response rate of 41.6%.

5.3.1 Results for the customer surveys

The questionnaire was sent to customers who live in both urban and rural regions in the Netherlands. In total we acquired 313 completed surveys, although some personal questions were not answered by all individuals. Only 4% of the customers say they will only buy financial products trough internet and no longer need the help of financial advisors. Two-thirds of the respondents were male. The average age of the respondents is in between 41 and 50 years. Almost one-third of the respondents obtained at least a high-school degree ("HAVO"), and more than one-third indicated that they have a university degree. This means that our respondents have a more than average level of education.

Table 5.1: Products purchased in the current and last year

Type of product	Amount	Respondents
Current account	55	309
Overdraft	9	309
Savings account	94	309
Credit card	32	309
Fixed credits/ revolving credits	17	309
Mortgage	63	309
Life Insurance	86	309
Non-Life Insurance	62	309
Investments	20	309
Investments including insurance	25	309
Risk of Life Insurance	29	179
Burial insurance	22	179

The respondents state that they are interested in financial matters either average or only little. A large group (close to two-third) state, they are average or little interested in economic issues.

In sum, our respondents are middle-aged, highly educated but are not much interested in financials or economics.

In the first part of the questionnaire we ask some general questions. The first is about the number of individuals who recently purchased a financial product upon the suggestion of their advisor. It turns out that 12 of the 313 customers indicated that they purchased a financial product from another advisor than in our survey. Also, 14 customers indicate that they prefer to purchase a financial product using the internet only. The other 299 individuals state that they will go and visit an advisor also the next time.

Table 5.1 presents the types of products that consumers purchased in the current or previous year. It is clear that they all seem to have substantial experience.

Customer knowledge (CK)

We start with twenty three questions on the knowledge that the customers claim to have. We present each time a histogram with the number of answers, where we give the statement in the label of each graph.

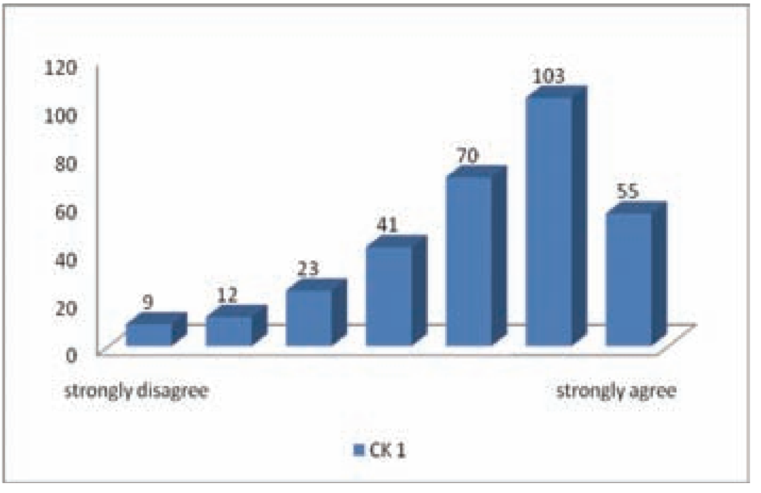

Figure 5.1: Answers to
"I consult my financial advisor for a reliable advice"

Figure 5.1 gives the answers to the first statement. Table 5.2 later on will present the test results for the test whether the mean is equal to 4. Figure 5.1 shows that more than 72% of the respondents agree with the statement that their financial advisor gives a reliable advice. The median is 6. The respondents are apparently very convinced they should go to a financial advisor for a reliable advice. They seem aware of the added value of the advisor. Whether a consumer is interested in finances turns out not to be relevant for this opinion. Mostly individuals in between 51-60 years old agree with this statement, followed by the age group of 21-30 years. Education seems not important.

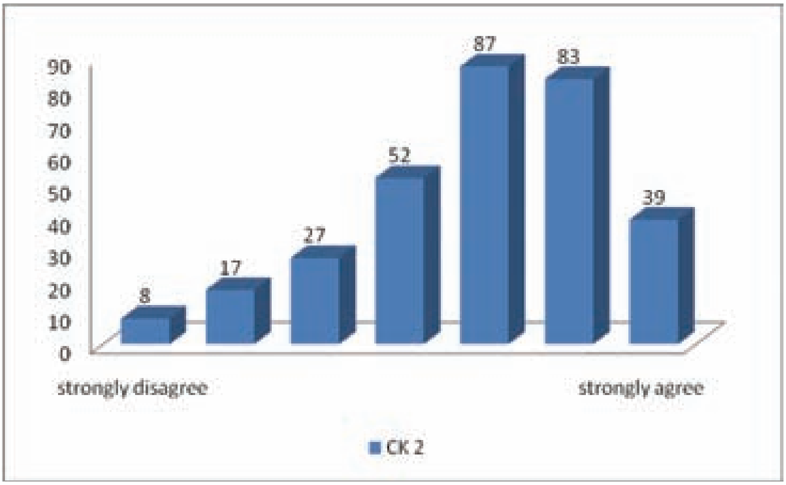

Figure 5.2: Answers to
"My advisor gives me the best possible solution to my financial question"

Figure 5.2 shows the answers to the second statement. Almost 67% of the respondents agree with this statement. Younger individuals do agree more than the older-aged response groups. The largest group of the respondents who agree with this statement have at least a high vocational education (HBO). Again, an interest in financials seems not to play a role.

Figure 5.3 contains the answers to the third question. Almost 56% of the respondents agree with this statement and concur that they will search for product information on the internet before they see their financial advisor. People in all age groups say they look for such information first. The age group 51-60 years agrees most, that is, 64% of those respondents say they prepare their visit to the financial advisor. Education plays an important role. People with higher education are more prepared.

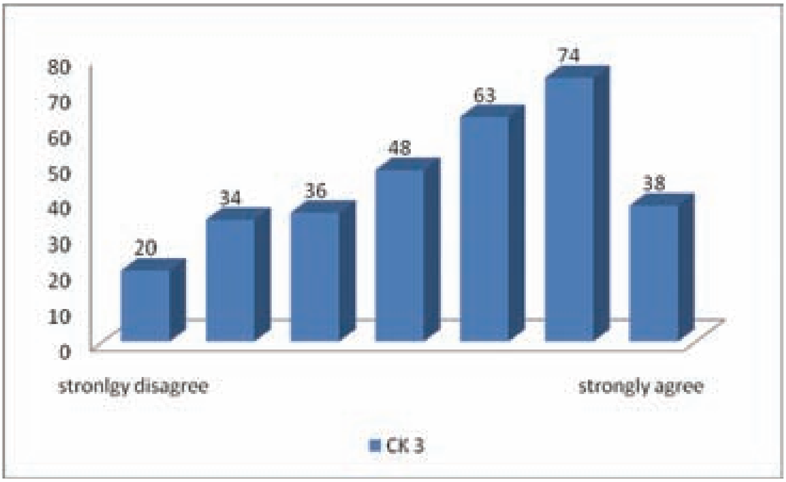

Figure 5.3: Answers to
"Before I see my advisor for financial advice, I search for product information on the internet"

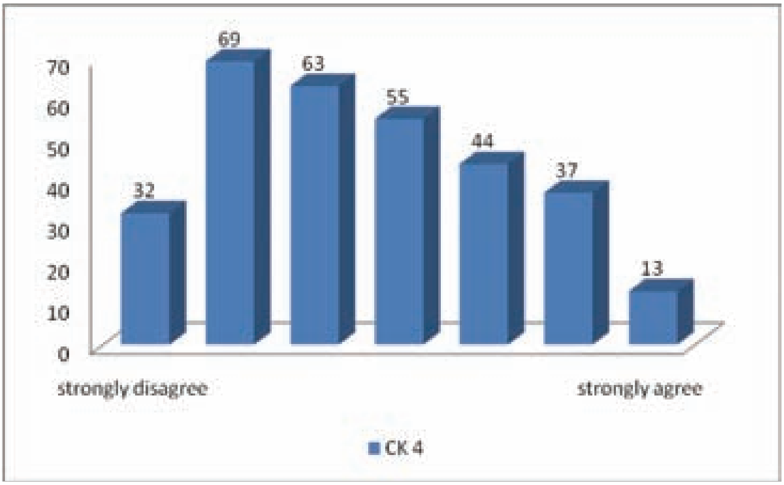

Figure 5.4: Answers to
"I receive so much information about financial products that I cannot disentangle relevant from irrelevant information"

Figure 5.4 shows customers' responses to statement CK 4. More than 52% of the respondents do not agree with this statement. Age seems to be important in disentangling relevant from irrelevant information. Younger individuals disagree more than the older customers. Education is also important. Highly educated people strongly disagree more than others.

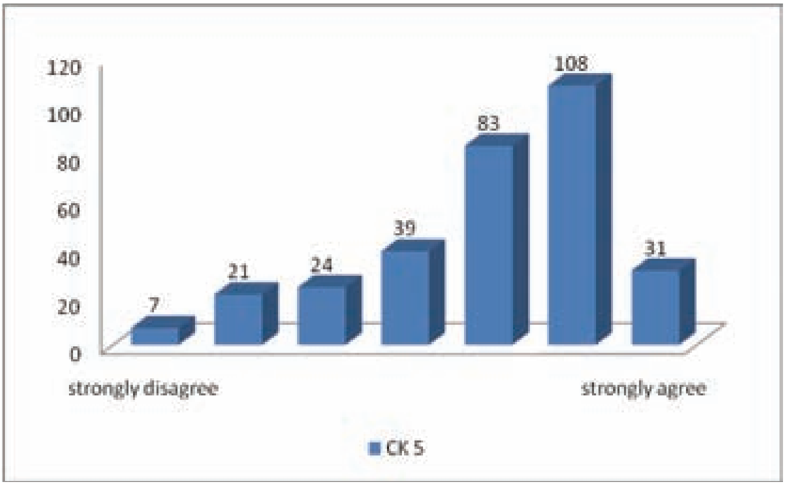

Figure 5.5: Answers to
“After taken advice from my financial advisor I have full knowledge of the consequences of my choices”

Respondents mostly agree with statement CK5. More than 70% of the respondents seem convinced that they have full knowledge of the consequences of their financial choices after taken advice from their financial advisor. Older people do agree stronger than the younger respondents.

Figure 5.6 shows that more than 65% of the customers agree with statement CK6. Age does not seem to play much of an important role. The group between 31-40 years old agrees a little less with this statement. The level of education does not seem to be important.

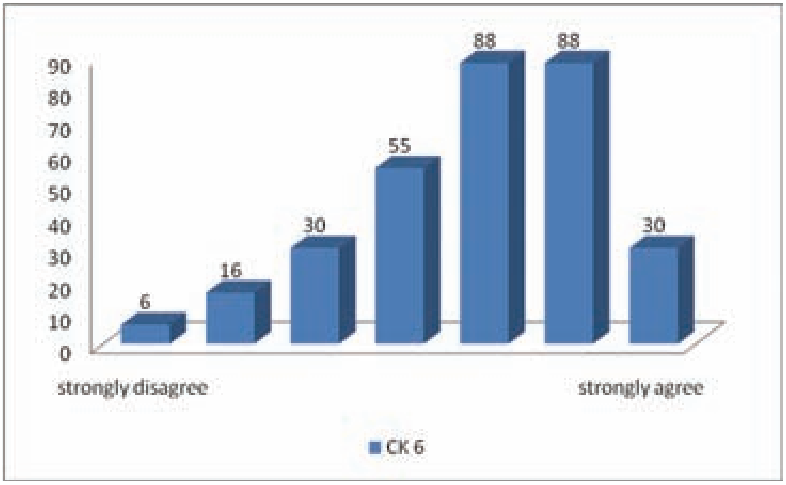

Figure 5.6: Answers to
"My advisor gives a full overview of the financial products that are relevant to me"

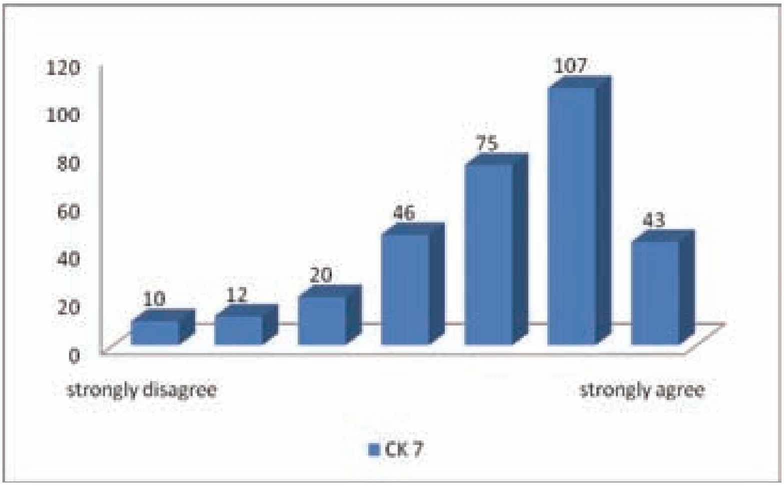

Figure 5.7: Answers to "The financial advice I received met my needs"

Respondents appear to be satisfied with the financial advice they have received in the sense that it met their financial needs. Figure 5.7 shows that almost 72% of the respondents agree with this statement. The age group of 51-60 years old agrees the most as almost 78% of this age group does agree with this statement. Education is not an important factor.

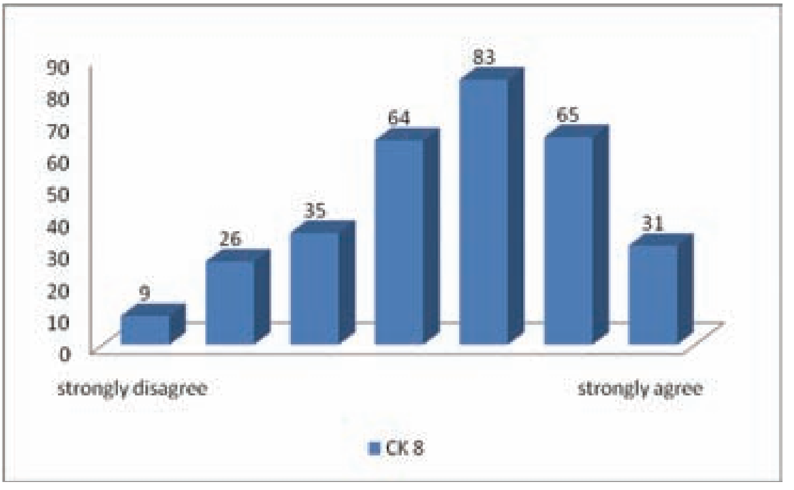

Figure 5.8: Answers to "Experience with financial products by people near to me is as important as the financial advisor's advice"

Figure 5.8 shows that more than 57% of the respondents agree with this statement, although the group 'slightly agree' is the largest response group (83). Age does play a role but a small one. Younger respondents agree a bit more than average. The older age groups agree less. This means that younger people are more influenced by their environment than older people are. Education also plays a role. People with higher education agree slightly more with this statement than people with a lower education.

Good previous experience with a financial advisor seems to be important to decide to go to the same financial advisor the next time. More than 89% of the respondents agree with this statement, see Figure 5.9. Age category and level of education does not seem to be important.

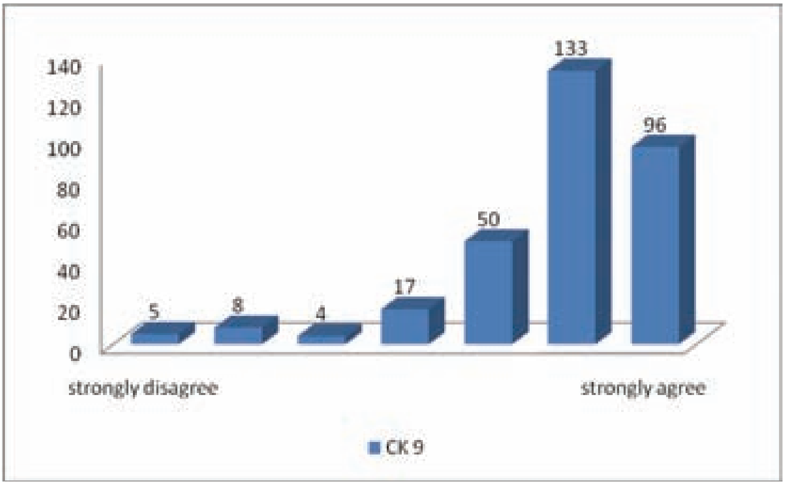

Figure 5.9: Answers to "When my financial advisor helped me well before, I will go for a consult the next time"

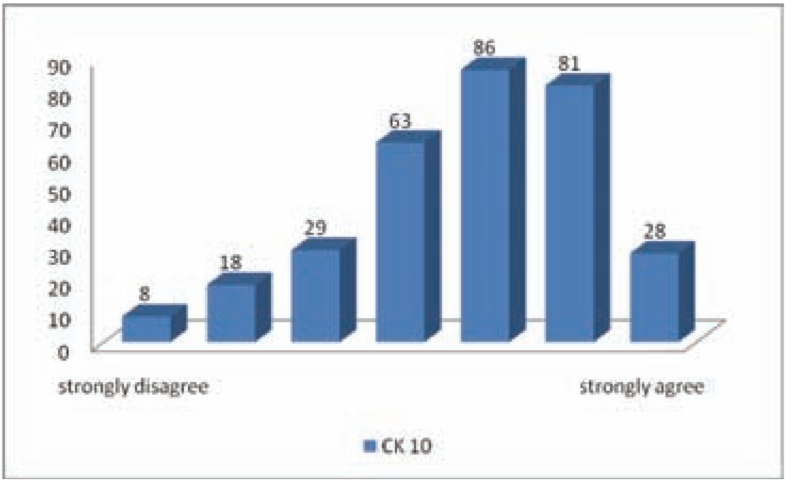

Figure 5.10: Answers to "The advice of my financial advisor is crucial for my product satisfaction"

Figure 5.10 depicts the responses to statement CK10, which concerns satisfaction. More than 62% of the respondents agree with this statement. Age seems to be important. The younger response group does agree with this statement, but the percentage of respondents is lower than the respondents of the older age group. In fact, it differs more than 11%. The older age group answers above average, and the younger below average. Interest in finances seems to play a more important role, as more interest is correlated with a higher score. Education also seems relevant. People with higher education agree below average and people with lesser education agree more than average on this statement.

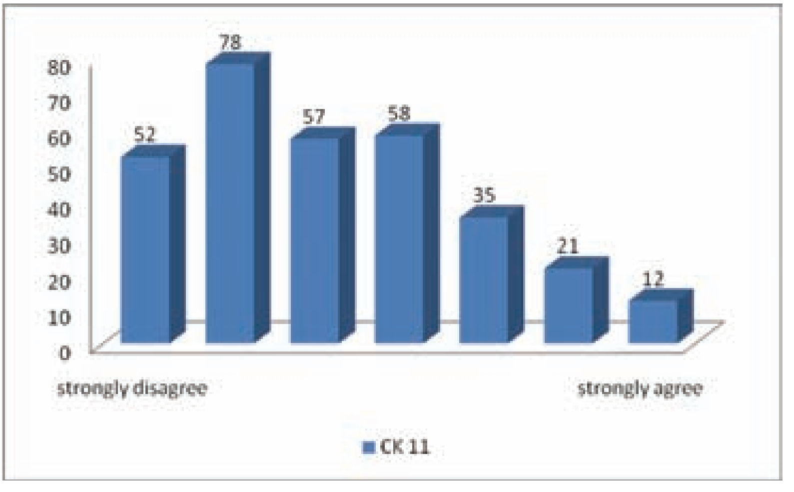

Figure 5.11: Answers to "I want to solve my financial / insurance needs right now. I will find out later if this solution is the best in the long run"

Figure 5.11 shows that 60% of the consumers disagree with this statement, which means that people have also a long term focus with their financial decisions. The respondents in age groups 21-30 years and 51-60 years disagree the most and above average. Out of the response group 21- 30 years it is 73% of the respondents who disagree with this statement. The respondents in the other age groups disagree below average. Higher educated people also disagree most.

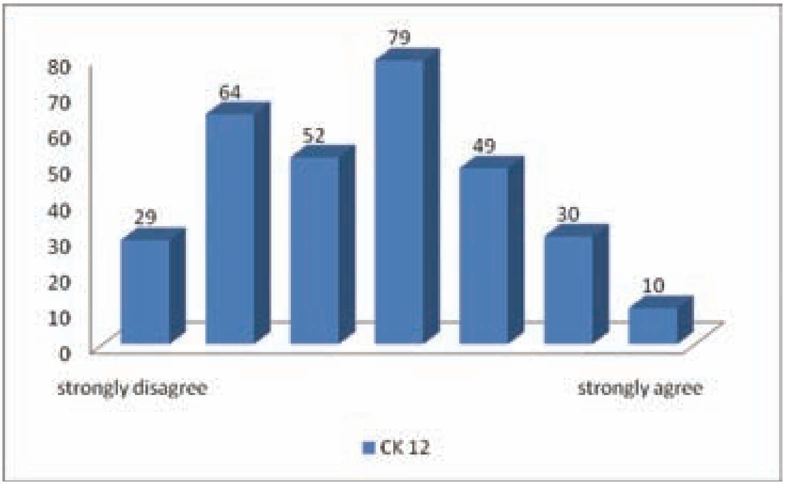

Figure 5.12: Answers to “My advisor’s solution goes beyond my financial possibilities”

Figure 5.12 shows the responses to statement CK12. Many respondents disagree with this statement. This means that consumers are aware of their financial possibilities even though their financial needs desire more. People with higher education more strongly disagree with this statement.

Figure 5.13 shows the results of the statement on the advisors fee and the relevance of paying for a good financial advice. Table 5.2 shows that the results are not significant, which is due to the fact that 38% of the respondents disagree with this statement, 39% agree with this statement and 23% of the respondents do not agree nor disagree. Of the higher educated customers 70% disagree with this statement. Age does not seem to be important, although people in the age groups 41-50 and 51-60 years old disagree the most with this statement and do not seem to want to pay for financial advice. In sum, the fee for the advisor does not seem to be an important issue amongst the customers.

