AMF HOUSEHOLD SAVINGS OBSERVATORY NEWSLETTER

AUTORITÉ DES MARCHÉS FINANCIERS

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EDITORIAL

Preventing aggressive online trading practices

Alarm bells began to ring early on at the AMF with regard to the growing presence of speculative trading in the retail investment market. We noticed that the sales techniques employed were often accompanied by considerable psychological manipulation of the victims. In order to better understand the methods used, we commissioned the social psychology laboratory at Aix-Marseille University, specialists in the sphere of social influence, to examine the testimonies of victims of forex and binary options trading and identify the persuasive marketing and engagement techniques in operation.

Their findings are illuminating, and cross-referencing them with financial regulations is equally enlightening.

We present some of these findings in this Newsletter.

They confirm that the methods used by speculative trading companies drag the victims into a spiral, under the guise of investment advice, of investing ever greater amounts, despite their initial losses (this is known as escalation of commitment). When used in a complex financial universe, these techniques constitute aggressive sales practices that are forbidden under consumer law.

In order to contain them, a system of alerts and education remain essential. The researchers' findings will help the AMF to communicate effectively with the general public.

As regards investor protection, Regulation (EU) No 600-2014, which will come into force on 3 January 2018, will enable Europe's regulators to take steps to ban certain products and dishonest marketing methods, and using the results of the social psychology research could make it easier to identify these.

The AMF remains determined to eradicate speculative product sales practices that are not in the client's best interest. ■

FOCUS ON

France lags behind on financial literacy

French people are less able than some of their European counterparts to answer questions about investments, expected returns and risk.

According to a recent international comparative study, there is less financial literacy in France than in nine other Western European countries. These findings are based on survey participants' ability to answer five comprehension questions on risk and return, interest rates, inflation, expected value and diversification.

Poor understanding of risk and return

In order to evaluate financial literacy at an international level, people are usually asked to respond to three questions on compound interest, inflation and diversification. In the most recent survey, the percentage of correct answers was 76% for compound interest, 64% for inflation and 49% for diversification. The results in France (73%, 57% and 44% respectively) were below these averages.

There were two additional, harder, questions on expected value and comparative risk, and the percentage of participants who gave the right answer to these ranged from just 9% (in France) to 19% (in Germany and Austria).

In total, just 8% of French and Portuguese respondents were able to correctly answer all five questions. The corresponding figure in Germany and Austria was 15%.

Diversification a little-known concept

More than a third of people surveyed replied "Don't know" to the question on diversification ("Do you think the following statement is true or false? "Buying a single company stock usually provides a safer return than a stock mutual fund."). In France, nearly 50% of participants said they did not know, compared with just 25% in Germany.

Education affects financial literacy

Those with a higher level of education are more likely to answer the questions correctly. For example, only 8% of people with a university degree or higher failed to correctly answer the two questions on interest and inflation, compared with 21% of less qualified respondents. However, only 20% of people with university degrees correctly answered the other three questions (diversification, risk, expected return). ■

1 When will the penny drop? Money, financial literacy and risk in the digital age", a survey of 1,000 people representing the 10 major Western European countries. The process was conducted online in November 2016. Allianz International Pension Paper, January 2017

Online trading marketing practices

The AMF has studied the techniques used to market trading in forex and binary options with regard to research on pressure and persuasion techniques. Main lessons learned.

Since 2011, the AMF has strived to combat the marketing of speculative forex and binary options trading to the general public. We decided very quickly that these products were not suitable for retail investors. We also noticed how certain 'sales techniques' have swelled losses, with many victims finding themselves dragged into a spiral and unable to get themselves out.

In order to better understand and regulate this phenomenon, and to help investors avoid the traps set by certain trading firms, the AMF commissioned the social psychology laboratory at Aix-Marseille University, specialists in the sphere of social influence and persuasive communication, to identify the techniques employed by these firms and come up with some recommandations[2].

Pressure techniques

Based on victims' testimonies gathered by the AMF and adverts published by the trading companies, the researchers were able to identify different forms of pressure, including commitment and persuasion techniques.

↗ In advertising

Adverts for speculative trading feature seemingly widespread persuasion techniques. They aim to lend credibility to the trading firm and its approach. In addition, they are directed at an inexperienced audience who know little or nothing about speculative trading.

