HSBC Private Banking

Video transcript

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Behavioural biases video

I'm Jonathan Sparks, I'm the Chief Market Strategist for the UK and Channel Islands. I work on some of the asset allocation decisions and also thematic investments and any other market updates you see.

Behavioural biases are in their very nature something that you wouldn't be aware of. They often can quite strongly affect your decision making and they can lead to outcomes particularly in investments that are not beneficial. And actually if you're made aware of these behavioural biases you'll be surprised actually how they can change the way you think and hopefully give you better outcomes.

So often the best way of revealing these biases is through some quite simple examples.

OK so loss aversion is actually when you're more averse to losses than you are a gain in similar magnitude. So for example, research has shown that actually people are indifferent between a gain that is twice the size of a loss. There was a Nobel Prize economist, winning economist, Paul Samuelson, who gave his friend a bet and he basically said if I flip a coin, you'll either get a £200 gain or a £100 loss. Will you take me up on that bet? And his friend was indifferent, he didn't want to take him up on that bet. So essentially he had loss aversion he didn't want to risk that loss even though the gain was much bigger. And essentially this is something that you can take with your investment decisions where actually you're averse to short term losses.

A lot of people have loss aversion to a certain degree it's just natural, we're generally risk averse.

So often if you have symptoms of loss aversion actually there's something called myopic loss aversion, perhaps you're checking, you have a portfolio and you keep checking it. And if you keep checking it you are aware of those very small losses that you've been maybe making so that makes you reluctant actually to take risk.

The downside of loss aversion is actually you become too risk averse. So often what you'll see is people who are loss averse and keep checking their portfolios actually take a lot less risk over the length of their investment time frame.

Over a long time period ideally you want to take more risk because that should give you more returns.

So the positive consequence of loss aversion is that actually if you need that money, if you can't really tolerate many losses, then being risk averse is obviously a good thing.

The only way you can actually be aware of these biases is actually talking to other people and that's why we have your relationship and investment team here to help you.