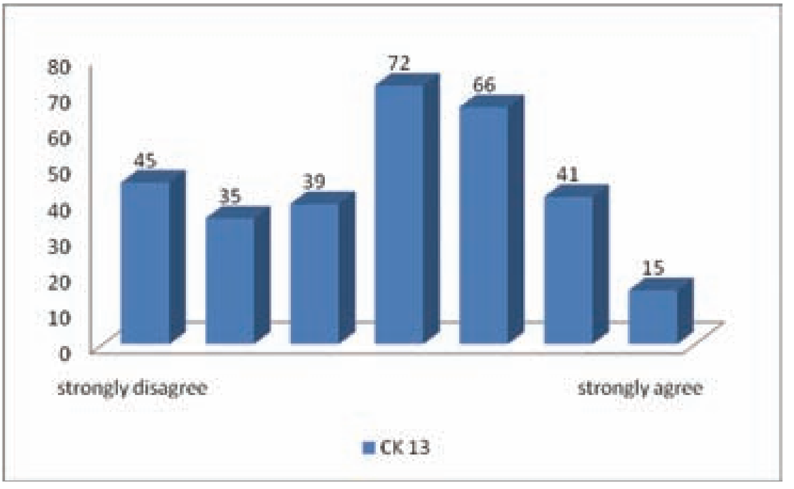

Figure 5.13: Answers to “I want to pay a fee for good financial advice”

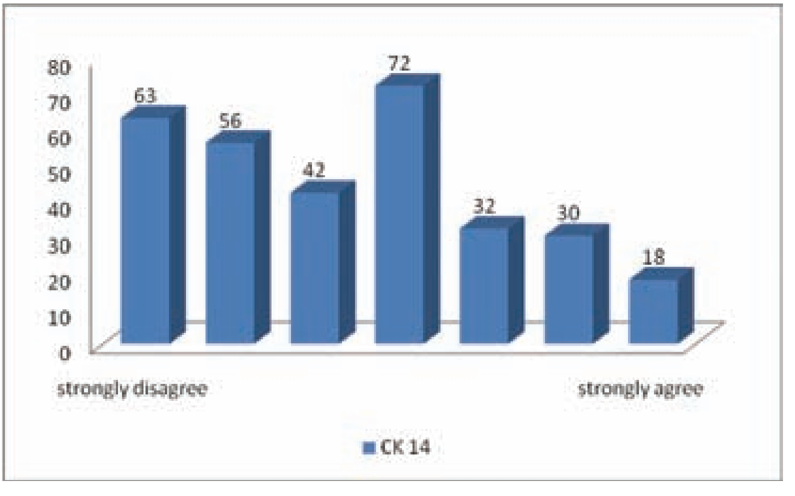

Figure 5.14: Answers to “The size of the advisor’s fee is relevant for my choice to purchase a financial product”

Figure 5.14 shows the results on statement CK14, and these support the findings for CK13. This statement also concerns the size of the advisor's fee. More than 51% of the respondents do not agree with this statement. They say the advisor's fee is not relevant for their choice of a financial product. 23% of the respondents do not agree nor disagree on this statement. Age does not seem to be relevant, nor does education.

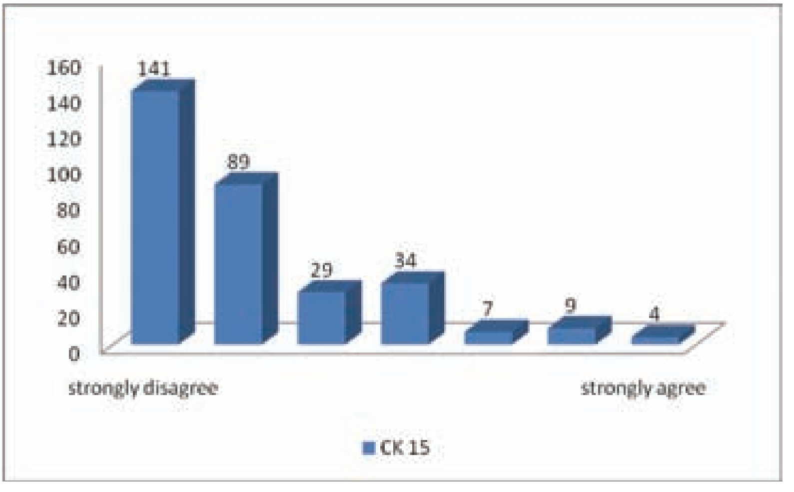

Figure 5.15: Answers to "The higher the fee for financial advice, the better it is"

Figure 5.15 shows that more than 82% of the respondents disagree with this statement. They do not see a relationship between a fee and good financial advice. Age and education do not seem to be important. This is quite an interesting result, and we return to the relevance of the fee in chapter 7.

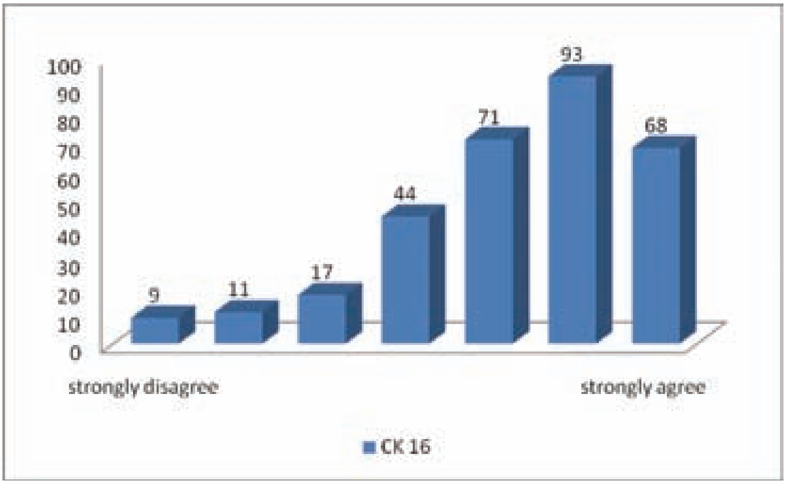

Figure 5.16: Answers to "I think it is useful to have a periodic dialogue with my financial advisor to see if my financial products still are sufficient for my financial needs"

Figure 5.16 shows the results for the statement on periodically analyzing financial needs. More than 74% of the respondents think these dialogues with their financial advisor are useful. The respondents of all age groups agree on this topic, except the age group from 61 years and older. The level of education does not seem to be important.

Figure 5.17 deals with the importance of written information related to the verbal advice of the financial advisor. Almost 52% of the respondents agree with the statement that the verbal advice of the financial advisor is more important than written information when they consider purchasing a financial product. About 18% of the respondents do not agree or disagree with this statement. Age of the respondent and level of education does not seem to be very important.

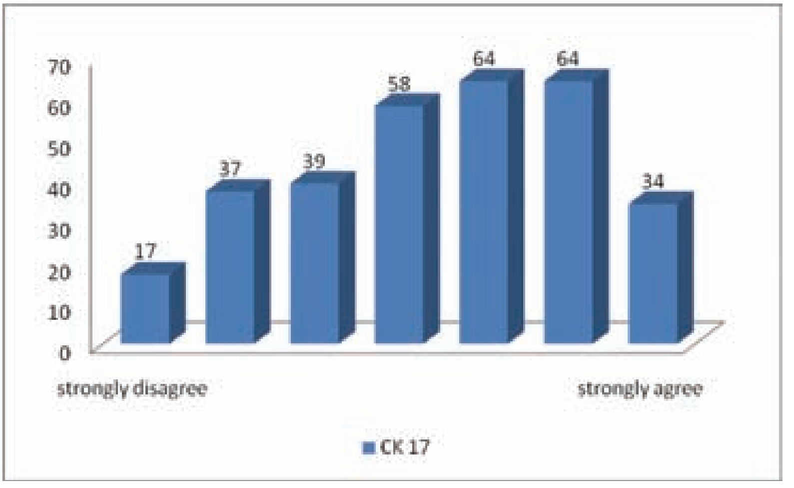

Figure 5.17: Answers to "A verbal advice of the advisor is more important than written information for my choice of a financial product"

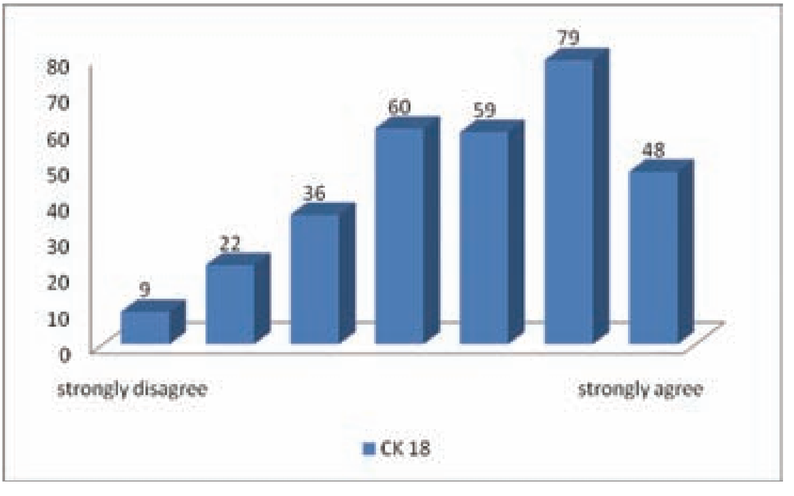

Figure 5.18: Answers to "I read the information on a Financial Information Leaflet"

The Financial Information Leaflet for some financial products is currently obligatory when providing financial advice on these products. Figure 5.18 shows the responses to statement CK18 where we ask if the consumers actually read the information on the Financial Leaflet. 59% of the respondents agree with this statement. There seems to be no relationship with age, although the respondents older than 61 disagree the most. The respondents with an HBO education level agree more often than respondents with other education levels.

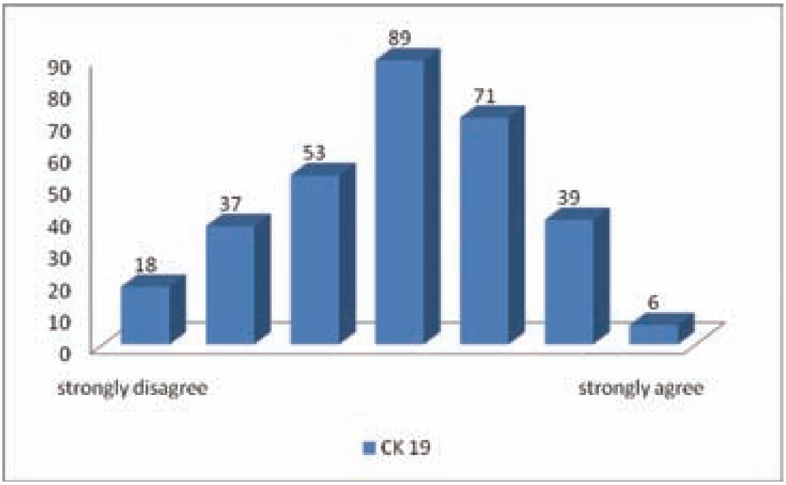

Figure 5.19: Answers to "I understand the information on a Financial Information Leaflet"

Not only reading a Financial Leaflet is important, understanding the contents of the leaflet is even more important. Figure 5.19 shows that 35% of the respondents disagree with this statement, almost 29% of the respondents do not agree or disagree and 37% of the respondents agree with this statement. These results are in all age groups and education levels, where people with HBO education disagree the most with this statement. Table 5.2 shows that the mean answer is not significantly different from 4. This is an interesting result, as it casts doubt on the relevance of such a leaflet.

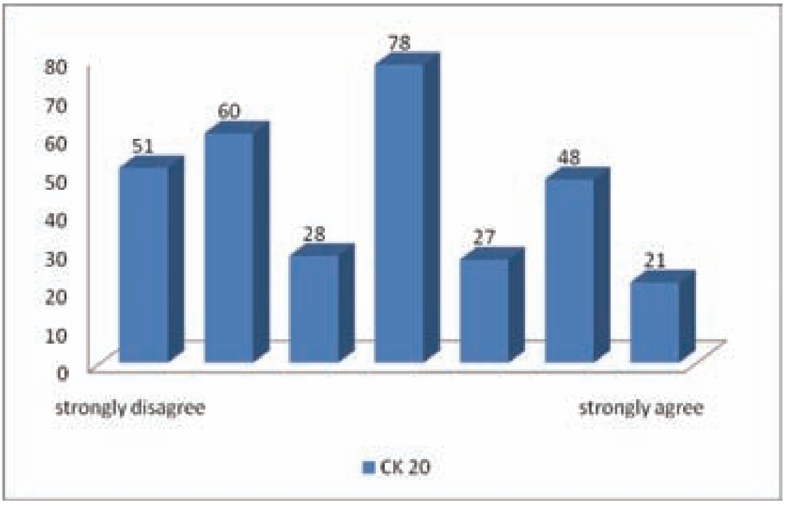

Figure 5.20: Answers to "I prefer paying a fee for financial advice based on time spent rather than as a percentage of the agreement"

Figure 5.20 shows the results of statement CK20. Almost 45% of the respondents disagree with this statement, that is, they do not want to pay a fee for financial advice based on time spent. They apparently prefer costs as part of an agreement. 30% of the respondents agree with this statement and prefer a separate fee. About 25% of the respondents do not agree or disagree. Age does not seem to be important, neither does level of education.

Figure 5.21 is about the importance of earlier experiences in purchasing financial products in the current purchasing situation. More than 73% of the respondents agree with this statement. All age groups show qualitatively the same results. Only the group 21-30 years old strongly agrees nor disagrees with this statement. Education plays a role, higher educated people strongly agree with this statement.

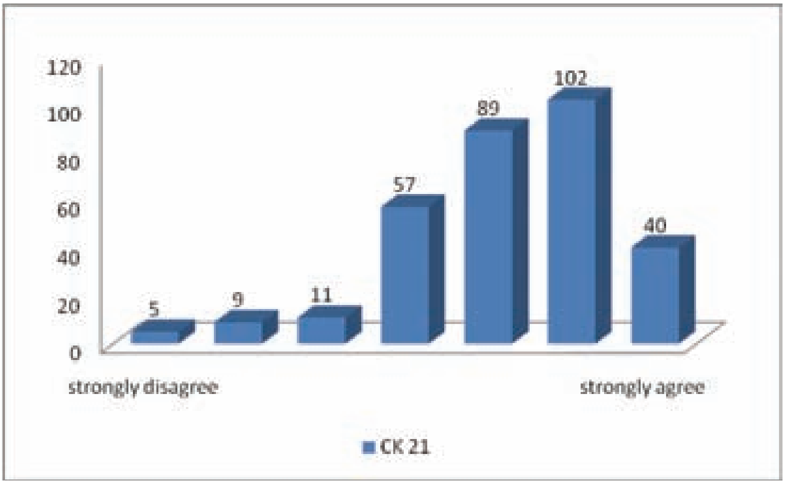

Figure 5.21: Answers to "Earlier experiences in purchasing financial products are important for my recent purchase of a financial product"

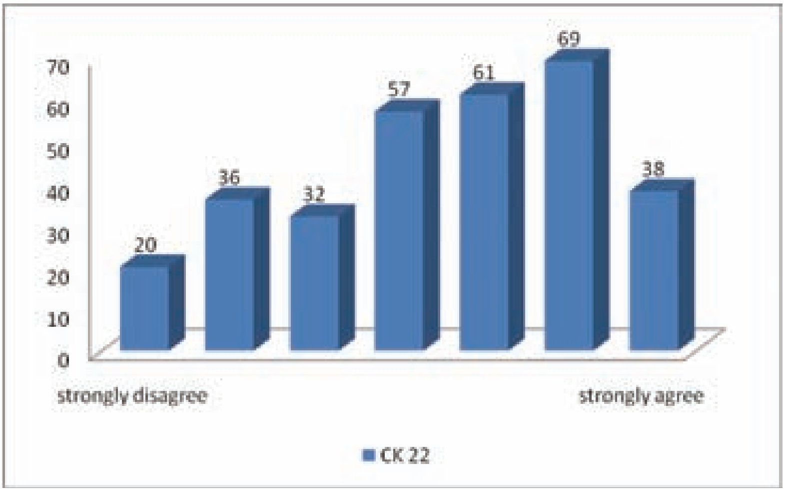

Figure 5.22: Answers to "A warning for loan advertisements makes me hesitant"

Figure 5.22 deals with a loan warning. More than 55% of the respondents agree with this statement that a warning (like "Borrowing money costs money") does make them to hesitate. Education seems to be important, because people with higher education disagree more with this statement, that is, they hesitate less after a warning. The age group 21-30 years and age group 51-60 agree more wih this statement.

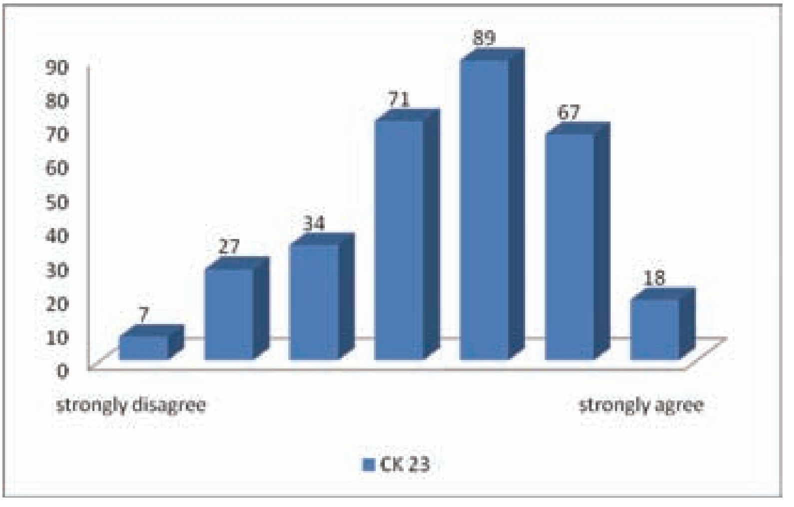

Figure 5.23: Answers to "The advisor's advice is crucial for my purchase decision"

Figure 5.23 shows that more than 55% of the respondents agree with the statement that their advisor's advice is crucial for their purchase decision. Age or education does not seem to be important.

Table 5.2 presents some key statistics on this first set of twenty three questions concerning consumer knowledge.

Table 5.2: Key statistics for the questions on consumer knowledge (the p-value concerns the test whether the mean equals 4)

Question	Mean	Median	P-value	Percentage	
				<4	>4
CK1	5.17	6	0.000	14.10%	72.80%
CK2	4.91	5	0.000	16.61%	66.77%
CK3	4.51	5	0.000	28.75%	55.91%
CK4	3.55	3	0.000	52.40%	30.03%
CK5	4.97	5	0.000	16.61%	70.93%
CK6	4.88	5	0.000	16.61%	65.81%
CK7	5.10	5	0.000	13.40%	71.88%
CK8	4.61	5	0.000	22.36%	57.19%
CK9	5.82	6	0.000	5.43%	89.14%
CK10	4.78	5	0.000	17.57%	62.30%
CK11	3.18	3	0.000	59.74%	21.73%
CK12	3.59	4	0.000	46.33%	28.43%
CK13	3.84	4	0.098	38.02%	38.98%
CK14	3.37	3	0.000	51.44%	25.56%
CK15	2.11	2	0.000	82.75%	6.39%
CK16	5.26	6	0.000	11.82%	74.12%
CK17	4.42	5	0.000	29.71%	51.76%
CK18	4.81	5	0.000	21.41%	59.42%
CK19	3.96	4	0.582	34.50%	37.06%
CK20	3.63	4	0.000	44.41%	30.67%
CK21	5.18	5	0.000	7.99%	73.80%
CK22	4.48	5	0.000	28.12%	53.67%
CK23	4.54	5	0.000	21.73%	55.59%

Perceived quality of advice (CQ)

We now turn to five questions asked to the customers, on the perceived quality of advice. So, this is what consumers say about the quality of the advisors. Table 5.3

gives some descriptive statistics of these questions, where it can be seen that all mean answers significantly differ from 4.

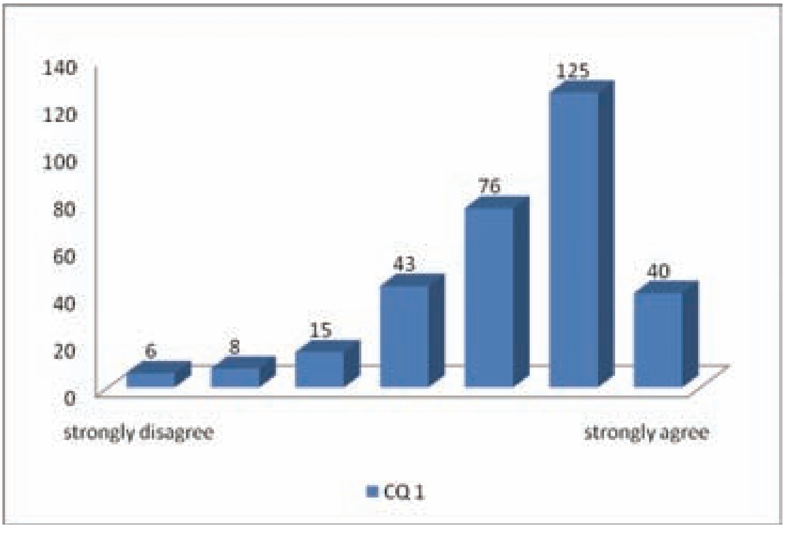

Figure 5.24: Answers to "My advisor has sufficient knowledge"

Figure 5.24 shows that 77% of the respondents agree with this statement and think that the advisor has sufficient knowledge to give them advice. Age or education does not seem to be important.

Figure 5.25 indicates that almost 66% of the respondents believe that advisors have creative solutions when they give advice. Again, age or education does not seem to be important.