Social proof and the norm of reciprocity (see inset) are pressure techniques that are also frequently used. For example, some adverts claim, inaccurately, that many people have already made lots of money. For example: "Over 1,257,400 people trade with Anyoption", "Some people in France are earning lots of money by trading in binary options".

In addition, offering some kind of gift (e.g. "We'll double your next deposit", "Get €50 cashback on your next trade") is an effective technique that makes web users more likely to contact the trading firm.

FOCUS ON

Social proof

Individuals tend to think and act in line with the thinking and actions of people who are like them. As such, they will deem behaviour to be appropriate to a particular situation if they see other people adopting it.

The norm of reciprocity

Individuals tend to try to repay benefits that they receive from another. If a person receives a service or a gift, he will feel beholden and will tend to give back quickly and more than he initially received.

↗ Exchanges between clients and trading firms

The trap closes once the user makes contact for the first time with a trading 'adviser'. The researchers uncovered several commitment techniques when they looked at exchanges between the clients and these 'advisers', which gradually led the clients to invest more and more money.

The 'adviser' attempts to win the client's trust by discussing their own expertise. The client therefore tends to become wholly reliant on their suggestions and feels responsible for the initial losses without questioning the expertise of the 'adviser'.

The 'adviser' sometimes forges a very close relationship with the client. In such a situation, because they feel emotionally involved, the client may comply more readily with the demands of the 'adviser', notably when these involve investing additional sums of money.

There is a clearly identifiable desire on the part of these 'advisers' to encourage their clients to invest without regard for the interests or financial resources. For example, they always try to persuade their clients to reinvest after losing their capital. An investment motivated by the goal of recovering a loss may lead to escalating commitment and encourage clients to persevere with an unprofitable course of action.

Such conduct goes against the rules of honesty and putting the client's interest first. It distorts or invalidates the free consent of the client.

Lessons on how prevent this phenomenon

To the uninitiated, things such as pressure techniques, the commitment principle and the norm of reciprocity are hard to see. They rely on principles that are deeply anchored within the individual, complicating efforts to resist. In order to fight these toxic practices, there are three things we can do to change the way investors think:

↗ Expose the persuasion techniques

According to the researchers, the best way to prevent the effects of these techniques is to inform the general public about their existence and their commercial purpose. Consumers need to know that contacting a trading company or 'adviser' is dangerous because their investment decisions could be subtly influenced. Recognising and exposing these techniques creates a healthy distance between the client and the seller, and decreases the opportunity for psychological manipulation.

↗ Bust the myth of the trader

The aura surrounding traders and trading needs to be removed. Their adverts convey a positive image of the trader as a symbol of social and professional success.

By identifying and subsequently rejecting the social representation elements of trading, investors can more readily dismiss the notion that trading is accessible to the general public and make these speculative techniques seem less attractive.

By calling into question the credibility of trading companies and their 'advisers', who offer unrealistic crash courses in trading, investors can more easily turn down these enticing, yet dangerous, offers.

↗ Halt the escalation of commitment

According to the researchers, the escalation of commitment process is extremely hard to stop once the trap has closed. They have come up with several recommendations for investors:

- write down their investments, gains and losses so they can keep track of all their decisions;
- set a reasonable limit not to be exceeded and accept that they might lose their capital before investing;
- discuss investment decisions with their friends and family, or with other investors, in order to get the opinion of someone other than their 'adviser', and ditch the sense of shame at losing their capital or the notion of being a victim of fraud. ■

↗ GOOD TO KNOW

Fighting fire with fire

In order to counteract the alluring adverts from trading companies, the researchers recommend using similarly persuasive techniques in AMF communications.

For example, testimonies from victims should be used regularly because the general public will identify with them and therefore accept the content more readily.

2. *"Analysis of techniques used to market speculative trading in forex and binary options with regard to research on compliance without pressure, persuasion techniques and nudges", Lionel RODRIGUES et Fabien GIRANDOLA (Aix-Marseille University), in Scientifc Working Papers, and "Perspectives on the techniques used to market speculative trading on the Forex and binary options markets", Risk and Trend Mapping, May 2017.*

Commitment techniques have been identified in forex and binary options trading

Commitment techniques	*Examples for trading*
Foot-in-the-door (ask for a little to get more)	A customer is asked to invest €250, then, a few days later, asked to add €450.
Door-in-the-face (get turned down before making a more modest request)	An 'adviser' requests an investment of €20,000. The client says no, so the 'adviser' asks whether they can invest €10,000.
But-you-are-free (evoke freedom when making the request)	Examples of the formulae used by 'advisers': "But it's your decision, I don't want to pressure you", "I can advise you but I can't make the decision for you".
That's-not-all (reveal the benefits gradually)	An 'adviser' encourages the client to invest more to get a 100% bonus, and a second bonus if they invest an extra €1,000.
Lure and Low-ball (present fake benefits based or hide drawbacks)	Having committed to the VIP trade, the client notices that their investment has not been doubled (this was a fake benefit).

