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Active vs. Passive Investors: Pushing the Right Buttons

by Nino DeNicola

Experienced financial professionals have learned to look for differences among their investor clients that will guide the manner in which they approach these individuals, as well as the types of instruments and services they offer.

Asset level, age, marital/family status, occupation and retirement timetable are all obvious distinctions. Less evident, but perhaps more influential in the long run, is the attitude of the client toward the investment process. The aggressive or hands-on "driver" wants to keep the reins in his own hands, while the passive "passenger" is content to delegate substantial decision-making authority to his chosen advisor.

These attitudinal distinctions emerge in study after study and can be more useful than the classic demographic distinctions.

One group, which we refer to as "delegators," view investing as more of an obligation or a necessity rather than intrinsically enjoyable. Delegators are by no means unsophisticated, either intellectually or in terms of their professional or business experience, and the affluent are as well represented in this segment as are those of more moderate means. Nonetheless, delegators tend to lack confidence in their own financial or investment acumen, preferring to lean on the counsel of those who have, in their view, superior investment credentials.

By contrast, the opposite camp has more of a "hands-on" or activist attitude. They enjoy the process—the game of investing—and tend to have considerable confidence in their own financial judgments.

These attitudinal differences do not correspond to age, sex, occupation or asset-level distinctions, but tend to cut across all such demographic lines.

The phenomenon of investor mind-set allows us to draw a number of conclusions about the behavior, needs, interests and response patterns of these two segments—delegative and assertive—which have practical implications for those banks seeking to attract the business of wealthy customers.

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The two groups are quite similar in the overall nature of their investment holdings. Both prefer to diversify as a means of risk reduction, to set differing objectives for the various investment vehicles (e.g., stocks and CDs) and to add to their investment portfolios in what amounts to an ad hoc fashion, responsive to opportunity. Where they differ is in their criteria of measurement and in their approaches to the management of the various investments.

The delegators, for instance, tend to be content with "decent" returns. They generally prefer to hold investments for the long term. Basically more risk averse, they approach the stock market with some apprehension, with little confidence in their ability to make individual buy/sell decisions.

On the other hand, the activists appear to expect superior returns, whatever the vehicles. More opportunistic, they seem more apt to undertake short-term switching among individual holdings, in the hope of making a "quick hit." And as might be expected, they manifest more confidence in making specific decisions about individual equities.

The two attitudinal groupings differ in the institutions or investment resources with which they conduct business. For the delegators, banks, including trust departments, are a more natural preference. This group also deals with attorneys, accountants and (in the wealthier subset) investment advisory firms on a regular basis.

Hands-on investors are generally less attracted to banks. They tend to be partial to, and comfortable with, discount brokerage services, and some are customers of no-load mutual fund families where they can make frequent, short-term switches among individual funds.

Potential customers in the delegator attitude group respond most favorably to claims dealing with customized product and service offerings and to the offer of one-on-one advisory service. Delegators also react favorably to evidence of an institution's prestige and stability. Convenience is an additional incentive.

Hands-on investors, on the other hand, tend to respond to messages about an institution's favorable performance or "track record." They want to know that varied and numerous investment options are available and, with respect to convenience, they are most concerned about the bank's physical location.

Both groups prefer to have direct contact with a specific advisor, account representative, broker or other official, but their expectations with respect to such attentions differ. The delegators want their advisors to perform a true consultative function, providing proactive assistance in managing the account and taking extra steps in the hand-holding area.

The activist wants the official serving his account to be a facilitator rather than an advisor, to serve as the fulcrum around which the services of the institution are organized—networking, cutting red tape and putting the client in touch with all sources of institutional expertise.

There are some common expectations. Both groups want to feel that control is ultimately in their hands and expect, at a minimum, to be involved in making the initial decisions about asset allocation across various risk categories. Both expect the service officer to have a "client" rather than a "customer" orientation, i.e., a sensitivity to personal needs and goals. Both show a preference for "red carpet" treatment, as well as an expressed desire for the account officer to manifest pro-active behavior, not only giving timely advice but helping assess the client's progress toward goals. The difference is in emphasis.

To attract the business of individuals in the two attitude groups, different approaches should be used. Delegators tend to be responsive to the influence of personal contacts—friends, relatives and business associates—and to the recommendations of professional advisors, such as attorneys and accountants, in the selection of an investment advisor or service provider.

Activists, by contrast, are more prepared to be influenced by print media: advertisements and newsletters, for example. They are ready to study these for promising information on performance, interest rates and other such data, because they are confident of their ability to analyze prospectuses.

Account statement preferences parallel these attitudinal differences. Delegators prefer user-friendly statements, even those which offer one-page summaries of current balances, net gains and losses. The hands-on investors, however, desire more detailed data, choosing to monitor all their transactions closely.

In one area, not unexpectedly, both groups agree on—the subject of compensation for investment services. Both wish that compensation could, in some manner, be linked to the performance of a vehicle or an account. The delegators, however, are resigned to paying for services, while the activists remain fee-averse. Delegators appear more tolerant of a pre-set fee structure, proportional to account size, while hands-on investors lean toward a "pay-as-you-go" system.

Service providers would benefit from assessing the size of each group within their own base of current and prospective customers. The savings and efficiencies, in terms of promotion and staff structure alone, would be significant. ■

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