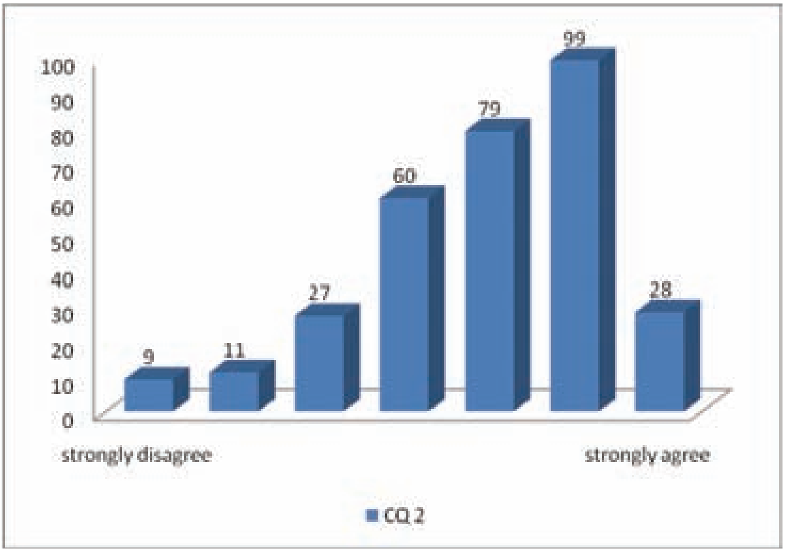

Figure 5.25: Answers to “My advisor provides me with creative solutions”

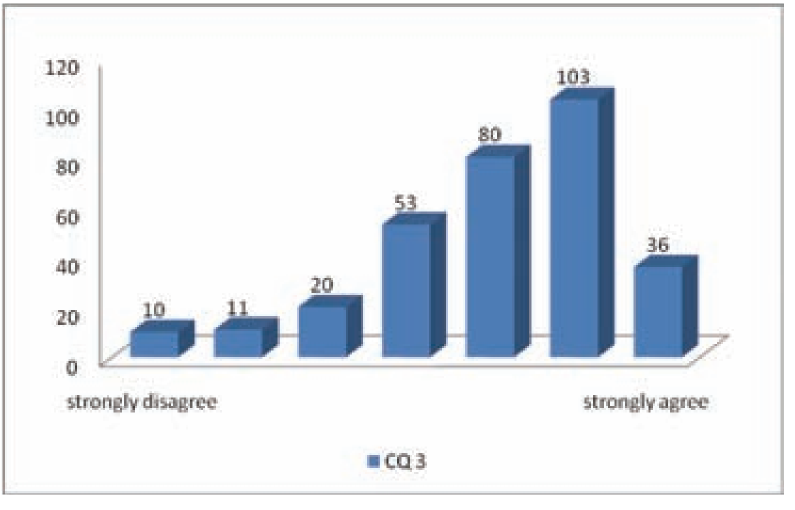

Figure 5.26: Answers to “My advisor gives me a proper advice”

Figure 5.26 suggests that almost 70% of the respondents agree with this statement, that is, customers think the advice is proper. Age nor education is important here.

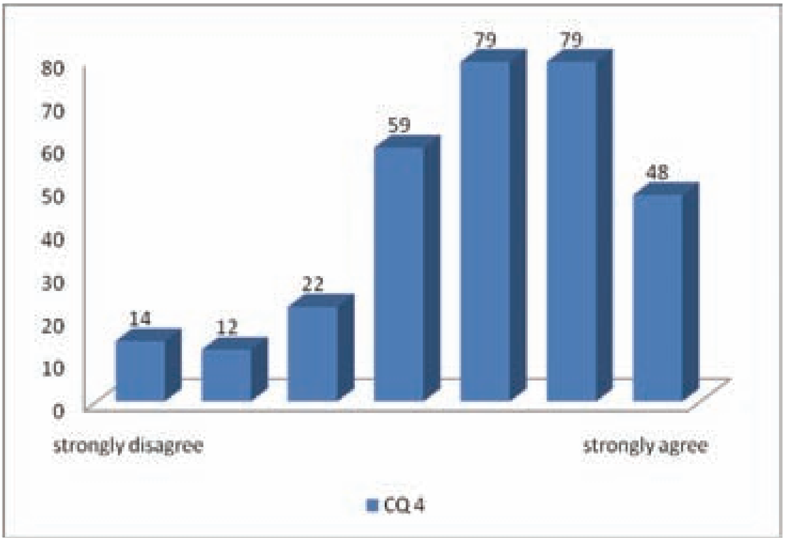

Figure 5.27: Answers to "My advisor is accessible to me"

Almost 66% of the respondents are satisfied with the accessability of the financial advisor. Age and education do not matter.

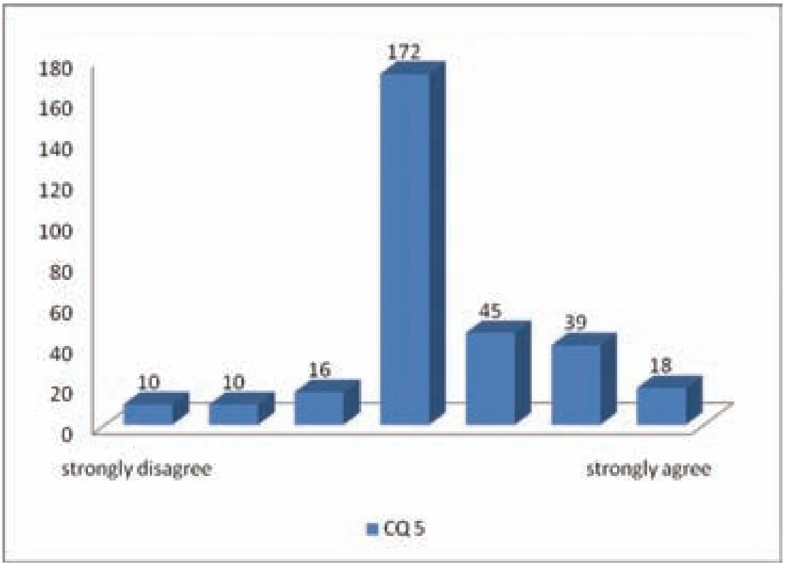

Figure 5.28: Answers to "The fee of my advisor is correct"

Finally, more than 55% of the respondents are indifferent or unlearned to whether the fee of the advisor is correct. Age and education does not seem to play a role. Again, this is an interesting finding, as usually it is assumed that the fee is very important. We return to this issue in Chapter 7.

Table 5.3: Key statistics for the questions on quality, as perceived by the consumer (the p-value concerns the test whether the mean equals 4)

Question	Mean	Median	P-value	Percentage	
				<4	>4
CQ1	5.27	6	0.000	9.27%	77.00%
CQ2	4.91	5	0.000	15.02%	65.81%
CQ3	5.03	5	0.000	13.10%	69.97%
CQ4	4.94	5	0.000	15.34%	65.81%
CQ5	4.36	4	0.000	11.61%	32.90%

5.3.2 Results for the advisor surveys

The participating companies distributed the questionnaire to their financial advisors. All these advisors give advice to individual customers about financial goals and financial products. No less than 266 advisors completed our internet survey. This is a response rate of 41.6%. Some advisors did not supply us with their personal information. About 78% of the advisors is male. 40% of the advisors is between 41 and 50 years old, and they have an average number of years of experience between 10 and 15 years. Their education level typically ranges from HAVO/MBO to HBO, and an academic degree seems rare.

The questionnaire started with information about which products the advisors give financial advice. Table 5.4 shows that there is a wide range of products of their attention.

Table 5.4: The advisors give advice about the following products

Product	Amount	Total
Current- and savings account	81	266
Consumer credits, overdraft	70	266
Investments	74	266
Investments and Insurances	33	266
Life Insurances	231	266
Non- Life Insurances	231	266
Mortgages	192	266
Risk life insurance	169	266
Funeral insurances	154	167
Other	48	266

Own perceived performance by the advisors (AM)

The first twenty three statements are about the own perceived performance of the advisors. The next set of statements concerns the quality of their advice. Again, we examine if age, education, and experience matter for their answers, using simple regression techniques.

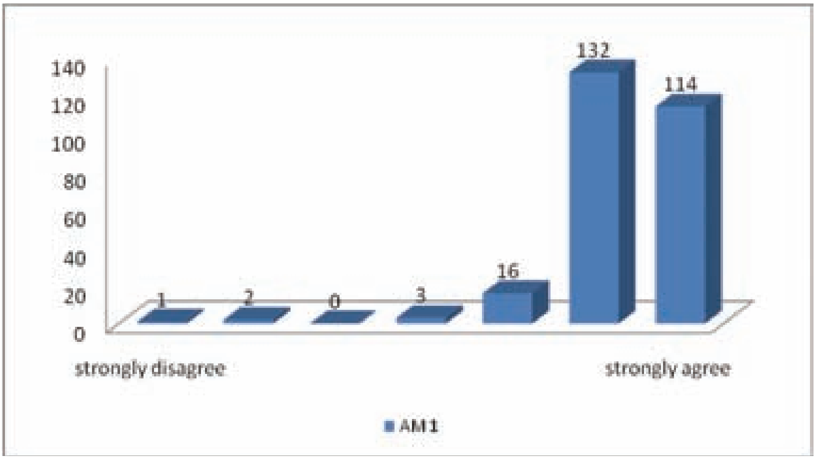

Figure 5.29: Answers to "With my advice I give the customer the feeling that s/he will make a good choice when purchasing a financial product"

Figure 5.29 presents that 97% of the respondents agree with this statement, that is, advisors are quite convinced that they give a customer a good feeling and that the customer will make a good choice. Table 5.5 gives the statistics of the various questions, and it is evident that the answers to this question significantly deviate from 4.

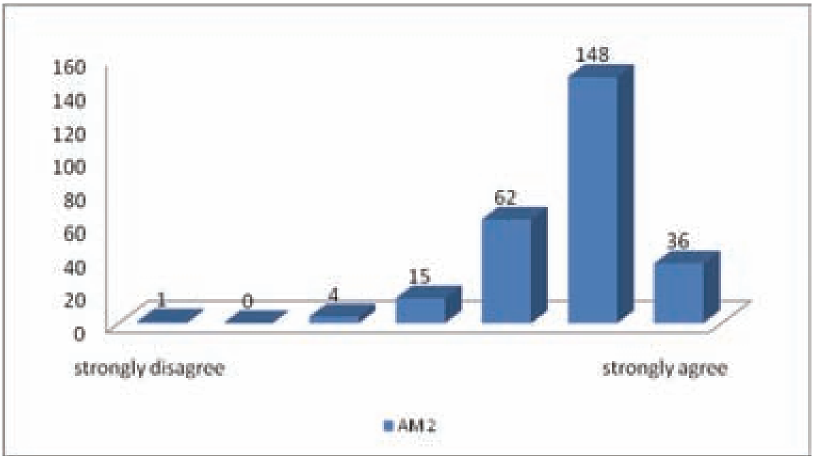

Figure 5.30: Answers to "My customers follow my advice for the solution of their financial needs"

Figure 5.30 shows that more than 92% of the advisors agree with this statement, that is, most customers will follow their advice about a solution to their financial product. The more years of experience, the more the advisor agrees with this statement.

Figure 5.31 show the results of statement AM3. Table 5.5 shows that the mean answer does not differ from 4. More than 42 % of the respondents do not agree with the statement. More than 33% of the respondents agree with the statement and more than 23 % of the respondents do not agree nor disagree. Lower educated advisors and also older advisors do agree more with this statement than their colleagues.

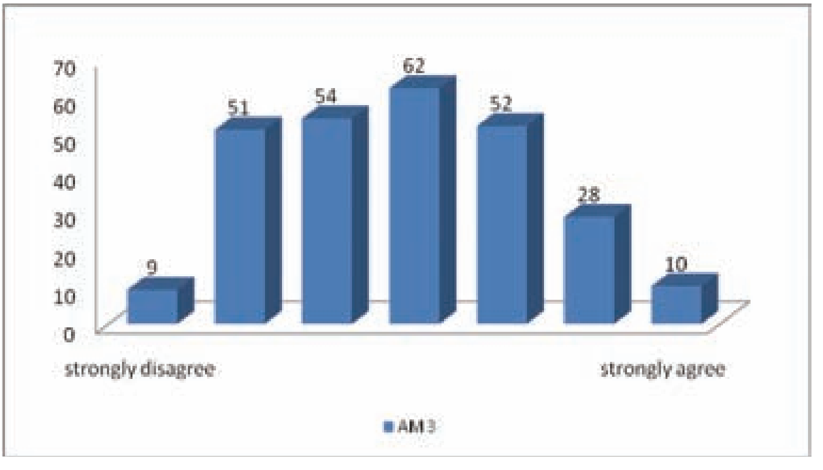

Figure 5.31: Answers to "Customers are well prepared about which solutions and products they want before they come to me for advice"

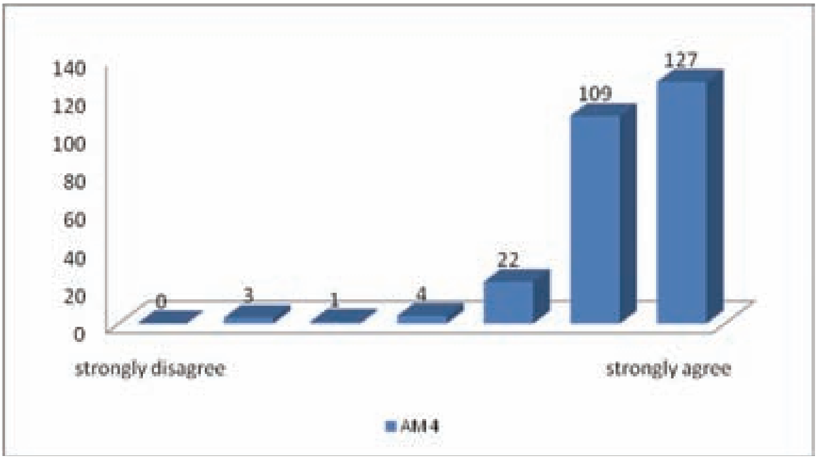

Figure 5.32: Answers to "I give customers adequate information about the financial products so that they are able to make a good decision"

Figure 5.32 suggests that the overwhelming majority of advisors believe that they give customers adequate information about the financial products so that they are able to make a good decision. Age, education and years of experience do not play an important role.

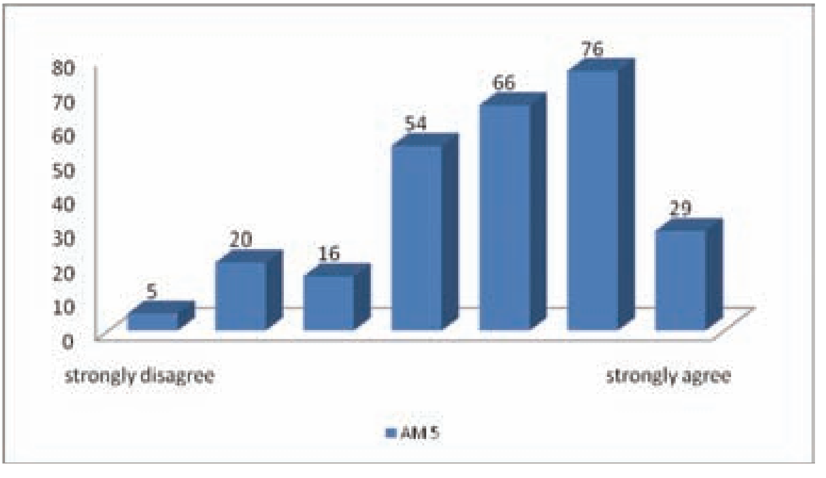

Figure 5.33: Answers to "Mandatory information has a positive influence on my job"

Figure 5.33 shows that more than 64% of the respondents agree with the statement that mandatory information (due to WFT) gives a positive influence on their job. Age, education and years of experience do not play an important role.

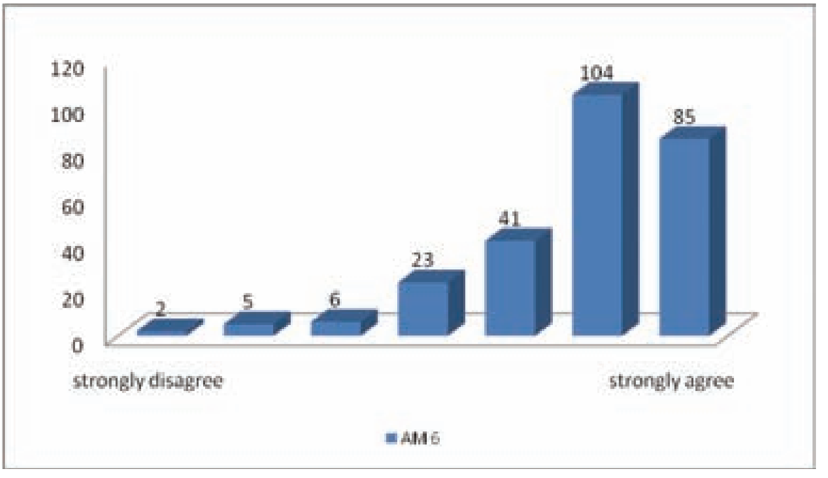

Figure 5.34: Answers to "I think a good advice is more important than striking a bargain"

More than 86% of the advisors think that good advice for a customer is more important than striking a bargain, as can be learnt from Figure 5.34.

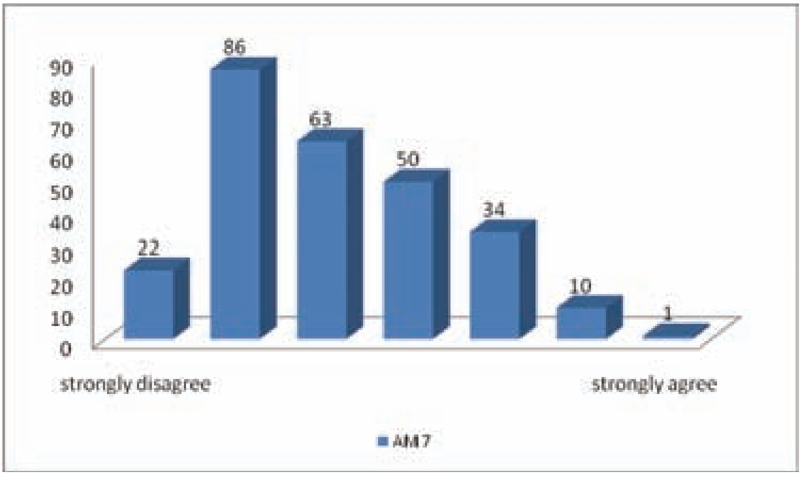

Figure 5.35: Answers to "The customer believes that experiences of other people are more important than my advice"

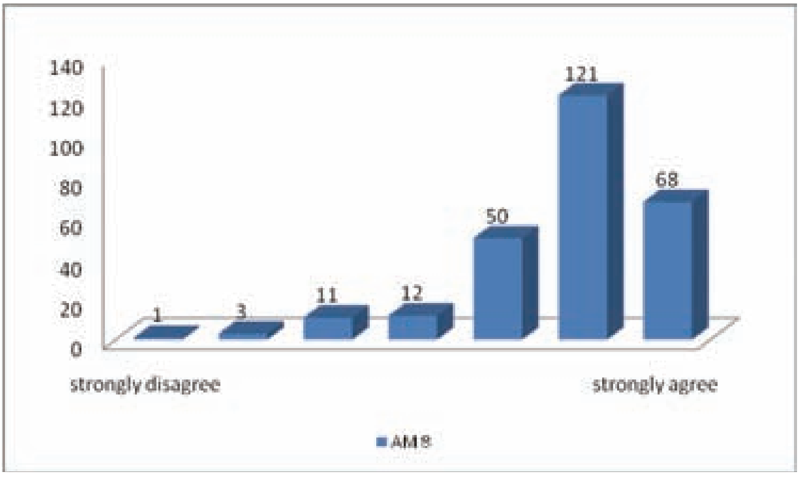

Figure 5.36: Answers to "A customer will come back to me for new advice when I gave him a good advice earlier"

Figure 5.35 shows that more than 64% of the respondents seem convinced that the influence of the personal network of the customer is less important than is the advice of the advisor. The group of advisors with more than 20 years of experience is most convinced.

Figure 5.36 give the results for statement AM8. Almost 6% of the respondents disagree with this statement. Hence, customers are believed to return a second time for new advice, after having received a good advice earlier. Age, eduation or years of experience of the advisors is not important.

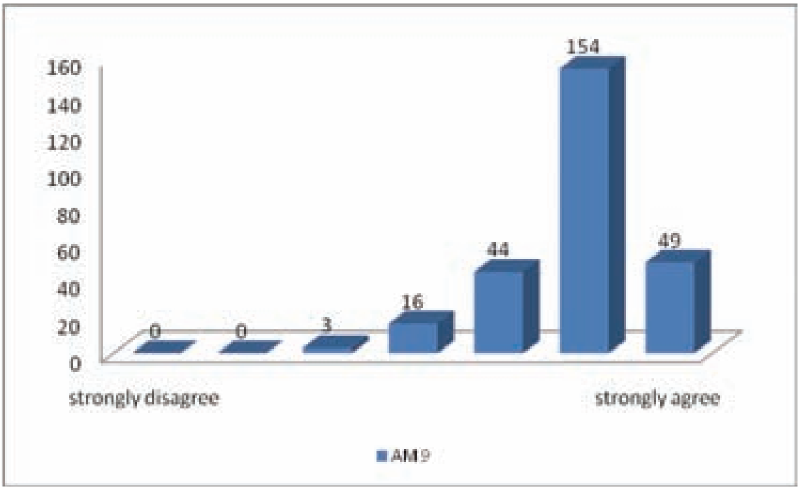

Figure 5.37: Answers to "Due to my advice, the customer is satisfied about the financial product he purchased"

Figure 5.37 shows that more than 92% of the respondents believe that the customer is satisfied about the financial product because of the advice.

Almost 61% of the respondents indicate that advice is not only about current financial consequences but also about future financial consequences, as shown in Figure 5.38. Years of experience or education do not seem to be important.