Household savings rate remains stable

French households saved 14.5% of their gross disposable income on average in 2016.

This figure was stable in comparison with the previous year. The financial savings rate (excluding mortgage repayments) was 5.4% (5.5% in 2015). ■

Source : INSEE, Informations Rapides, March 2017

French people more attracted to equities

In 2017, 38% of French people consider equities to be an interesting investment opportunity.

This represents an increase in the figure for the previous year (29%). Men tend to be more interested (44%), and the same goes for people with assets of more than €50,000 (57%), share savings plans (PEAs) or shares (68%), a salary savings plan (56%) or a retirement savings product (52%).

A respective 68% and 59% of people in 2017 are interested in buy-to-let investments and life insurance. ■

Source : IFOP for Cercle de l'épargne, AG2R-La Mondiale and Amphitéa, survey conducted on a representative sample of 1,001 French people aged 18 or over in March 2017.

Salary savings continue to grow

In 2016, investments in employees' savings schemes (PEEs) and retirement employees' savings schemes (PERCOs) increased by more than 9%.

Investments in salary savings schemes (both PEEs and PERCOs) totalled more than €13.7 billion last year, up €1.2 billion on 2015. Specifically, €3.5 billion resulted from mandatory profit-sharing and €4.6 billion from discretionary profit-sharing (+21% on 2015). In addition,

€3 billion came from voluntary employee contributions and €2.6 billion from employer contributions.

Total plan assets at the end of 2016 were €122.5 billion, an increase of 4.3% on a year earlier, primarily because of the rising equity and bond markets. Diversified savings funds, i.e. money market funds, equity funds, bond funds or mixed funds, account for 61% of these total assets. Employee-shareholder funds, which are invested mainly in shares of the employer, account for the remaining 39%. ■

Source : French Asset Management Association (AFG), March 2017.

Real estate investment funds prove popular in 2016

Investments in retail open-ended property investment funds (OPCIs) and real estate investment trusts (SCPIs) increased by 38% in 2016.

Inflows to the 178 SCPIs climbed by 30% to €5.6 billion, while those to OPCIs jumped by 66% to €4.1 billion.

Assets totalled €55.2 billion at the end of 2016, including €43.5 billion in SCPIs (+15% in a year and +75% over five years) and €8.7 billion in OPCIs (+92% in a year).

This means that investment in real estate now accounts for 1.7% of household financial savings (excluding unlisted shares and current account deposits). ■

Source : French Association of Real estate investment Companies (ASPIM), March 2017.

Awareness of FinTechs spreads

One in four French people say they are aware of so-called robo-advisors.

Although the general public do not really know what the term FinTech means, many investors use these new financial services without knowing it. For example, 47% are aware of crowdfunding sites (an increase of nine percentage points on 2016) and 26% of robo-advisors (up one point).

Indeed, 15% say they have already used a crowdfunding site and 6% have used a robo-advisor.

These people tend to be 'digital' clients, who favour online banking, and wealthy clients, with more than €25,000 of assets invested or to invest. They tend to be economically active men living in the Paris area. ■

Source : Harris Interactive for Deloitte, survey conducted on a representative sample of 2,000 French people aged between 18 and 70, March 2017.

114,000 individuals invested in FCPIs and FIPs in 2016

Investments in venture capital funds totalled €967 million in 2016.

This comprised €410 million (+11% on 2015) in innovation funds (FCPIs) and €557 million (+14%) in local investment funds (FIPs). This is the highest amount of inflows since 2008, when the figures were 31% and 5% higher respectively.

In 2016, 114,000 individuals (+15% on the previous year, -21% on 2008) invested €8,500 on average, primarily to capitalise on expected tax cuts. ■

Source : AFG-AFIC, March 2016.

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