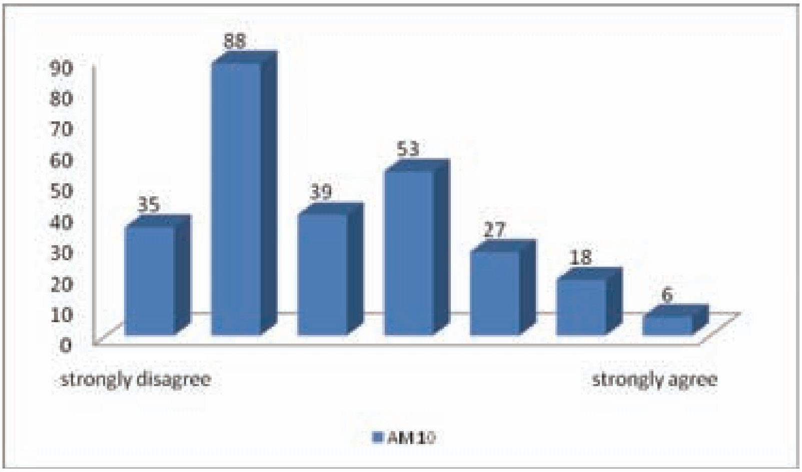

Figure 5.38: Answers to "My advice is about actual financial consequences and not so much less about future financial consequences"

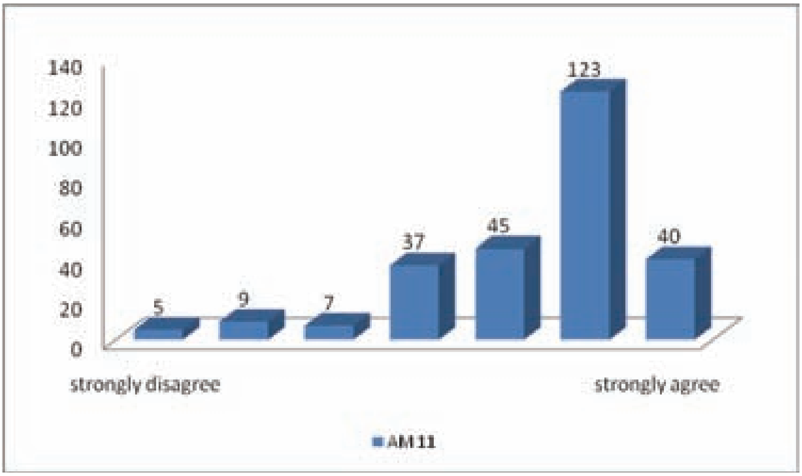

Figure 5.39: Answers to "A customer's financial possibilities are most important to me, even if the client thinks otherwise"

Figure 5.39 shows that more than 78% of the respondents agree with the statement that financial advice is based on the financial possibilities, even if the client thinks otherwise.

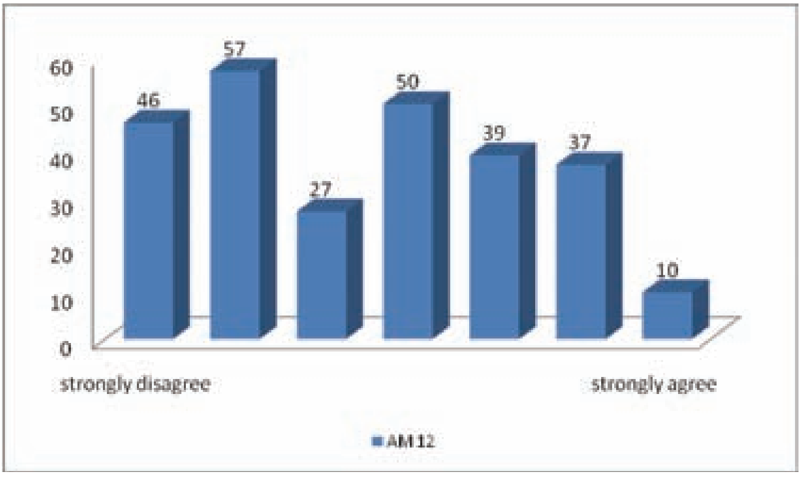

Figure 5.40: Answers to "I clearly inform my customers about what I earn with this advice"

Figure 5.40 is about disclosure and telling the customer about the earned wages or fee of the advice. More than 48% of the respondents disagree (which is a significant fraction) with this statement and do not tell the customer their earnings. More than 32% is transparent about wages. The years of experience seems to play a role. The group with most years of experience disagree the most with this statement.

Interestingly, statement AM13 concerns the advisors' opinion if the customer is interested in the earnings of the advisor. 56% of the advisors agree with the statement that the customer appears not to be interested in the earnings of his advice. Years of experience and education do not seem to be important.

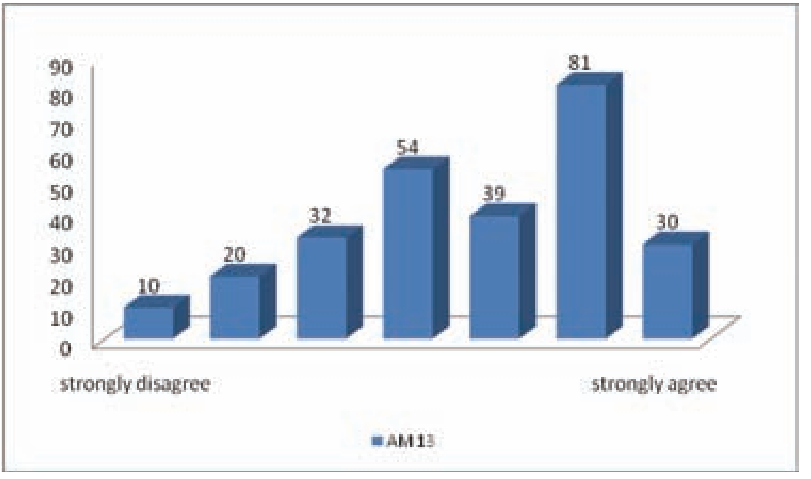

Figure 5.41: Answers to "My customer has no interest in what I earn with my advice"

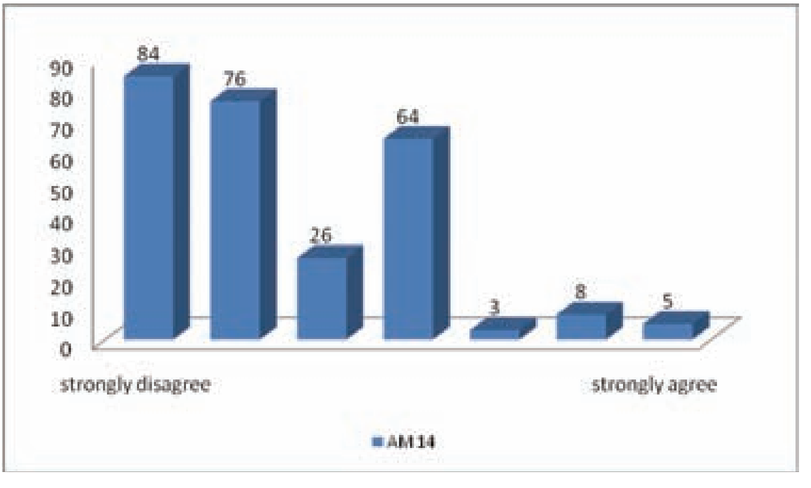

Figure 5.42: Answers to "My customer wants to receive an explicit invoice instead of paying my fee as part of the total sum"

Figure 5.42 concerns the situation whether the advisor thinks that the customer wants to receive a specified invoice for the financial advice or that the customer wants this to be integrated in the total sum. Almost 70% of the advisors disagree with this statement. There is no difference between the answers of the groups with few or many years of experience or level of education of the advisor.

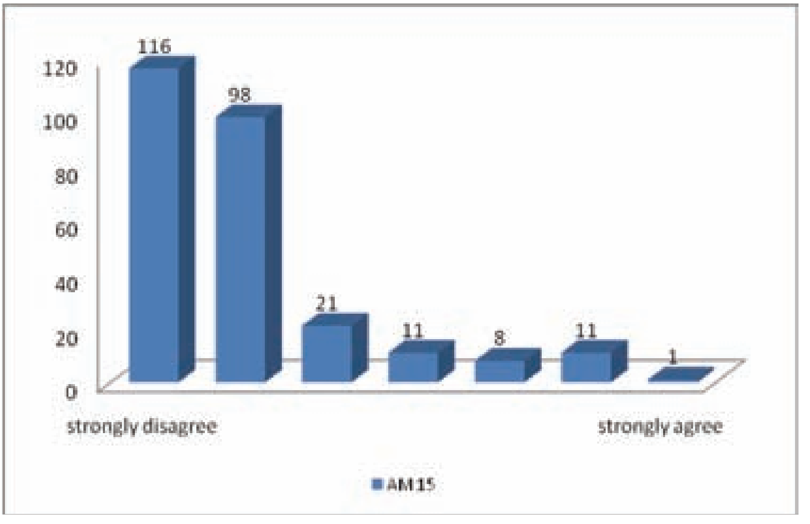

Figure 5.43: Answers to "I find customer contacts about the up-to-datedness of their financial choices a waste of time"

Periodic contacts with customers about the up-to-dateness of their financial choices is obligatory for financial companies. Figure 5.43 shows the opinions of the advisors on statement AM15, where we asked if the advisor thinks this contacts are a waste of time. More than 88% of the advisors disagrees with this statement. Years of experience or level of education seem not to be important.

Figure 5.44 shows that more than 97% of the advisors are convinced that their customers understand their advice.

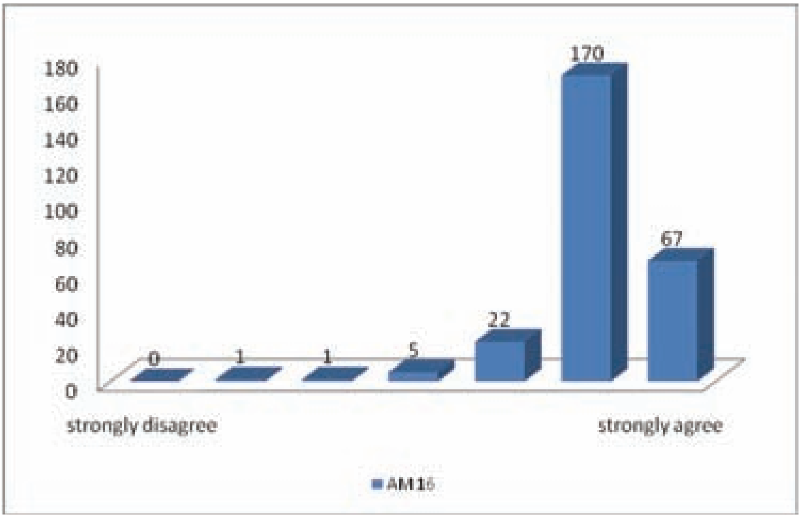

Figure 5.44: Answers to "My customer understands my advice"

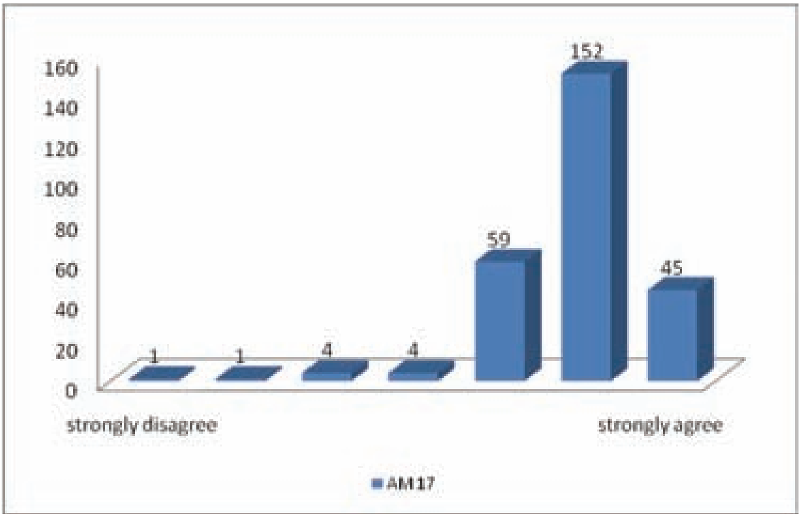

Figure 5.45: Answers to "My customers understand the consequences of their financial choices for their future financial situations"

Relatedly, more than 92% of the advisors believe that their customers understand the consequences of the financial choices for their future financial situation, see Figure 5.45.

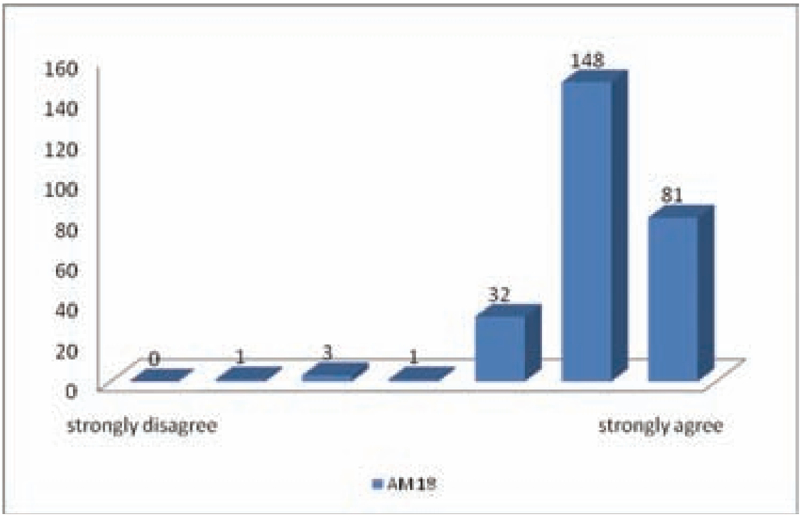

Figure 5.46: Answers to "My advice is understandable for the customer"

The histogram in Figure 5.46 indicates that more than 98% of the advisors agree with the statement that their advice is understandable for the customer.

In Figure 5.47 we give the results for statement AM19. Almost all advisors agree with the statement that their advice is more important for the customer's decision making than written information. Years of experience or education does not seem to be important.

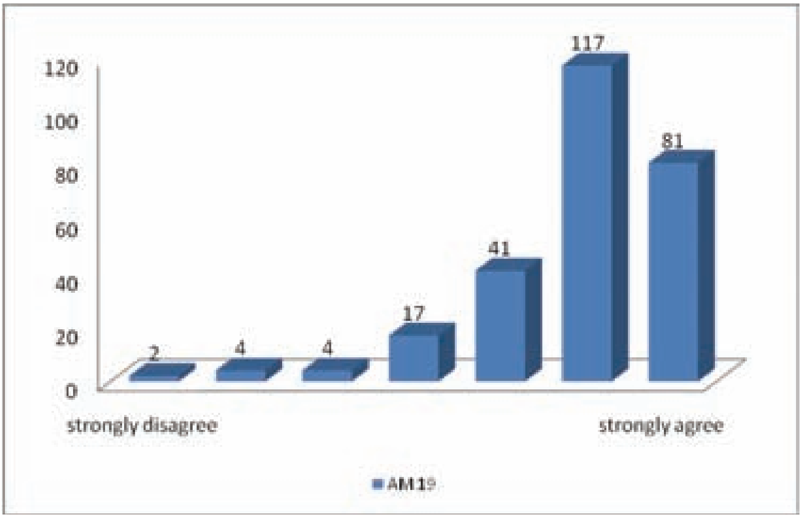

Figure 5.47: Answers to "My advice is more important for a customer's decision making than product information in brochures"

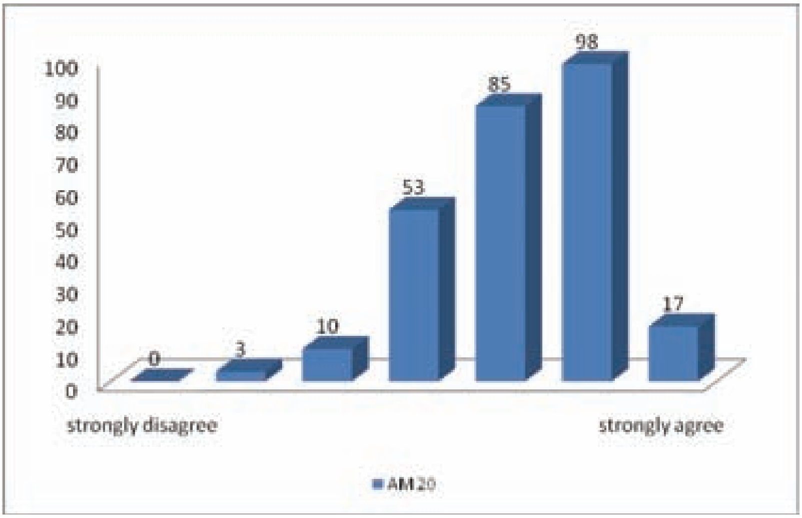

Figure 5.48: Answers to "My customers think about me as their problem solver"

Figure 5.48 suggests that more than 75% of the respondents agree with the statement that their customers think about their financial advisor as their problem solver for a financial question. The advisors between 31 - 50 years old are dominant in the group who not agree nor disagree.

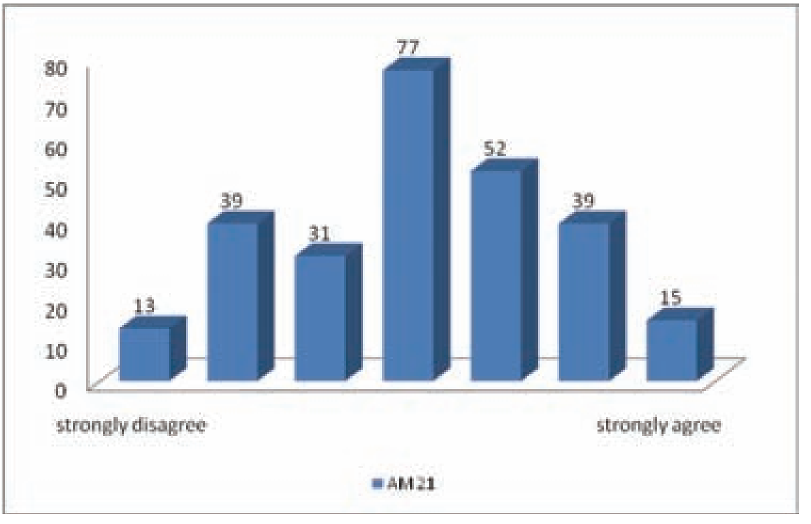

Figure 5.49: Answers to "A customer is alerted after reading a warning sentence in the prospectus of a loan"

Figure 5.49 shows that more than 31% of the advisors disagree with this statement. More than 39% of the respondents agree, while 29% of the respondents did not agree nor disagree. Table 5.5 indeed confirms that the mean answer is not significantly different from 4.

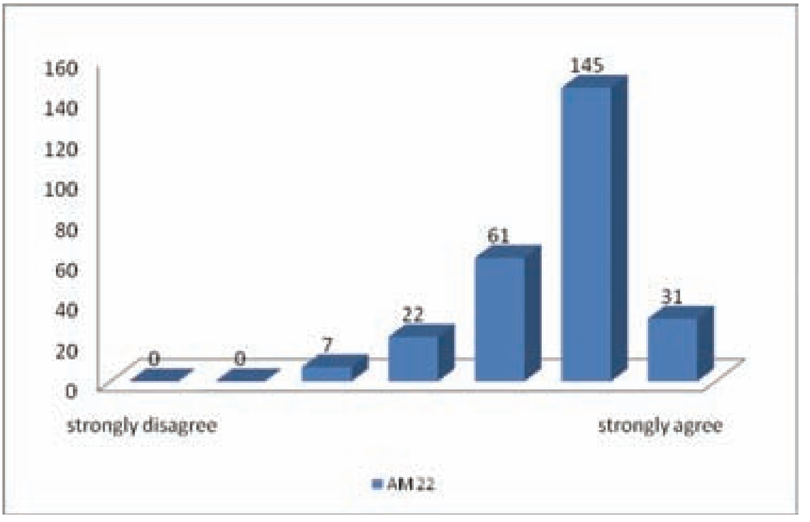

Figure 5.50: Answers to “My advice is crucial for customers’ decision making”

Figure 5.50 indicates that the advisors are pretty confident about their relevance to customers. More than 89% of them agree with the statement that their advice is crucial for customer’s decision making.

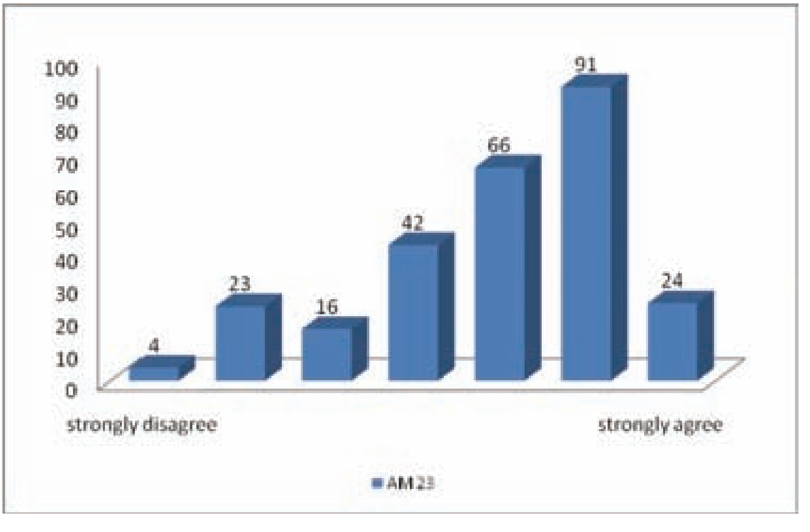

Figure 5.51: Answers to “My customers want to know the risks of the products”

Finally, Figure 5.51 shows that 68% of the advisors are convinced that the customers want to know the risks of the products advised. Years of experience and education does not seem to be important.

Table 5.5: Key statistics for the questions on advisor performance (the p-value concerns the test whether the mean equals 4)

Question	Mean	Median	P-value	Percentage <4	>4
AM1	6.29	6	0.000	1.13%	97.74%
AM2	5.73	6	0.000	1.88%	92.48%
AM3	3.83	4	0.065	42.86%	33.83%
AM4	6.31	6	0.000	1.50%	96.99%
AM5	4.88	5	0.000	15.41%	64.29%
AM6	5.81	6	0.000	4.89%	86.47%
AM7	3.08	3	0.000	64.29%	16.92%
AM8	5.79	6	0.000	5.64%	89.85%
AM9	5.86	6	0.000	1.30%	92.86%
AM10	3.10	3	0.000	60.90%	19.17%
AM11	5.39	6	0.000	7.89%	78.20%
AM12	3.49	4	0.000	48.87%	32.33%
AM13	4.71	5	0.000	23.31%	56.39%
AM14	2.51	2	0.000	69.92%	6.02%
AM15	2.00	2	0.000	88.35%	7.52%
AM16	6.11	6	0.000	0.75%	97.37%
AM17	5.84	6	0.000	2.26%	96.24%
AM18	6.13	6	0.000	1.50%	98.12%
AM19	5.88	6	0.000	3.76%	89.85%
AM20	5.19	5	0.000	4.89%	75.19%
AM21	4.10	4	0.289	31.20%	39.85%
AM22	5.64	6	0.000	2.63%	89.10%
AM23	4.92	5	0.000	16.17%	68.05%

Own perceived quality by the advisors (AQ)

Next, we ask five question about the own perceived quality of the advisors.

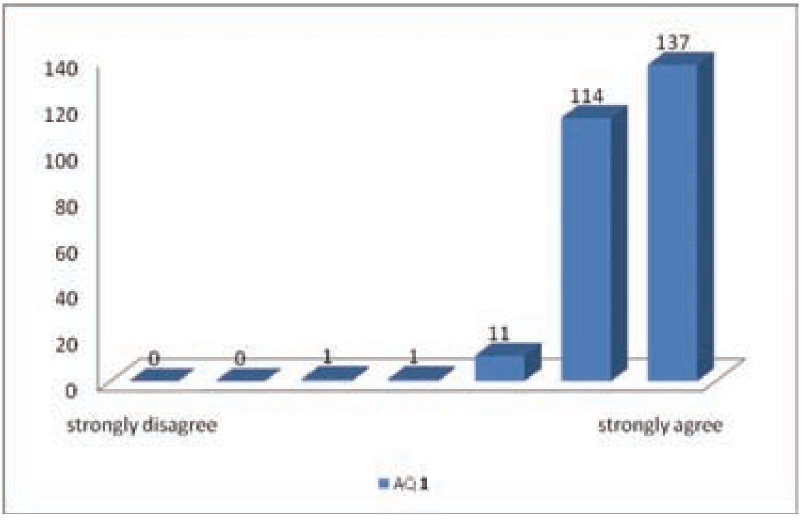

Figure 5.52: Answers to "I have sufficient knowledge for my advice"

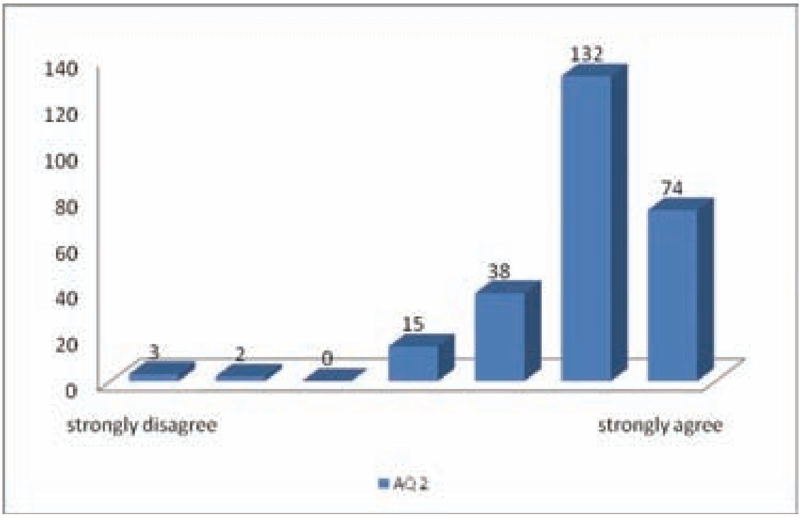

Figure 5.53: Answers to "I have creative solutions for my advice"

Figure 5.52 demonstrates that the advisors are quite confident about their own capabilities as more than 99% of the advisors agree with the statement that they have sufficient knowledge for their advice. In addition, Figure 5.53 amplifies this as more than 92% of the respondents agree with the statement that their advice consists of creative solutions.

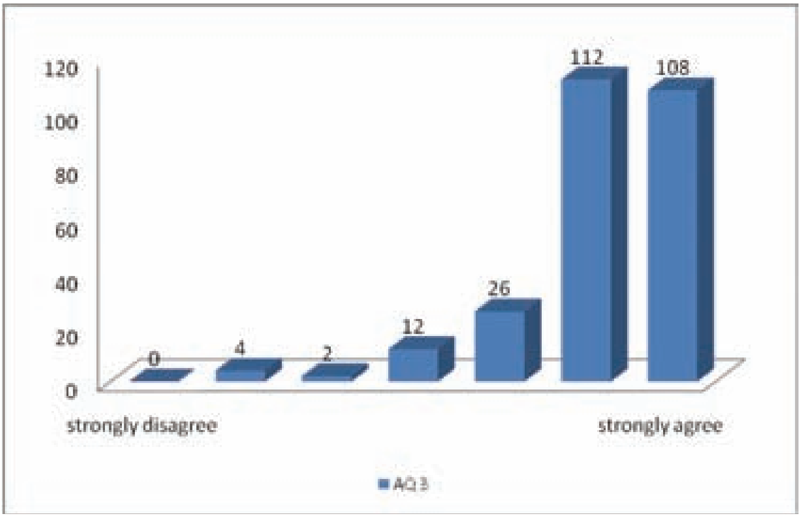

Figure 5.54: Answers to "I give proper advice"

Moreover, more than 84 % of the respondents agree with the statement that they give prover advice, see Figure 5.54.

Figure 5.55 shows that more than 85% of the advisors agree with the statement that they are accessible for their client.

Finally, Figure 5.56 shows the results of statement AQ5. The mean is significantly different from 4, see Table 5.6. More than 52% of the respondents agree with this statement that the fee for advice is correct. However, and interestingly, more than 42% of the respondents do not agree nor disagree with this statement.

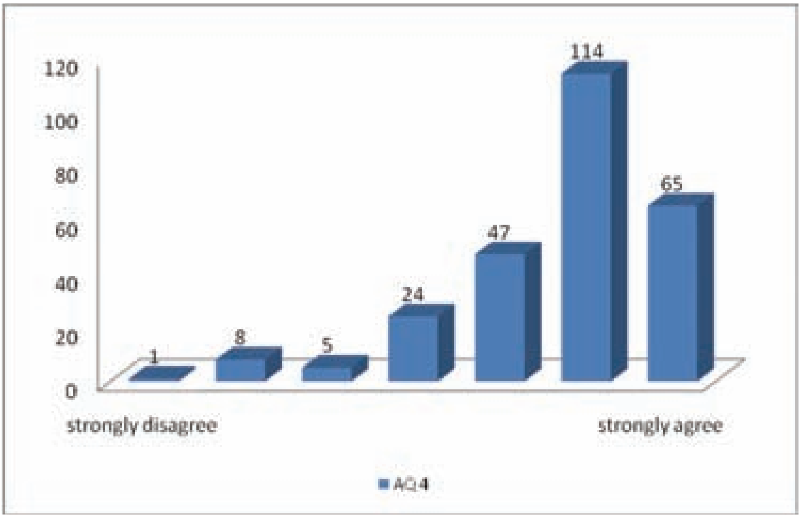

Figure 5.55: Answers to "I am accessible to my client"

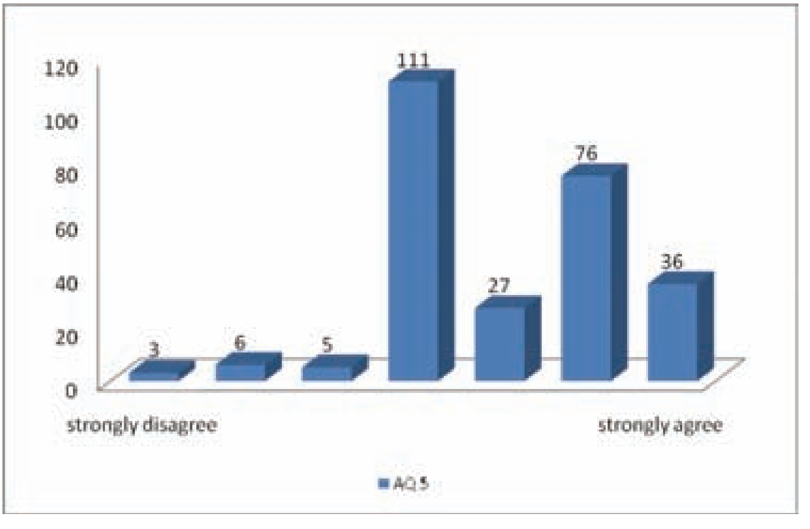

Figure 5.56: Answers to "My fee for advice is correct"

Table 5.6: Key statistics for the questions on advisors quality (the p-value concerns the test whether the mean equals 4)

Question	Mean	Median	P-value	Percentage	
				<4	>4
AQ1	6.46	7	0.000	0.38%	99.24%
AQ2	5.94	6	0.000	1.89%	92.42%
AQ3	6.14	6	0.000	2.27%	84.09%
AQ4	5.69	6	0.000	5.30%	85.61%
AQ5	4.99	5	0.000	5.30%	52.65%

Working conditions of advisors

We also asked the advisors about their working hours concerning sales activities and advice. The results are presented in the next three graphs. The first deals with their own working hours, and the second with those of their colleagues. The third question is about the optimal division of working hours.

Figure 5.57 suggests that 93 advisors give advice 75% of their time and 25% is for sales. Figure 5.58 shows that they believe their colleagues do the same. Interestingly, most advisors feel that 50/50 would be optimal.

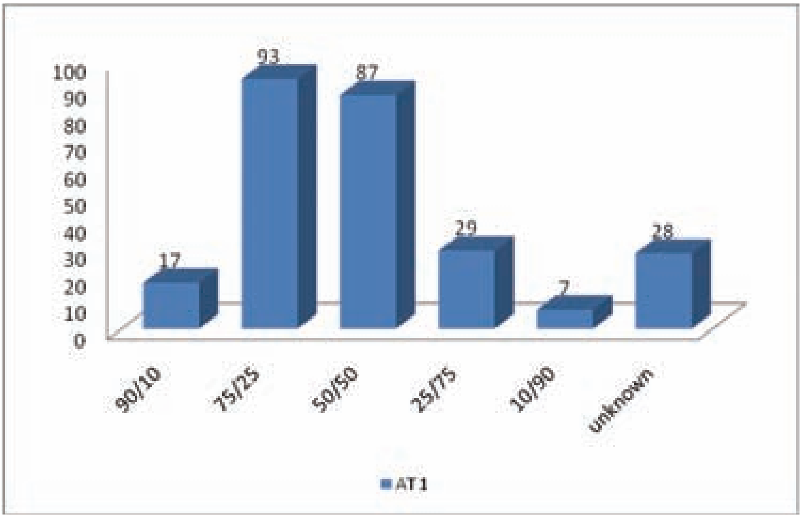

Figure 5.57: Answers to "Fraction of working hours concerning advice relative to sales"

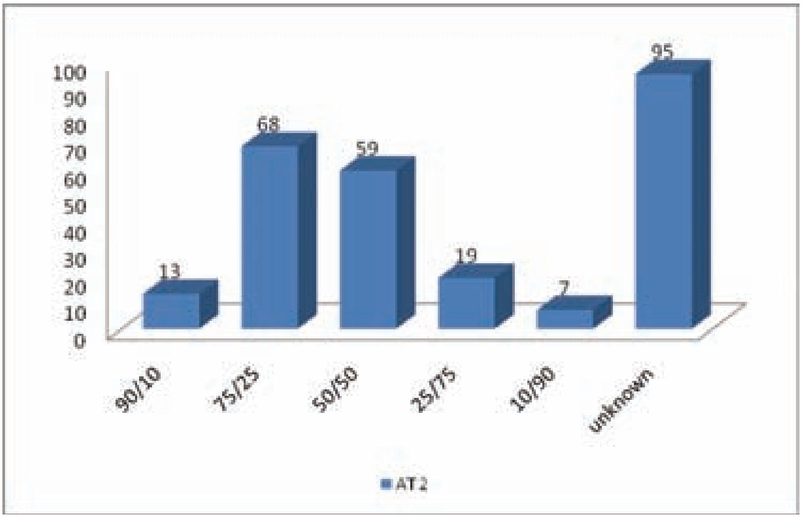

Figure 5.58: Answers to "How my colleagues allocate time to advice relative to sales"

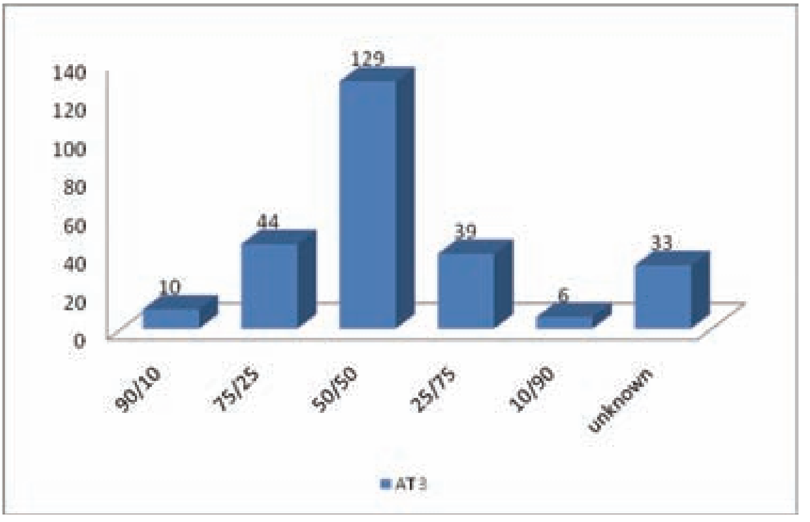

Figure 5.59: Answers to "Optimal division of time spent on advice and sales"

5.3.3 Personal face-to-face interviews with advisors

During the time of carrying out our internet survey, we also personally interviewed eight financial advisors. These advisors have many years of experience in providing customers with financial advice.

The issues discussed were the same themes as in the questionnaire. The first item was the duty of care, as this is an overarching issue for many relevant topics in legislation about consumer protection concerning financial advice and quality of advice of the advisors. All advisors think this focus on duty of care is important and that it is a way to load a customer relationship and to make the customer feel welcome at the company in the many years after the advice. Some advisors note that some customers do not want this much attention. Giving too much attention makes some customers to become insecure about the earlier advice.

The second issue of discussion was the preparation of the customer before he or she seeks advice. All advisors described two types of customers, that is, those who are well prepared and did some research before the advice, and those who did not. The prepared customers are more aware of the impact of the financial advice and are more critical about the given advice. They are also aware of the risks involved. The advisors indeed also describe customers who are not aware of their own financial situation and are not prepared. They all regard this as a difficult type of customer.

The advisors we interviewed all mention that today's customer is less self-confident than those a few years ago. Customers are aware of potential risks of financial decisions and many are suspicious about the advisor and his advice. This imposes some additional weight on the relationship between customer and advisor.

About the information needed to provide financial advice, all advisors mention unwillingness by some customers to provide the financial advisor with all relevant information. They notice that this is mainly because of not understanding why for example pension information is needed to give a full financial advice about mortgages.

About the advisors' fee, the interviewed advisors notice that the customer usually is not aware of the fee that the advisor receives for his advice. They mention that the customer does not ask for it and is also not aware that advice and duty of care cost money. The advisors also notice that the customers with insurance questions ask more support than customers who want to purchase banking products.

The customer receives much written information during the advising process. This can be brochures, financial leaflets, offers, legal information and so on. The advisors are aware that consumers do not read all the provided written information. Consumers do take notice of the discussed risks, but these are not decisive in their decision about purchasing a financial product, according to the advisors.

We also discussed the working hours of the financial advisors. All advisors prefer a fifty/fifty time management between giving advice and selling products. The advisors also made some concluding remarks in the sense that they experience some tension and stress between obtaining sales targets and giving advice.

In sum, these personal interviews emphasize the findings earlier in this chapter.

5.3.4 Feedback of the participating companies

Finally, our results of the survey were also discussed with the managers of companies participating in this research. These conversations were also part of a robustness check of the survey. In total we visited seven times the participating companies in the period May 2010 until April 2011. We discussed the results of the internet survey and the results of their (own) advisors and (own) customers. All the participating companies understood and agreed with the results and the opinions of their customers. They also recognize the opinion of their advisors which we received during the personal interviews. They all are searching for a way to handle new legislation and to incorporate the meaning of this legislation in every day practice. They are all willing to act responsibly, but they are searching for the right way to do so.

In the sessions we presented the results of the reactions of the customers and of the advisors. We grouped the questions according to the topics. We had interesting discussions about the differences in perception of the customers and the advisors about the same topics. Especially the difference in answers about the questions of quality of advice was worth discussing. For all these questions we found that the advisors were far more optimistic about how they think their customers would answer the questions than that the customer really did.

5.4 Conclusion

This chapter described the design of our survey for customers and their financial advisors and the detailed responses to the range of questions. We added the outcomes of personal interviews with financial advisors and the feedback from the company's managers.

Although we were not able to collect data for each pair of advisor and customer, we believe that average scores are already quite interesting. It appears that the customers seem to have a rather positive opinion about their financial advisors. They are not very demanding in terms of the size of the fee. The financial advisors seem to be quite convinced about their behavior. They are convinced that they possess the knowledge to provide a customer with good financial advice.

In the next two chapters we will use the information in this chapter to test a few relevant hypotheses concerning the relationship between an advisor and an advicee.

Chapter 6:
Financial Advisor and the Customer: Expertise

Abstract

We address the relationship between a consumer, who intends to purchase a financial product, and a financial advisor, who gives advice and at the same time tries to sell that product. A particular feature of this relationship is that it may involve asymmetric information, where one of the two parties can feel to be better informed than the other on the various aspects of the product. Second, the advisor has two roles and that is giving advice and sales. The relationship is important for consumers as the impact of financial decisions on consumers' financial lives is substantial.

To characterize the relationship in more detail we draw on two different literatures. In this chapter, we use the theory of Advise Giving and Taking (Jungermann, 1999) for decisions in financial services. It focuses on the differences in substantial expertise between the consultant and the client, and it zooms in on the interaction between consultants and clients. The current chapter focuses on the role of expertise of advisors and of customers. We put the hypotheses to a test where we use the data as described in Chapter 5. Not all data of that chapter will be used, as we only select those questions that are relevant for the hypotheses. A few of our main findings are the following.

We find that perceived and experienced advisors' expertise plays an important role in various dimensions of consumers' decision making. Higher educated customers are better informed about the product but feel less helped by the advisors. The novelty of our empirical work is that we test similar hypotheses for consumers and for advisors alike. Hence, we shall be able to compare their answers, and we observe salient asymmetries.

6.1 Introduction

The role of expertise is important in the relationship between an advisor and a customer. Financial products are usually complicated as they have many attributes and items, and one might expect that the advisor knows more about the specific features of these products. At the same time, the customer may also acquire information, for example through the internet, his or her social network, and past experience. Then still, it is an open question if the available information can be fully understood. Recall that we have seen in Chapter 3 that for example computations with percentages already constitute a rather difficult task.

When an advisor and a customer enter a relationship, they have prior expectations about the level of expertise of their counterpart. It is now of interest to see if the expectations match, and whether there are any other variables that mediate these expectations. Indeed, the financial products are usually such that the help of a financial advisor is required. In turn, the advisor wants to sell the product, so he is also interested in a high-level relationship which may lead to further calls for advice in the future.

Another feature that characterizes the relationship between a financial advisor and a customer concerns various legal issues. In many countries there are legal constraints that should make the relationship between the two more transparent. In fact, financial products, like pharmaceutical products, usually come with a prescription for its use and a description of potential side effects. Also in the Netherlands, there is law on financial services (the "Wet Financiële Dienstverlening (WFD), later called "Wet Financieel Toezicht (WFT)). This legislation has been introduced to protect customers against inappropriate financial products and it aims at more transparency of financial products. In this way consumers will receive more information about products and thus should be able to make better decisions. This law affects providers of financial products, because they have to provide customers with clear and understandable information, like the Financial Information Leaflet (Financiële Bijsluiter, FB). Providers of financial products also have to provide the advisors of these products with this information, when these financial advisors work at a financial institutions, investment firms and banks.

The primary objective of this chapter is to study the relationship between the financial advisor and the customer, where we focus on (perceived) expertise of the two counterparts. To characterize the relationship in more detail, and to formulate testable hypotheses, we draw on related studies. We use the theory of Advise Giving and Taking (Jungermann, 1999) for decisions concerning financial services. It focuses on the differences in content-related expertise between the consultant and the client, and it zooms in on the interaction between consultants and clients. Oehler and Kohlert (2009) tested this theory and these authors report evidence of information and interest asymmetry between financial advisors and their clients, where these asymmetries have an effect on the (perceived) quality of advice. We draw on these and related studies when putting forward a set of testable hypotheses. In this chapter we limit ourselves to the role of expertise of advisors and of customers. In the next chapter various qualitative aspects of the relationship will be addressed.

The outline of this chapter is as follows. In the next section we discuss the literature on expertise in a relationship. In Section 6.3 we put forward our hypotheses. In 6.4 we discuss the empirical results, and in Section 6.5 we give a summary of the main findings.

6.2 Literature

Consumers of financial products have to make many decisions in a short period of time. They have to incorporate new information, and they face choices with various consequences for their current and future financial situation. Therefore, many consumers resort to financial advisors.

The general topic of decision making has been and still is a key topic in many studies and journals. Decision making involves various steps, which should end with choosing the overall preferred choice option. Simon (1955, 1957, and 1992) describes several stages of decision making in case of so-called Rational Decision Making. First, an individual gathers information about each of the choice alternatives. Next, an individual has to design a choice rule with which the best option can be selected. Finally, an individual makes the final choice. These stages assume an "approximate" rationality, as the individuals have only access to limited information and usually do not have full information about all aspects of the choice alternatives. Simon introduced this concept as “bounded rationality” (Simon 1956, 1957), that is, the rationality of individuals is bounded or limited because of the information they have, the cognitive limitations they face, and because of the time available to make decisions. Simon (1957) argues that most individuals are only partly rational in their decision making process, also as they limit the number of alternatives options they want to choose from, both due to time and resources constraints. Simon also suggests that individuals use heuristics to make decisions, in order to reduce the complexity of the choice process when calculating the utilities of the offered alternatives.

An interesting feature of decisions concerning economic problems is the probability that a choice option occurs. For example, when a consumer makes a choice amongst various types of mobile phones, then that is a different choice situation than when an individual has to evaluate financial products with returns that depend on the future behavior of, say, the stock market. Tversky and Kahneman (1974) argue “that people rely on a limited number of heuristic principles which reduce the complex tasks of assessing probabilities and predicting values to simpler judgmental operations”. They claim that these heuristics can be useful but the authors also show that sometimes these heuristics may lead to systematic errors.

Tversky and Kahneman (1974) present three heuristics which individuals typically use to assess and evaluate probabilities. The first heuristic is called representativeness, where individuals choose options which resemble the familiar options. Judgment of probability along this heuristic can lead to serious errors because similarity is not affected by the same factors which affect the probabilities. The second heuristic is availability. The problem with this heuristic is that probabilities are associated with choice options that come to mind and hence unconsidered alternatives are neglected. The third heuristic, which may lead to bias in the choice process, concerns adjustment and anchoring. .

In economic decision making, individuals have to make decisions under risk and uncertainty. In their Nobel Prize winning article, Kahneman and Tversky (1979) address the choice between risky options. They develop the so-called prospect theory, where they describe the process of decision making under risk. Interestingly, the role of an advisor was not addressed in their study.

When purchasing a financial product, most individuals seek advice from a financial advisor who for example might help with selecting various alternatives to be included in the consideration set of the customer. Such advice can be given by a person, but it may also be that information is found by internet-based search routines. In our study, we assume that an individual can consult the internet, but in the end still seeks contact with an actual person for advice.

Akerlof (1970) is a seminal article on the relationship between advisors and customers. He postulates that advisors have more knowledge about the products and about aspects of their advice than that their customers do. He illustrates this phenomenon of asymmetric information to the case of second-hand automobiles, but it is easily appreciated that the same results carry over to the market of financial products. Financial advisors might have more knowledge of financial products than their customers can and will have.

Financial products are typically purchased after financial advice has been acquired. After having received financial advice, individuals are presumed to be able to make "informed rational decisions". Jungermann (1999) argues that this particularly holds for "dyadic decisions", which are decisions of advisees after obtaining advice with a financial advisor, and which are examples of complex personal decision problems. Suggesting that standard decision theory does not fit, Jungermann proposes an alternative approach to analyzing and aiding decision making, where he draws on concepts different from the traditional expected utility approach. Key players in his case of dyadic decisions are the consultant (advisor) and the client. He defines consultant as the "expert" and he uses client as "the affected layperson", who in this case is the consumer of a financial product.

In essence, Jungermann (1999) puts forward the notion of "informed rational decisions" or "informed decision making" and with that the assumption that "people want to make their own choices and that people know better than others what is good for themselves". Individuals are able to make their choices autonomously and rationally, and this seems in contrast to the theory of Tversky and Kahneman (1974) who postulate that consumers face biases in their decision making due to the fact that they use heuristics. However, Jungermann (1999) argues that "autonomy" and "rationality" are just illusions, or hopes, or ideals. He states that "clients have to make their decisions in a certain social setting, where they interact with someone who is an expert in the subject matter and where they discuss such matters" (Jungermann, 1999, p.2). And, clients face much "new, unfamiliar, complex and confusing information" (Jungermann, 1999, p.2).

Jungermann (1999) further argues that for decisions concerning financial products or medical treatment there are various arguments against applying standard decision analysis tools. The first argument concerns the potential fact that the range and time horizon of events is unlimited, where quantification of relevant information is vague and hypothesizing potential outcomes and utilities is difficult. A second argument is that information is of a probabilistic nature. A third argument is that clients have no relevant reference framework because they have to act in yet unfamiliar situations. Consumers face unique problems and they do not have factual knowledge. Finally, decision analysis does not incorporate the fact that the decision process itself can have an effect on the outcome of the decision.

Jungermann (1999) therefore proposes an alternative for this decision making analysis in case of financial products, which he calls Advice Giving and Taking Model (AGT model). In this approach he recognizes the fact that in dyadic situations, like financial advice, "the decision makers are neither expert in the subject matter nor are they experts in the decision making procedures. As a result, they do not primarily determine the decision. Such clients understandably and justifiably expect and get a substantial recommendation from the consultant who thus represents the real locus of the decision." (Jungermann, 1999, p 4). Both clients and consultants (like customers and financial advisors) are aware of their different levels of expertise. They share the same goal of their meeting, that is, advisors are willing to give advice because advisees expect them to do so. The expert-consultant and the layperson-client both face different roles in this process.

The AGT model contains four steps. The first step is the description of the problem, or, as Jungermann calls it, the elicitation of knowledge. If clients are not familiar with the problem for which they need advice, then confusion begins with the first step. More factual information can create even more confusion. At this stage the advisor and advisee already face an asymmetry in information. One interesting aspect is the client's attitude towards risk. If all is well, advisors reveal that "they know more about the clients' conditions and values than the clients themselves knew before the meeting". (Jungermann, 1999, p 5).

The second step in the AGT model is the identification by the consultant of several options by a so-called categorized-and-matching strategy. Consultants use the information gathered to propose these options. Jungermann postulates that consultants will try to identify a single option only. If the advisor sees several options, (s)he will pick those that have proven most successful in the past. Furthermore he postulates that for experienced consultants it will take only little time to find an option while for lesser experienced advisors it will take more.

The third step in the AGT model involves the consultant to offer the identified option(s). In this stage the advisor only presents the output of his or her search, and not the road that led to the recommendation. Advisors will explain and justify the recommendations, and give arguments in favor of the recommendation.

The fourth and final step involves the advisee who evaluates the advice and decides to accept or not. According to the AGT model, a customer does not choose from several options or advised options with different uncertainties, but the customer only decides to reject or accept recommended options.

Jungermann (1999) further argues that an implication of the AGT model is that the behavior of customers cannot only be explained by their evaluations of the options, as in fact acceptance or rejection can also be derived from other motivations. Examples of such motivations are confidence and trust in the advisor.

These latter factors also have an impact on the perceived quality of the relationship between a financial consultant and a customer. Oehler and Kohlert (2009) used the AGT model to show that this satisfaction of clients may indeed have little to do with the quality of the factual information exchange between clients and advisors but more with qualitative factors like friendliness and appearance of the advisor.

Oehler and Kohlert (2009) describe in their study that the legal framework of protection of customers of financial advice apparently does not work in Germany. The demand for competent and comprehensive financial advice has grown because of changes in legislation but also changes in wealth and disposable income, and even the presence of limited financial literacy. The authors discuss the discrepancy between the low quality of financial advice offered to customers and the high quality of financial advice German citizens apparently demand, which in turn emphasizes the importance of the advice giving and taking context as discussed in Jungermann (1999).

Oehler and Kohlert (2009) claim that, due to the information asymmetry across the client and financial advisor, only a few clients, who are those with high financial knowledge, shall be able to evaluate the quality of the financial advice. The majority of clients, however, does not have these skills and must rely on other qualities of advice. Further, they recognize an interest asymmetry between the client and the financial advisor. Only in the case of an advisor who negatively exploits the situation, in combination with asymmetry of information, customers face the risk of receiving poor advice. However, in case actual service and advice giving is offered free of charge and then cross-subsidized by provisions and fees resulting from the sales, advisors find themselves under pressure to sell their products as efficient as possible. They thus are confronted with the market's self-healing power to prevent bad advice, additional to what can be achieved by regulations.

When evaluating Jungermann's (1999) AGT model, Oehler and Kohlert (2009) argue that clients face a risk of receiving product recommendations which are not suitable for the client but are only in the interest of, say, the bank of the advisor. The clients' ability to evaluate the offered solutions or recommendations thus depends on his or her financial knowledge. They also argue that the lower the quality of this financial knowledge, the more the client shall trust the advisor (Sniezek and van Swol, 2001) and the higher the probability that the recommendation of the financial advisor is followed (Harvey and Fisher, 1997). Recommendations are usually given at the end of the advising session, when the chance of information overload is high.

Oehler and Kohlert (2009) conclude their study with the statement that "neither markets' self-healing power nor the regulatory framework can do what they are supposed to do" (ibid, p. 110). Advisors still have a large freedom in the way they give advice to customers. And, customers with the least financial knowledge suffer most from potential low quality of financial advice.

6.3 Hypotheses

Based on the above literature, we distinguish two distinct participants in the advising process concerning financial products. The first is the financial advisor, who has expertise in and experience with the products, and also has expertise in advising and sales of these products. The second is the customer, who seeks advice for a financial issue, like a mortgage or a pension plan, and who may want to purchase a product that fulfils the financial needs.

The literature assigns an important role to the concept of expertise in the advising process and in the (perceived) quality of advice. We define that an individual has expertise if he or she shows great skills, knowledge and experience in a certain field of interest. In this chapter we address the expertise of the advisor and the expertise of the customer. In this section we first put forward a range of hypotheses on expertise, where we first consider the expertise of the advisor and then that of the customer. In the next section we will put these hypotheses to a test, where we rely on the empirical results in Chapter 5.

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6.3.1 The advisor has expertise

Jungermann (1999) introduced his Advice Giving and Taking theory because customers have to make individual decisions following some kind of consultation. Traditional decision making theory does not include that advice-giving element. In contrast, the AGT theory does cover the potential differences between the relevant expertise of customers and the financial advisors, where the level of education can be a mediator. Oehler and Kohlert (2009) document evidence that higher educated individuals receive better advice. These authors further suggest that the fact that higher educated individuals receive better financial advice than people with less education makes a strong appeal on the advisors' expertise. Better informed individuals demand better advice.

It is thus important that the financial advisor is aware of the fact that a higher educated customer is better prepared. During the advising process the advisor provides the customer with much information, which in many cases shall be mostly new information for the customer. Better educated customers are better able to digest such new information, as better educated customers will enter a dialogue with an advisor being better prepared. Before we turn to the education level, we first put forward the following hypothesis:

Hypothesis 6.1: *A financial advisor assumes that a customer who seeks advice is prepared.*

Akerlof (1970) argues that customers enter the dialogue with an advisor with high expectations. Jungermann (1999) and Oehler and Kohlert (2009) present similar situations concerning financial products. Customers expect to become well informed and they are also prepared to make a final decision. We thus postulate:

<u>Hypothesis 6.2</u>: *Individuals have high expectations when they ask for financial advice.*

Jungermann (1999) and Oehler and Kohlert (2009) document that the customers may have consulted written information themselves, but then still, the perceived expertise of the advisor in crucial for a consumer's decision making. According to these results, we also hypothesize:

<u>Hypothesis 6.3</u>: *The advisor's expertise plays a more important role in a consumer's decision making than written information*.

6.3.2 The customer has expertise

According to the Advice Giving and Taking theory, the expertise of a customer is important for his decision making. When preparing to receive a financial advice, customers have several opportunities to gain information. Various internet sites can be consulted which contain general information about the attributes and items of financial products and about the suppliers of these products. Furthermore, consumers can gain information from other individuals and experiences can be shared. These days, recommendations via social media are also perceived as useful. Finally, some individuals will also consult other people who already have experience with the advice process. In sum, there are various ways for individuals to collect and evaluate information in order to build a level of expertise prior to entering the dialogue with a financial advisor.

When an individual enters a meeting with an advisor, he or she shall have prepared the meeting according to their own skills and abilities. It seems unlikely that an individual will have a dialogue with an advisor if he or she will not be able to understand and appreciate the choice options. At least, each individual should feel confident enough, that is, if asked, individuals would claim that they are well prepared and that they understand the problem at hand, whether this is true or not. Hence, we postulate:

<u>Hypothesis 6.4</u>: *Individuals are self-confident in that they understand the relevant and available information for the financial issue at hand.*

Further to Hypothesis 6.1, we postulate that:

<u>Hypothesis 6.5</u>: *A higher educated customer feels better prepared.*

Another key aspect of the AGT theory is that individuals do not seek financial advice very often. In contrast to many products that consumers purchase in their lives, like products that are purchased on a daily basis (bread), or other products less frequently (TV sets), a mortgage load may be acquired perhaps only once or twice in a lifetime. Jungermann (1999) posits that it is this low frequency that is one of the drivers of asking for advice. Indeed, one would not have many occasions in which a decision on a financial product can be dismissed and replaced by a new decision. Further, higher educated individuals, who are more self-conscious and self-reflective, would be more aware of the potentially long-lasting consequences of a decision and hence they are inclined to be better prepared. Hence, we postulate that:

<u>Hypothesis 6.6</u>: *A higher educated individual makes more effort to understand the various features of financial products.*

The classical decision making theory (Simon 1957) assumes that consumers will seek information, evaluate all relevant options and obtain all knowledge concerning the decision they have to make. In their search for information it is assumed that consumers also are aware of the short term and longer term consequences of all possible choices. The AGT model suggests a positive relationship between the level of education of a customer and his or her expertise. As we have defined expertise in terms of past and present knowledge, it is now also interesting to see how insights of consumer develop into the future. Are they able to think in terms of scenarios? And, can they imagine what the possible consequences would be of various choices that they can make? All this is perhaps difficult to answer, but we do postulate that:

Hypothesis 6.7: *Higher educated individuals are more aware of the potential consequences of their choices*.

Available, transparent and understandable information plays an important role for consumers to make it easier for them to make financial decisions. On the other hand, being well prepared and having obtained much information about financial products during the advising process, does contain a risk of feeling overwhelmed by the information. People can suffer from information overload. Such an overload, in turn, can make it more difficult to decide, and hence individuals would seek for the limits to the amounts of information and will try to select only the most relevant information (Simon, 1957).

During the decision making process, an individual has to evaluate the risks involved when making a decision. He or she has to evaluate the consequences of the choice. When there is more information available, then the evaluation of these consequences can be made easier, but when too much information is available, such an evaluation can become impossible (Iyengar and Lepper, 2000). Also, when more options are available, there will be a stronger preference for simple options (Iyengar and Kamenica, 2010). Thus we postulate:

Hypothesis 6.8: *Information overload leads to lesser abilities to evaluate the consequences of a decision.*

Following up on this hypothesis, we refer to Oehler and Kohlert (2009) in what they call the "Preference for self-protecting behavior". This says that when individuals feel that they are overloaded with information, through the internet, social media and various other sources, they have an increased inclination to ask for advice from an outside expert. Hence, our final hypothesis thus reads as:

Hypothesis 6.9: *A consumer who feels to be overloaded by information, needs more advice from a financial advisor.*

6.4 Empirical results

In this section we shall evaluate the nine hypotheses in the previous section against the data that we collected and already summarized in Chapter 5. Again, we first look at the hypotheses on the advisors and then we turn to the consumers. When available, the hypotheses will be tested using data for both advisors and customers. An overview of the hypotheses and the relevant questions of the survey is given in Appendix 6A and 6B.

6.4.1 The advisor has expertise

We test Hypothesis 6.1 using question AM3, which is a question to the advisors and it reads as “Customers are well prepared about which solutions and products they want before they come to me for advice”. Table 5.5 shows that the mean score is 3.83 while the median is 4, and that the mean is not significantly different from 4 (p-value is 0.065). So, we find no support for Hypothesis 6.1

A related question is AM16, that is, ”My customer understands my advice”. The mean score is 6.11 and this is significantly different from 4. Most advisors agree that their customers understand the recommendations and hence that they were well prepared.

In sum, the advisors are in doubt whether the customers are well prepared, but that does not seem to reduce the impression that customers do understand the outcome of the advice process.

To evaluate Hypothesis 6.2, we cannot ask for expectations as all surveyed individuals have already experience with financial advice, so we resort to some evaluations afterwards, as an indication of expectations. We consider CK2, which reads as “My advisor gives me the best possible solution to my financial question”. This statement receives substantial support from the interviewed customers with a significant mean value of 4.91. Further, CK5’s statement “After taken advice from my financial advisor I have full knowledge of the consequences of my choices” also receives full support from the customers as the mean value obtains a 5% significant value of 4.97.

The very notion that customers have high expectations from the advice process would likely be due to the fact that they themselves are not able to fully grasp the contents of the information brochures. CK19 deals with this as it states "I understand the information in a Financial Information leaflet". Interestingly, we find that the mean value of 3.96, which is not significantly different from 4. Combined with the significant mean of 4.42 for statement CK17, which says that "A verbal advice of the advisor is more important than written information for my choice of a financial product", we find that the high expectations of customers do not necessarily associate with the quality of the information on the written material. In fact, the answers to CK1 and CK2 suggest that the expectations are high simply because the advice is given by an advisor, who must have some experience and expertise, and CK9's answers strongly suggest that the expectations are high due to the fact that the customer felt well served the previous time, see also the answers of the advisors to "A customer will come back to be for new advice when I gave him good advice earlier" (AM8 with mean value 5.86)

Finally, Hypothesis 6.3 can be analyzed using a variety of statements in Chapter 5. CK17 provides the most direct support, with an average score of 4.42. Also the statement "My advisor has sufficient knowledge" (CQ1) attains a mean value of 5.27, and this exceeds 4. Other statements on quality, like CQ2 and CQ3, give support to the impression that the advisor create added value in the advice process.

The advisors themselves also feel that they have added value over written information as can be learned from AM19 ("My advice is more important for a customer's decision making than product information in brochures"), with no less than 89.85% of agreement responses. In sum, we find ample support for Hypothesis 6.3.

6.4.2 The customer has expertise

It is important for a customer to be well prepared and hence to have gathered and understood the appropriate information. The legislative framework in the Netherlands imposes an obligatory Financial Information Leaflet. The answers to CK18 ("I read the information on a Financial Information Leaflet") show that the mean value is 4.81, which is significant, but is also indicates that 21.41% of the customers do not read the leaflet. The subsequent question CK19 ("I understand the information on a Financial Information Leaflet") gives a mean answer of 3.96, which is not significantly different from 4. Also, 34.5% of the customers claim that they do not understand the Financial Leaflet. In sum, we are tempted to conclude that Hypothesis 6.4 should be rejected. Customers are not confident that they understand the written available materials.

To test Hypothesis 6.5, we have related the answers to CK3 to the education level of the customers. We regressed the scores of this question on (an intercept and) dummy variables for the education, and we find significant estimated parameters for HBO or WO education. The overall mean value of the answers to CK3 for not HBO or WO is 4.51, while for HBO it is 4.88 and for WO it is 5.05.

To test Hypothesis 6.6, we ran a similar regression where the dependent variable is the score on question CK22, and the same dummy variables are the explanatory variables. The estimated parameters for MO, MBO, HAVO, VWO, HBO and WO are all not significant. Hence, we observe no positive relationship between the level of education and reading the Financial Information Leaflet with a possible consequence that one hesitates due to a warning for loan advertisements. Higher educated people do not have stronger hesitation than people with lesser education. Hence, we do find evidence against Hypothesis 6.6.

In the relationship of customers' expertise and their level of education we examined if customers with higher education are more aware of the consequences of their choice. We asked if "After taken advice from my financial advisor I have full knowledge of the consequences of my choices" (CK5), and this obtained a mean value of 4.97. A similar regression, as before, gives significant parameters for the education level WO, which is negative. So, we not obtain any support for Hypothesis 6.7.

The two most interesting questions in Chapter 5 concern the Hypotheses 6.8 and 6.9. These days, due to legislation and due to many media and information channels, there is a serious chance of information overload, and this could prevent customers from making the proper choices, and therefore an increased wish to consult a financial advisor. We asked the customers whether they feel they do receive so much information about financial products that they cannot disentangle relevant from irrelevant information. Interestingly, the mean score of the answers to CK4 is 3.55, and this is significantly below 4. Hence, the customers do not think that they receive an overload of information. We checked if education plays a mediating role, but found no such impact.

We also test if “Experience with financial products by people near to me is as important as the financial advisor’s advice” (CK8). The significant mean value is 4.61, so other experiences are also important, or even more important. Therefore we can conclude that the experiences with financial products of people in a customer’s environment are equally important than financial advice from a professional. This in turn suggests that there is no support for Hypothesis 6.8, as customers can even handle additional information than that obtained from an advisor.

A test for Hypothesis 6.9 involves a regression of the answers to CK2 against an intercept and the answers to CK4. The relevant t-value is -0.448. A similar regression of CK1 against CK4 gives a similarly insignificant t-value of -0.064. In sum, we do not find support for Hypothesis 6.9.

6.4.3 Comparing advisors and customers

The previous two subsections dealt with the answers to the statements when posed to advisors and customers separately. In this subsection we will see if there are any significant differences across these two sets of respondents on questions that are broadly similar. The results appear in Table 6.1

Comparing the questions AM3 “Customers are well prepared about which solutions and product they want before they come to me for advice” and CK3 (“Before I see see my advisor for financial advice, I search for product information on the internet”), we get the impression that consumers feel better prepared than that the advisors think they are.

Comparing AM4 with CK4, we see that advisors feel that customers face an overload of information, while consumers significantly state that they disagree with that statement. Hence, advisors seem to feel themselves as more relevant than they perhaps are. This is reinforced by the answers to AM7 and CK8, where consumers indicate they learn more from relatives and friends than that advisors expect them to do.

The impact of long-term financial possibilities is not different across advisors and customers, while from comparing AM11 with CK12 we learn that advisors seem more concerned with the current financial possibilities of customers than the customers do themselves.

Finally, advisors are much more positive about their role and importance of their advice during the advising process. The difference across the means is no less than 1.464, which says that advisors agree (much) more with the statement that customers are more influenced by their advice than by the written information.

Table 6.1: Comparing the mean scores for advisors and for customers: Expertise

Type of expertise	Advisors	Customers	Difference	p-value
Information available AM3 versus CK3	3.83	4.51	-0.68	0.000
Information overload AM4 versus CK4	6.31	3.55	2.76	0.000
Information of relatives AM7 versus CK8	3.08	4.61	-1.53	0.000
Long term financial possibilities AM10 versus CK11	3.10	3.18	-0.08	0.549
Current financial possibilities AM11 versus CK12	5.39	3.59	1.80	0.000
Advice > written information AM19 versus CK17	5.88	4.42	1.46	0.000

6.5 Conclusion

In this chapter we reviewed the available literature on customers of financial products and their financial advisors. With the AGT model of Jungermann (1999) we postulated nine hypotheses concerning expertise. Expertise plays an important role in explaining various aspects of the relationship between the customer and the financial advisor.

The empirical results show some interesting conclusions. We find that advisors expect to encounter customers with high expectations and hence customers who are well prepared. We also find that the advisor's expertise is more important for customer's decision making than any written information, where the advisors believe this to be much more important than customers do.

About the customers' expertise we find that customers confidently claim to understand the available information. We also find evidence that a higher educated customer is better prepared and spends more effort to understand the various features of financial products. Not unexpectedly, we also document that customers with higher education are more aware of the future consequences of their choices. Education of the customer plays an important role in understanding the advice and financial information.

The amount of information received by customers also plays a role in customers' decision making. Customers do not agree that they receive an overload of information during the advising process, whereas advisors feel that customers do. In sum, we find quite some asymmetric perceptions by customers and advisors.

Appendix 6A: Hypotheses 'The advisor has expertise'

In this appendix we give an overview of the relevant questions in our survey, described in Chapter 5, to examine our hypotheses in 'the advisor has expertise'.

Hypothesis 6.1: A financial advisor assumes that a customer who seeks advice is prepared:

- AM3 "My customer has no interest in what I earn with my advice"
- AM16 "My customer understands my advice"

Hypothesis 6.2: Individuals have high expectations when they ask for financial advice:

- CK1 "I consult my financial advisor for a reliable advice"
- CK2 "My advisor gives me the best possible solution to my financial question"
- CK5 "After taken advice from my financial advisor I have full knowledge of the consequences of my choices"
- CK9 "When my financial advisor helped me well before, I will go for a consult the next time"
- CK17 "A verbal advice of the advisor is more important than written information for my choice of a financial product"
- CK19 "I understand the information on a Financial Information Leaflet"
- AM8 "A customer will come back to me for new advice when I gave him a god advice earlier"

Hypothesis 6.3: the advisor's expertise plays a more important role in a consumer's decision making than written information:

- CK17 "A verbal advice of the advisor is more important than written information for my choice of a financial product"
- CQ1 "My advisor has sufficient knowledge"

- CQ2 “My advisor provides me with creative solutions”
- CQ3 “My advisor gives me a proper advice”
- AM19 “My advice is more important for a customer’s decision making than product information in brochures”

Appendix 6B: Hypotheses 'The customer has expertise'

In this appendix we give an overview of the relevant questions in our survey, described in Chapter 5, to examine our hypotheses in 'The customer has expertise'.

Hypothesis 6.4: Individuals are self-confident in that they understand the relevant and available information for the financial issue at hand.

- CK18 "I read the information on a Financial Information Leaflet"
- CK19 "I understand the information on a Financial Information Leaflet"

Hypothesis 6.5: A higher educated customer feels better prepared.

- CK3 "Before I see my advisor for financial advice, I search for product information on the internet"
- Level of education of customer

Hypothesis 6.6: A higher educated individual makes more effort to understand the various features of financial products;

- CK22 "A warning for loan advertisement makes me hesitant"
- Level of education of customer

Hypothesis 6.7: Higher educated individuals are more aware of the potential consequences of their choices.

- CK5 "After taken advice from my financial advisor I have full knowledge of the consequences of my choices"
- Level of education of customer

Hypothesis 6.8: Information overload leads to lesser abilities to evaluate the consequences of a decision.

- CK4 “I receive so much information about financial products that I cannot disentangle relevant from irrelevant information”
- CK8 “Experience with financial products by people near to me is as important as the financial advisor’s advice”

Hypothesis 6.9: A consumer who feels to be overloaded by information, needs more advice from a financial advisor.

- CK1 “I consult my financial advisor for a reliable advice”
- CK2 “My advisor gives me the best possible solution to my financial questions”
- CK4 “I receive so much information about financial products that I cannot disentangle relevant from irrelevant information”
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Chapter 7:
Financial Advisor and the Customer: Relationship

Abstract

To characterize the relationship and satisfaction with the relationship we draw on two distinct literatures. First, as in Chapter 6, we rely on the theory of Advise Giving and Taking (Jungermann, 1999) for decisions in financial services. This theory addresses the differences in relevant expertise between the advisor and the advisee, and it zooms in on the interaction between the two. Second, we consider the consumer relationship marketing literature (Palmatier et al., 2006) which addresses relational mediators and the moderators on these mediators. We draw on both these literatures when we put forward a set of testable hypotheses, which we hold against part of the data summarized in Chapter 5.

One of our results is that trust increases with a frequent contact between the advisor and the customer and that customer loyalty is anyway rather high. Interestingly, and in contrast to expectations, the fee of the advisor does not play a role in consumers' decision making nor does it in perceptions of quality. Surprisingly, legally prescribed written information has no impact either. Word of mouth and a complete overview of financial opportunities have a positive influence on the perceived quality of consumers' decision making. Finally, we find that advisors are overconfident regarding their relevance for the relationship. We evaluate some of our findings with some recent advances in other literatures.

7.1 Introduction

In the previous chapter we discussed the importance of the expertise of a financial advisor and his or her customer. In this chapter we take another view by focusing on the relationship between the two players, where constructs as trust and satisfaction are key issues.

This chapter commences with a discussion of the relevant literature, where part of it will be used to put forward various hypotheses. Particular attention will be given to transparency and the disclosure of the advisor's fee, and their impact on trust and satisfaction. In the subsequent Section 7.3 we present our hypotheses based on this literature. In Section 7.4 we discuss our empirical results, where we evaluate the hypotheses using the data collected and summarized in Chapter 5. In Section 7.5 we review the main findings in this chapter.

7.2 Literature

This chapter deals with various qualitative aspects of the relationship between a financial advisor and the customer. The previous chapter dealt with expertise, where issues as asymmetric information (Akerlof, 1970) and search for information by a customer were analyzed. In this chapter we address qualitative aspects such a trust and satisfaction. For that reason, we shall revert to literature on relationship marketing, where such issues are central.

Financial advisors are usually the same individuals who try to sell financial products. Frequently, the advisors themselves work for a financial institution or a bank. These institutions benefit from a long-term relationship with customers so that they do not divert to a competitive firm and so that they can perhaps cross-sell other products in the future. The perceived quality of the financial advice thus becomes an important marketing instrument to gear a sound relationship with customers.

To analyze the long term relationship between financial advisors and customers we look at the Relationship Management literature. Palmatier et al. (2006) provide a systematic review and evaluation of the literature on relationship marketing (RM) where they address the various moderators of relationships between firms and customers. The authors give insights into which RM strategies are most effective for building long-lasting high quality customer relationships and which outcomes are most affected by RM. They also address the moderators that are most effective in influencing relationship outcomes and how an RM strategy can build on these moderators.

Palmatier et al. (2006) indicate that a customer relationship is two-sided and that both parties typically share the benefits of a strong relationship. Also, they note that some antecedents and outcomes may have differential effects according to the type of dependence between firm and customer. They distinguish three different theories. The first theory is the customer-focused theory, which aims to increase customer loyalty. The second theory is seller-focused, where seller expertise reflects the knowledge, experience, and overall competence of the seller. The third theory concerns the dyadic relational mediator. Customer- and seller-focus antecedents are meaningful from one side of the exchange dyad, but other antecedents require the active involvement of both partners in the relationship and are equally meaningful from both perspectives. The consequences of this dyadic mediator are that cooperation captures the level of coordinated and complementary actions between exchange partners in their efforts to achieve mutual goals. Trust and commitment between exchange partners are critical for such cooperation.

As relational mediators Palmatier et al. (2006) distinguish several items, such as commitment, trust, relationship satisfaction and relationship quality. We will also consider these items and we will operationalize them below. As antecedents the authors mention relationship benefits, a customer's dependence on seller, relationship investment, seller expertise, communication, similarity, relationship duration, interaction frequency and conflict. Finally, Palmatier et al. (2006) discuss the set of potential outcomes of the relationship like expectations of continuity, word of mouth, customer loyalty, seller objective performance and cooperation. The authors define trust as confidence in an exchange partner's reliability and integrity. And they define relationship satisfaction as a customer's affective or emotional state towards a relationship, where it is stressed that it reflects the customer's satisfaction with the relationship and not the customer's satisfaction with the overall outcome of the advice process.

For our research purposes it is important to consider the items of trust, relationship satisfaction, relationship investment and seller expertise (see Chapter 6). Also important are expectations of continuity of the relationship, which is important for the lifetime value of customers to the financial advisors, word of mouth and customer loyalty.

Beloucef et al. (2004) argue that trust, commitment and customer satisfaction are influencing the outcome of the relationship between an advisor and customer. In their study they find that service quality is a significantly important moderator. Twyman, et al. (2006), Doney and Cannon (1997), and Hibbard, et al. (2001) show that trust is an important factor and serves as a relationship mediator. Trustworthiness is important for the appreciation of (financial) advice, but also for returning a next time for obtaining new financial advice or perhaps alternative financial problems (cross selling). Trust is also mentioned as an important factor in the effective communication of risk, which, as we saw in Chapter 6, is a key aspect in the financial advice process.

De Wulf et al. (2001) conjecture that customer loyalty is an important factor for the outcome of a relationship process, and as such observed customer loyalty is an instrument to measure satisfaction of the relationship.

For many products (like durable consumer goods and various services), RM strategies are fully in the hand of firms and customers. It is worth to mention here that for financial products, at least in the Netherlands, there is legislation (like the WFT) that partly addresses RM issues. The WFT was introduced to prevent individuals from obtaining too many loans, more than they are able to pay back in time, and therefore too many debts (see the statistics in Chapter 2). Such legislation prescribes to suppliers of financial products to give detailed information about loans and complex financial products (like the one analyzed in Chapter 4). The WFT also prescribes how financial advisors should behave. For example, it is not allowed to make individuals to acquire a mortgage that exceeds 5 times their annual income. So, issues like disclosure (of advisors' fees), transparency and duty of care are not only features that are defined in the free marketplace, but they are also imposed by law.

In contrast to perhaps politicians' views, Oehler and Kohlert (2009) test the market of financial services and they postulate that the regulatory framework does not work in protecting customers of financial advice from getting bad advice. Cain et al. (2011) state that "disclosure is often proposed as a remedy for conflicts of interest, but it can backfire, hurting those whom it is intended to protect". These latter authors suggest that in specific domains, like financial services, the most common policy response to conflicts of interest is to disclose them. Supporters of disclosure supposedly argue that “transparency improves market efficiency, increases welfare, and protects the public by reducing information gaps between conflicted advisors and recipients of their advice” (ibid, pp 836-837)’. Cain et al. (2011) focus on realistic cases in which the quality and results of advice cannot be perfectly verified. Using four studies they examine the effects of disclosure and how it can enhance the discounting of conflicting advice. The authors conclude that disclosure is not a solution to the problem created by conflicts of interest. In fact, they show how disclosure can hurt just the people they aim to protect. In their recommendations, the authors include that “objectivity may be better: regulators should focus less on disclosing sources of bias and more on censuring that objective information reaches the audience, if not in lieu of biased information, at least directly alongside it.” (ibid p.851). Cain et al. (2011) believe that regulators “are attracted to disclosure if they see it as absolving them of responsibility for protecting consumers by ostensibly empowering consumers to protect themselves.” (ibid p. 850).

Leiser et al. (2011) examine a pension plan selection in Israel. In their experiments they also find paradoxical effects of disclosure. Their experiments show that their public is not financially literate (like many people are, see Chapter 3 of this thesis), and that the group faces uncertainty about their preferences of choice of pension plan. They also signal that disclosure causes some overreaction of the advised group, which is keen to make the best decision, but where the individuals do not trust the advisor and instead do the opposite than advised.

Earlier, Cude (2005) found evidence that, in the case of insurance disclosure, the customers’ understanding is limited and customers are not likely to read it. Day (1976) described the regulatory effects of disclosure, which is a transformation “from availability to awareness and comprehension” by the customer. He also found little effect on buyer behavior after giving the provided information on fees. Both the studies of Cude (2005) and Day (1976) do present evidence that the content and style of disclosures has impact on the willingness to read disclosures. Weil et al. (2006) argue that transparency measures and measures of disclosures are only effective when the output they provide ‘is embedded in everyday decision-making routines’ of both the users of information and the providers of the disclosure information. They call it the most important condition for the effectiveness of the transparency system. Finally, Li and Madarasz (2008) find that in fact nondisclosure can give a higher welfare for all participants.

7.3 Hypotheses

The financial advisor has expertise on the financial products and he of she also has experience with the advice process itself. However, an advisor usually does not inform how exactly he or she arrived at the final option that is presented to the customer. The customer only can accept or reject the option provided. The advisor has an interest in that the customer chooses this option, in particular as the advisor may also be the salesperson of that financial product. Therefore, investment in the relationship between advisor and advisee and the resultant level of satisfaction are important features.

To define satisfaction of a relation, most authors draw upon the relationship profitability model; see Storbacka et al. (1994), Barnes (1997), Crosby et al. (1990) and Verhoef (2003). This model is about the satisfaction of the consumer with the intention of the sellers to improve selling in the future. Note that this model does not address the satisfaction level of the advisor.

Similar to Chapter 6, we separately address the satisfaction of the customer and that of the advisors, where now the order is reversed. The next two subsections deal with the hypotheses.

7.3.1 The customer is satisfied with the relation

Advisors involved in the sales and advising process are, as the customer relationship literature says (Palmatier et al. 2006), playing the role of "relationship manager". The quality of the relationship between the advisor and the customer is important for customer satisfaction during the advising process and after purchasing the advised products. It is also important for customer satisfaction and new advice in the future. Future sales and advices opportunities depend mostly on relationship quality. Oehler and Kohlert (2009) found in their research that people who are better prepared and with higher education receive better financial advice, as we also have confirmed in Chapter 6. These authors also demonstrate that these individuals are more satisfied with the relationship. Hence we postulate the following Hypothesis:

Hypothesis 7.1: *Customers with more financial knowledge are more satisfied with the given advice.*

Crosby et al. (1990), among others, have shown that the frequency of contact between the customer and the advisor is important for consumer satisfaction with the relation. Customers who are more satisfied with the provided advice are more willing to come back another time for a new financial advice, possibly on a new financial product (cross selling). Following this, we put forward:

Hypothesis 7.2: *Customers are more loyal when they are more satisfied.*

One important factor for customers, and a key motivation to seek advisors' help in financial decision making, is that customers think that advisors understand financial products better than they do themselves. In other words, consumers expect advisors to have expertise, see Akerlof (1970) and Jungermann (1999), and it is this belief that makes customers to rely on their advice. This entails that at the entry level the consumers trust that advisors know what they do. We postulate the following Hypothesis:

Hypothesis 7.3: *The perceived expertise of advisors makes customers to rely on their advice.*

Transparency of information and disclosure of the advisor's are prominent themes in political discussion and changes in legislation. Regulators and various consumer organizations are convinced that advisors recommend financial products only for their own interest, that is, for their own fee .It is commonly believed that the disclosure of the fee makes consumers more aware of the true costs of the financial products. Also it is commonly believed that the advisors' fee plays an important role in consumers' decision making and that consumers should be able to choose an advisor with the lowest fee. As mentioned, Cain et al. (2011) and Leiser (2011) show that disclosure of the fee or costs of a financial product has, perhaps unexpected, contradictory effects. We follow these studies by postulating:

Hypothesis 7.4: *Information about the advisor's fee is of no importance to the customer.*

So far, we postulated our hypotheses about customers being satisfied with the relation with their financial advisor. In the next subsection we focus on how the advisor can be satisfied with the relation with the customer.

7.3.2 The advisor is satisfied with the relation

Salespeople and advisors perform the role of "relationship manager". Palmatier, et al. (2006) describe this role and they stress the importance of relationship management for the perceived quality of advice. Oehler and Kohlert (2009) also mention the relevance of a well-prepared advisor in the advising process, and we re-iterate this relevance for the satisfaction level of the advisor. These authors also state that a higher educated customer is prone to get better advice. Hence, the satisfaction level of the advisor (in part) depends on the level of preparation of customers, and we therefore postulate:

Hypothesis 7.5: *An advisor is more satisfied with a relation when potential customers are better prepared.*

The fee of an advisor is important element of the relationship between a financial and a customer. Policy makers who are in favor of disclosing these fees believe that after disclosure the financial advisor only advises on products purely in the customer's interest and customer's needs and that the fee itself is not a driver for the relationship. Cain et al. (2011) and Leiser (2011) show that people, who are in favor of the disclosure of fees, believe that disclosure leads to a better advice. It also prevents, in the same people's view, that an advisor gives advice only in his or her interest and not for a customer's benefit. If the customer feels that the advisor only has the customer in mind, and not his or her fee, then the customer will be more satisfied with the relationship and, subsequently, the advisor will be more satisfied. Hence we postulate the following hypotheses:

Hypothesis 7.6: *The disclosure of the fee of an advisor comes to the benefit of the relationship.*

A financial advisor and, at the same time, the seller of financial products can also be satisfied with the relation with the customer if a customer decides to come back a next time for new advice (perhaps on new products), see Palmatier et al. (2006). The recommendations that customers make to others (word of mouth) is a crucial feature of relationship investment. These customers' recommendations are in turn relevant for customer satisfaction. When someone can recommend an advisor, then this customer is satisfied with the relationship. Taking this together, we put forward:

Hypothesis 7.7: *Customers and advisors alike are satisfied with their relationship if the customer is loyal to the advisor*

7.4 Empirical results

In this section we shall evaluate the seven hypotheses in the previous section against the data that we collected and already summarized in Chapter 5. We first look at the hypotheses on the consumers and then we turn to the advisors. When available, the hypotheses will be tested using data for both advisors and customers. We give an overview of the used questions for examining our hypotheses in Appendix 7A and 7B.

7.4.1 The customer is satisfied with the relationship

The first hypothesis states that customers with more financial knowledge are more satisfied about the given advice. Oehler and Kohlert (2009) stress that education and interests in financial products seem to be important for the perceived quality of advice. Better prepared customers do get more out of the relationship, and hence are more satisfied. The scores on question CK10 ("The advice of my financial advisor is crucial for my product satisfaction") strongly support this conjecture as the mean score 4.78 is significantly different from 4. The scores on CQ3 ("My advisor gives me a proper advice") with a significant mean of 5.03 show that the surveyed customers in general are satisfied.

When linking the answers to CK10 with statements of consumers' interest in financial information, we find that individuals who claim to have no or little interest in financial information are also not satisfied about the advisor giving proper financial advice. Only 12.4% of these individuals are satisfied. This is in stark contrast to individuals who do claim to have an interest, as 61% of these also state that they are satisfied. In sum, satisfaction levels increase when consumers' involvement in the advising process and it clearly pays off to be better informed in advance.

The answers to statement CK9 provide a direct test for Hypothesis 7.2. When we ask "When my financial advisor helped me well before, I will go for a consult the next time", we observe a mean value of 5.85, which is far away from 4, and which is of course significantly different from 4. The possibility that a customer visits another financial advisor is not studied. Hypothesis 7.3 is on the perceived expertise of advisors that makes customers to rely on their advice. We asked our surveyed customers a direct question on the perceived expertise and this is CQ1 ("My advisor has sufficient knowledge". The mean answer to this question is 5.27, and again this is significantly different from 4. When we ask if "A verbal advice is more important than written information for my choice of a financial product" (CK17 with a significant mean of 4.42), then we again find that customers are satisfied due to the expertise of advisors. Hence, we find support for Hypothesis 7.3.

Legislation in the Netherlands establishes that a disclosure of the advisor's fee is as an important element of providing reliable advice. It aims at providing a full overview of costs and fees, which supposedly makes it possible for a customer to make a more objective decision. However, recent literature on the effect of disclosure, as Cain et al. (2011) and Leiser et al. (2011), presents evidence to the contrary. These studies claim that disclosure of the fee that an advisor will receive does not meet its goals. We followed this literature when putting forward our Hypothesis 7.4.

When we ask 313 customers whether "The size of my advisors' fee is relevant for my choice to purchase a financial product" (CK14), we estimate a mean value of 3.37, which turns out to be significantly below 4. A related question is CK13, where we posit "I want to pay a fee for good financial service". The responses to this statement obtain a mean value of 3.84, which is not significantly different from 4. Hence, it seems that consumers are indifferent to the fee of the advisor. This seems to be supported by the answers to CQ5 “The fee of my advisor is correct”, which attain a mean value of 4.36, which is significantly different from 4, although the percentage of individuals marking a 4 is 55.5%. In sum, the fee of the advisor does not seem to play an important role in the relationship between a consumer and a financial advisor, and hence we find no evidence against Hypothesis 7.4.

7.4.2 An advisor is satisfied with the relation

Oehler and Kohlert (2009) suggest that the quality of advice is influenced by the level of education of customers. The preparation of the customers before they seek advice is relevant for the quality of advice and therefore relevant for the advisor’s satisfaction with the relationship. Our Hypothesis 7.5 summarizes this. When we consider the answers to statement AM3 (“Customers are well prepared about which solutions and products they want before they come to me for advice”). Interestingly, even though better prepared customers get the most out of the relationship, the insignificant mean value of 3.84 for AM3 shows that advisors do not feel that their customers are well prepared.

A very prominent topic is the fee of an advisor. We asked about this to the customers, and now it is interesting to learn about the opinions of the advisors. Our Hypothesis 7.6 reads as “The disclosure of the fee of an advisor comes to the benefit of the relationship”, and it entails that the advisor only considers the interests of the customer. Statement AM6 (“I think a good advice is more important than striking a bargain”) obtains an estimated mean of 5.81, which significantly deviates far away from 4.

Disclosure of a fee is important for a customer to get all relevant information so he or she will be able to make an objective decision. It should be the case that the advice of a financial advisor is independent from the fee to be received. For the quality of the relationship between a financial advisor and his customer this presumption is relevant.

To examine the role of the fee in more detail, consider the statement under AM13, which reads “My customer has no interest in my earnings of the advice”. The 266 advisors report a significant mean score of 4.71. Additionally, confronted with the statement “My customer wants to receive an explicit invoice instead of paying my fee as part of the total sum", most advisors strongly disagree (mean value of 2.51). We can safely conclude that the advisor believes that his fee is of no importance to his advice and that customers prefer a fee integrated in a total sum instead of a specified invoice. When we ask the advisors whether they clearly inform their customers about what they earn with their advice (AM12), we see that almost 49% of the respondents do not agree with this statement. When we correlate AM12 with AM13 we see that the advisors, who believe that their customers are not interested in the advisor's fee, also are the respondents who do not inform their customers about what they earn with his advice.

The fee that an advisor will receive after providing a customer with advice, and selling a financial product, is not the only factor that can lead to objective financial advice. An advisor should also be honest and have integrity. Statement AM11 ("A customer's financial possibilities are most important to me, even if the client thinks otherwise"), with a significant mean score of 5.39, shows that advisors perceive themselves as honest. To the satisfaction of advisors, such honesty (and of course perceived expertise), they would hope that "My customers follow my advice for the solution of their financial needs". The answers to the related statement AM2 have a significant mean of 5.73. In sum, the fee is not the driver of the satisfaction of advisors with the relationship, but it is (in part) the fact that customers adhere to their advice.

Customer loyalty to their financial advisors is high, see also Chapter 6. Advisors believe that an advice is good when the customer wants to come back a second time with a new financial question. The related responses to statement AM8 obtain a mean value of 5.79, which is far from 4. The satisfaction level of advisors is evidenced further when we consider the answers to AM9 ("Due to my advice, the customer is satisfied about the financial product he purchased"), which has a mean of 5.86. Hence, we obtain support for Hypothesis 7.7, that is, customers and advisors alike are satisfied with their relationship if the customer is loyal to the advisor.

7.4.3 Comparing advisors and customers

As in Chapter 6, it is now interesting to compare the answers to the statements made by the customers and the advisors, when they face (broadly) similar statements. It might be that financial advisors are overconfident, also when it concerns the quality of the relationship.

Sniezek and van Swol (2001) deal with the relations between trust, confidence, and expertise in judge-advisor systems. They stressed the importance of an ongoing relationship as a basis for trust. We found similar results in Chapter 6. Sniezek and van Swol (2001) also address the relation between trust and the acceptance of advice.

In a recent study Radzevick and Moore (2011) explicitly address the potential overconfidence of an advisor in the relationship between advisor and advisee. The key notion they examine is whether confidence is positively correlated with accuracy. These authors present evidence that the customers' selection decisions depend more on to what extent the advisors express confidence than on the advisors' previous accuracy. They also report evidence that advisors will increase their expressions of confidence over time. When customers select more confident advisors, their performance will be evaluated higher.

These recent findings are also important for our research. We can compare the results about advisors and customers' opinions towards the quality of advice, as a measure of satisfaction. Table 7.1 shows some statistics about the differences in confidence between the financial advisor and the customer towards the quality of advice. Clearly, advisors are far more positive with the statements than the customers are.

Figure 7.1 reinforces the conclusion from Table 7.1 by presenting the percentages of respondents who agree with a certain statement. Clearly, advisors are much more in agreement with the statements.

Finally, Table 7.2 compares customers' opinions and advisors' opinions about the items that are important for the satisfaction levels of the relationship. Concerning commitment and trust there is strong evidence for advisors' overconfidence towards these items.

Interestingly, the advisors and customers do show some disagreement over the importance of (disclosing) the fee.

Table 7.1: Comparing the mean scores for advisors and for customers: Quality of advice

Quality of Advice	Advisors	Customers	Difference	p-value
Sufficient Knowledge AQ1 versus CQ1	6.46	5.27	1.190	0.000
Providing Creative Solutions AQ2 versus CQ2	5.94	4.91	1.025	0.000
Proper Advice AQ3 versus CQ3	6.14	5.03	1.108	0.000
Accessibility AQ4 versus CQ4	5.69	4.94	0.753	0.000
Fee is Correct AQ5 versus CQ5	4.99	4.36	0.631	0.000

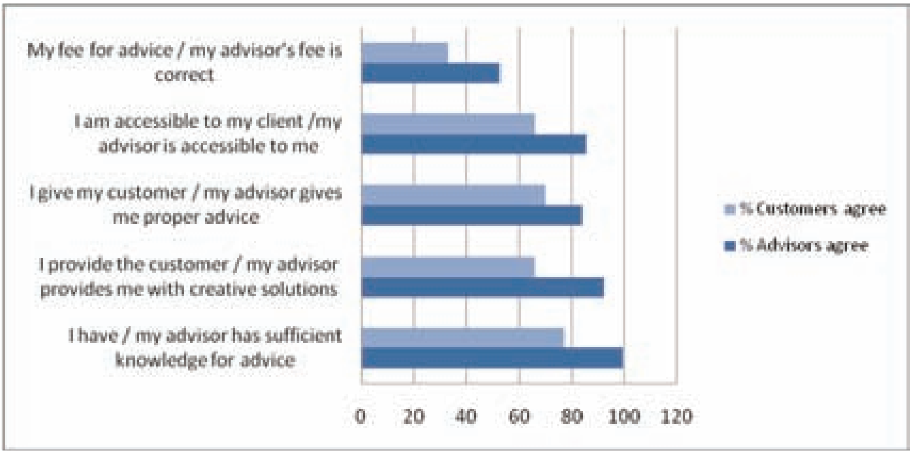

Figure 7.1: Overconfidence of advisors towards quality of advice

Table 7.2: Comparing the mean scores for advisors and for customers: Relationship

Type of relationship	Advisors	Customers	Difference	p-value
Financial advisor is visited for good financial advice AM1 versus CK1	6.29	5.17	1.117	0.000
Best suitable advice AM2 versus CK2	5.73	4.91	0.815	0.000
Come back after good advice AM8 versus CK9	5.79	5.82	-0.028	0.775
Customer satisfaction after advisor's advice AM9 versus CK10	5.86	4.78	1.088	0.000
Informed customer wants to pay for advice AM12 versus CK13	3.49	3.84	-0.348	0.019
Fee is important for purchase decision AM13 versus CK14	4.71	3.37	1.340	0.000
Invoice as percentage of agreement AM14 versus CK20	2.51	3.63	-1.121	0.000
Duty of care talks useful AM15 (negative) Versus CK16	6.00	5.26	0.738	0.000
Loan warning hesitates AM21 versus CK22	4.10	4.48	-0.375	0.007
Advice most important For purchase decision AM22 versus CK23	5.64	4.54	1.106	0.000

7.5 Conclusion

Our empirical results, shaped by the hypotheses that we drew from the relevant literature, suggest a few interesting conclusions. First, customer satisfaction scores indicate that a customer receives a better financial advice if he or she is higher educated and has more prior knowledge. Customer loyalty is anyway high, and this, together with the findings in Chapter 6, suggests that seeking advice is in some sense a habitual activity: one simply needs advice, no matter what. Furthermore, we see that customers rely on the advice of the financial advisor if they believe that the advisor has expertise. And, quite intriguingly, we find evidence that the fee of the advisor is not important for the customer.

At the other end of the dyadic relationship, advisors are aware that customers are well prepared prior to seeking advice. The advisor also feels that he or she gives advice purely in the interest of the customer. The fee is viewed as not important. The products he will advice are in the customers' benefit. The advisor is also convinced that the customer will come back for new advice. Finally, the advisor believes that his or her advice deserves a fair price and that a customer is willing to pay for that.

Finally, in general the advisors are happier with the relationship, more impressed by their own quality, and more convinced about their own integrity, than that their customers do.

Appendix 7A: Hypotheses "The customer is satisfied with the relationship"

In this appendix we give an overview of the relevant questions of our survey, described in Chapter 5, to examine our hypotheses in 'The customer is satisfied with the relationship'

Hypothesis 7.1: Customers with more financial knowledge are more satisfied with the given advice

- CK10 "The advice of my financial advisor is crucial for my product satisfaction"
- CQ3 "My advisor gives me a proper advice"

Hypothesis 7.2: Customers are more loyal when they are more satisfied

- CK9 "When my financial advisor helped me well before, I will go for a consult the next time"

Hypothesis 7.3: The perceived expertise of advisors makes customers to rely on their advice

- CK17 "A verbal advice of the advisor is more important than written information for my choice of a financial product"
- CQ1 "My advisor has sufficient knowledge"

Hypothesis 7.4: Information about the advisor's fee is of no importance to the customer

- CK13 "I want to pay a fee for good financial advice"
- CK14 "The size of the advisor's fee is relevant for my choice to purchase a financial product"
- CQ5 " The fee of my advisor is correct"

Appendix 7B: Hypotheses "The advisor is satisfied with the relation"

In this appendix we give an overview of the relevant questions of our survey, described in Chapter 5, to examine our hypotheses in 'The customer is satisfied with the relationship'

Hypothesis 7.5: An advisor is more satisfied with a relation when potential customers are better prepared

- AM3 "Customers are well prepared about which solutions and products they want before they come to me for advice"

Hypothesis 7.6: The disclosure of the fee of an advisor comes to the benefit of the relationship

- AM2 "My customers follow my advice for the solution of their financial needs"
- AM6 "I think a good advice is more important than striking a bargain"
- AM11 "A customer's financial possibilities are most important to me, even if the client thinks otherwise"
- AM12 "I clearly inform my customers about what I earn with this advice"
- AM13 "My customer has no interest in what I earn with my advice"

Hypothesis 7.7: Customers and advisors alike are satisfied with their relationship if the customer is loyal to the advisor

- AM8 "A customer will come back to me for new advice when gave him a good advice earlier"
- AM9 "Due to my advice, the customer is satisfied about the financial product he purchased"

Chapter 8:
Summary and conclusions

In the introduction of this dissertation we described the background of Customer First in the Banking Code in the Netherlands. This Banking Code pays attention to improving customer satisfaction. Interestingly, the code does not address the relevance of improving customers' financial literacy and ability to good financial decision making. We conjectured that such literacy is important, as it also increases the skills of individuals when they consult a financial advisor. This last chapter of the dissertation summarizes the main findings of our empirical studies. Next we discuss a few limitations of our studies. Finally, we translate some of our results to practical implications.

8.1 The main findings

In Chapter 2 we presented summary statistics of the amounts of consumer credits and consumer savings in the Netherlands and various other countries. We gave figures on various credit products, like credit card limits, overdraft on current accounts and mortgages. It was illustrated that consumer credits in the Netherlands are substantial. In fact, relative to other countries, some types of consumer credits in the Netherlands are exceptionally high. We also saw that trends in consumer credits are positive, almost without exception. Notable were the growth of tax privilege savings and the large number of savings in life insurances. The main conclusion to take away from this chapter is that the total size of consumer credits is large, and perhaps too large.

In Chapter 3 we presented empirical results on individuals who have to perform computations with interest rates. Our main conclusion is that consumers face substantial difficulties dealing with interest rates. In fact, the outcome was that the answers were given randomly. We also found that individuals are inclined to downward estimate the months that are required to pay back loans. Hence, they believe that debts are paid off earlier than they are in reality. Our findings suggest one possible reason why households can run into financial problems. When it is believed that loads are paid off early, households might be tempted to accept new loan offers too soon. An important additional finding is that the monthly payments apparently serve as a moderator. When these amounts increase, the size of the self-serving bias decreases. We argued than when loans have higher monthly payments, consumers will make less mistakes.

In Chapter 4 we paid attention to campaigns like “borrowing money costs money”. The campaign is meant to make customers more aware of the impact of loans on their household finances and on their long-term financial situation. We argued that such a campaign can be made more effective if the actual amount of the extra money is given. We tested our conjecture for newly collected data, concerning the purchase of an LCD TV test and a sofa. We found that the willingness to pay on credit diminishes when the total amount involved in the loan was described. Our empirical evidence suggested that actually mentioning the total amount involved in the purchase on credit made consumers less prone to opt for credit payments. We therefore recommended that the punch line “borrowing money costs money” should be completed as for example: “when you purchase this television set it costs you 338 euro if you pay with cash and it costs you 472 euro when you pay 8 euro per month in 59 monthly terms”.

The first three chapters indicated that individuals have many debts and that they face difficulties when making financial decisions. In many cases, consumers revert to an advisor who should help them to make proper decisions. We believe it is important now to learn more about the relationship between a financial advisor and his or her customer. The next chapters deal with this relationship, for which we collected a unique set of data.

In Chapter 5 we described the surveys we used to collect the data on consumers of financial products and their advisors. We presented the design of the internet survey for customers and their financial advisors, and we discussed the detailed responses to the range of questions. We added the outcomes of personal interviews with financial advisors and the feedback from the company’s managers. With the help of two Netherlands-based financial institutions, we could collect a large number of respondents, which made the outcomes of our analysis rather accurate. Part of the data of this chapter we used in the subsequent chapters to test a few hypotheses on the relationship between advisors and advisees.

In Chapter 6 we focused on the concept of expertise in this relationship, where we considered the expertise of the customer, as perceived by the advisor, and the expertise of the advisor as perceived by the customer. The relationship may involve asymmetric information. Also, the financial advisor often has a double role, which is giving advice and sales of the products. To characterize the relationship more in detail we draw on the Advice Giving and Taking (AGT) literature (Jungermann, 1999) for decisions on financial services.

The results of the tested hypotheses in Chapter 6 led to some interesting conclusions. The advisor knows that well educated customers are better prepared. Customers with less understanding tend to expect more expertise of the advisor. The advisor's expertise is more important for customer's decision making than any written information, where the advisors believe this to be much more important than customers do. Customers confidently claim that they understand the available (written) information. Customers also agree that a higher educated customer is better prepared and spends more effort to understand the various features of financial products. Customers with higher education are more aware of the future consequences of their choices. Apparently, education plays an important role in understanding the advice and financial information.

The amount of information received by customers also plays a role in customers' decision making. Interestingly, customers do not agree that they receive an overload of information prior to advising process, whereas advisors feel that customers do. In sum, we find quite some distinct perceptions by customers and advisors, although both believe that the amount of information makes a customer unable to make a good decision about the risks.

In Chapter 7 we focused on the satisfaction levels of the advisor and the customer with this relationship, where our hypotheses were framed according to the AGT theory again, and to the relationship marketing literature (Palmatier et al., 2006).

Customer satisfaction scores indicated that a customer receives a better financial advice if he or she is higher educated and has more prior knowledge. Customer loyalty is anyway high, and this, together with the findings in Chapter 6, suggests that seeking advice is in some sense a habitual activity. One needs advice, and one reverts to an advisor. Furthermore, we saw that customers rely on the advice of the financial advisor if they believe that the advisor has expertise. And, in contrast to common wisdom, we found evidence that the fee of the advisor is not important for the customer.

At the other end of the dyadic relationship, the advisors felt that customers are well prepared prior to seeking advice. The advisor also felt that he or she gives advice purely in the interest of the customer. The fee is viewed as not important. The products he will recommend are in the customer's benefit. The advisor is also convinced that the customer will come back for new advice. Finally, the advisor believes that his or her advice deserves a fair price and that the customer is willing to pay for that. In general, we noted that the advisors are happier with the relationship, more impressed by their quality, and more convinced about their integrity, than that their customers are. We also obtained strong evidence for overconfidence of the advisor towards their customers.

8.2 Limitations

A substantial part of this dissertation concerns our study of the relationship between financial advisors and their customers. We wished to compile a large database which would allow us to draw some generalizing statements. To get in touch with financial advisors and their customers in a real-life setting, we had to search for financial services companies who were willing to participate in our research.

We found two companies who wanted to participate. We did not have to pay for surveying their customers and financial advisors. However, the exact moment of sending out the surveys had to fit with the companies' other customer contact moments and the other contact moments with their financial advisors that were already planned. The contents of the questionnaires of customers and financial advisors had to be discussed by the participating companies. And, it was an opportunity for the companies to ask their customers and financial advisors questions they were already planning to survey themselves.

These conditions did affect our research in a way that the questionnaires and our hypotheses were not made at the same time. Also, the questionnaires contained some questions that we did not use for our tests in Chapters 6 and 7. However, we found the answers interesting enough to report them.

The first questionnaires were distributed in December 2009 and the last in May 2010. It could be that this timing came at a special moment as this period marked the worldwide recovery from the 2009 recession. Fortunately, financial advisors and customers of a company were surveyed in the same period.

A final potential limitation is that, due to time constraints and organizational issues, as well as due to the protection of customer information, we were not able to investigate one-to-one relations between the financial advisor and his customer. That is, our results in Chapters 5, 6 and 7, are based on average scores, while it would have been better if we could have interviewed pairs of individuals, that is, the advisor and the advisee at the same time. On the other hand, now the data were impersonal, and this could have led to more honest answers.

8.3 Implications and topics for future research

One key finding of this dissertation is that being prepared for financial decision making seems to be very important, for all aspects of the relationship. The customer of financial products has to be prepared before he of she seeks financial advice and has to decide whether to purchase a financial product like a pension product or a mortgage. Also a financial advisor has to prepare for the financial advice he will be giving. He is not only the expert about the financial products, but also the expert about the advice itself.

Expectations about the quality of advice are high, and perhaps may become unrealistic. Indeed, despite the advice given by the financial advisor, the customer still has to decide. The abilities to make a good decision are then important. We recommend that financial literacy has to improve to make customers better prepared for their financial decision making. So, financial literacy is not only important in itself, it also drives the quality of and satisfaction with the relationship between advisor and advisee.

The advisory process is dyadic and has two participants, and both these participants have their responsibilities. To improve the financial literacy of the customers, the ability to do calculations has to be improved. We did see that computations with interest rates are difficult, so we recommend the design of simple tools for consumers to make these computations. Companies that sell products on credit should be obliged to present the actual amount of money involved in the transaction. At the other end, we noted that the advice itself is more important than any written information. This puts a strong appeal on the advisors and their communication skills.

We also found that the disclosure of fees does not have the implications that policy makers think they have. In fact, other literature shows that disclosure can even hurt the people who it aims to protect. However, we found that customers do not have strong opinions about the fee of an advisor. Advisors are believed to be more concerned with the quality of their advice than the fee that they charge. On the downside, advisors are too confident about various aspects of their job. This may make it difficult to understand the customer and his needs. Customers understand less than what advisors think, and here lies the crucial feature of their relationship.

Customer first? Our results indicate that a customer has to work hard to become first in the advisors opinion. To receive good financial information and good financial advice, the customer has to be prepared, has to become financially literate, and has to invest some time and effort to understand financial advice.

Customer first? Our results further show that advisors are convinced that they advise to the customer's benefit. However, they have to invest in time and effort to really appreciate the customers' needs and to help them to make a sound financial decision. They may be confident but overconfidence can hurt the relationship and hurt the quality of advice.

Customer first? Policy makers are convinced that disclosure of fee improves the quality of financial advice and the relationship between a financial advisor and a customer. Our research does not support this notion. In fact, we would claim that a too strong appeal on disclosure of the fee blurs the real important issues of financial literacy and of the levels of expertise of advisors and customers.

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Summary in Dutch / Samenvatting in het Nederlands

Klant Centraal?
De relatie tussen adviseurs en consumenten van financiële producten.

"Klant Centraal" is een belangrijk onderwerp in de recent in Nederland geïntroduceerde Code Banken. Deze code behandelt voornamelijk de klanttevredenheid en is gericht op het terugwinnen van vertrouwen in de banken door de Nederlandse consument. De code behandelt echter niet het verbeteren van eventueel financieel inzicht van consumenten en het bevorderen van hun vermogen om goede besluiten te nemen over persoonlijk financiële onderwerpen, gegeven het feit dat zij meestal advies inwinnen bij een financieel adviseur. Dit proefschrift gaat over deze twee onderwerpen, welke door de voorzitter van Federal Reserve, Ben Bernanke, in een eerdere toespraak benoemd zijn als belangrijke onderwerpen voor de economische welvaart van huishoudens en voor de stabiliteit van het financiële systeem in zijn geheel.

In de eerste hoofdstukken geven we een overzicht van de bedragen die gemoeid zijn met individuele schulden en spaartegoeden. We geven de informatie van Nederlandse huishoudens, gerelateerd aan de cijfers van andere Europese landen en, indien van toepassing, aan cijfers van de VS. Verder laten we zien dat consumenten moeite hebben met berekeningen met percentages. Vervolgens tonen wij aan, op basis van nieuw verzamelde gegevens, dat de bereidheid om te kopen op afbetaling vermindert, indien het totaal te betalen bedrag expliciet wordt vermeld.

Consumenten zoeken meestal hulp bij hun keuze van financiële producten. Velen gaan voor advies hierover naar een financieel adviseur. Het tweede deel van dit proefschrift gaat over een uitgebreid onderzoek onder financieel adviseurs en hun klanten. Deze gegevens zijn verzameld met hulp van twee Nederlandse financiële organisaties. We richten ons op de ervaren expertise van adviseurs en van de klant in het besluitvormingsproces, en op het niveau van tevredenheid met deze relatie en van transparantie van de beloning van de adviseur. We plaatsen de antwoorden van de adviseurs en consumenten naast elkaar en constateren en substantieel verschil in opinie tussen beiden over dezelfde onderwerpen.

About the author

Anita Vlam (1964) studied economics at Erasmus University Rotterdam and received her doctoral degree in 1989. After her graduation she worked for about twenty years in process management, as a team manager mortgages and senior product manager mortgages at several financial services companies. Since 2008 she participated the Mature Talent Program of the Erasmus School of Economics to do research and write a PhD. Her research interests include financial literacy, financial services, consumer behavior and relationship management.

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CUSTOMER FIRST?

THE RELATIONSHIP BETWEEN ADVISORS AND CONSUMERS OF FINANCIAL PRODUCTS

Customer First is an important issue of the recently introduced banking code in the Netherlands. It mainly concerns customer satisfaction and it is aimed at regaining trust of customers. Interestingly, the code does not address the urgency of improving customers' financial literacy and their ability to make sound financial decisions, given that they consult a financial advisor. This dissertation specifically considers these two topics.

In the first chapters we present empirical results about the sheer size of consumer debts and about the difficulties that consumers have with interest rate computations. With newly acquired data, we also document that the willingness to purchase on credit gets reduced when the total amount involved is mentioned explicitly.

As consumers apparently need help, many turn to financial advisors. The second part of this dissertation deals with an extensive survey amongst financial advisors and their customers. This unique database could be compiled with the help of two Netherlands-based financial institutions. We address the perceived expertise of the advisor and the advisee, the satisfaction levels and the relevance of the disclosure of the advisor's fee. We also contrast the answers of advisors and consumers and we document a substantial difference in opinions about the same topics.

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