

Navigating individual financial well-being

South Africa | 06 June 2015 | Insight

Authors and contributors



Anne Cabot-
Alletzhauser

Navigating individual financial well-being

Financial decision-making is challenging. Simple decisions like spending rather than saving can be difficult to make. And this is quite apart from the challenges posed by product complexity.

In a recent study by Bhargava, Loewenstein & Sydnor (2015), they examined health insurance choices that had been made as simple as possible. They looked at these choices in the context of a single employer with 50 000 employees where all health insurance choices were offered by a single provider and had the same healthcare features. The only variation was in the financial dimensions of the decisions. These financial dimensions covered what individuals would pay monthly as a premium, what they would pay for out-of-pocket, co-payments and so on.

What they found is that most individuals chose options that were inferior in every way to other options that were available, primarily due to leaning on maladaptive rules of thumb. For most of the options chosen, there was another option that was better on every dimension. These are called dominated options. This is like choosing a slow, uncomfortable, expensive car rather than a fast, comfortable, cheap one. This demonstrates that even when much of the complexity is removed – like differences between providers and many of the features of the product – individuals still struggle to navigate decisions.

Many financial decisions involve a far more complex decision-making process. We've argued that to keep people engaged, we need to address their own criteria for well-being. These criteria may be more subjective than economically rational. The issue is not that their priorities are flawed, the issue is more that they may not understand the long-term financial consequences of those decisions.

Individuals need ways to map their overall objective to their financial decisions so that they have a context in which to place them. In many cases, a financial product is not the only way to solve a specific problem. Alternatives exist that may be social, for instance. The implication is that by balancing financial and alternative strategies, there may well be opportunities for individuals to stretch their money further.

As product complexity increases, it becomes harder for individuals to navigate such decisions. Where possible, this complexity should be avoided and where unavoidable, it needs to have tangible benefits for well-being.

In the sections that follow, we look at several types of financial decisions – about choices relating to insurance, medical aid, savings and investments and even how to manage the inevitability of death. We place them in the context of the overall problems that people are trying to solve with financial products and then look at the alternative strategies available. Then we look at what types of considerations an individual could look at to navigate what strategy makes the most sense for them.

While these sections target the individual decision-making process, they are not aimed specifically at the individual. The purpose is to illustrate how an understanding of Understanding the trade-offs well-being informs the kinds of guidance and models that can be used. Too often the instinctive reaction for financial services is to point people towards more products and this is not always the answer that will best serve an individual's financial well-being.

Instead, by placing decisions in a broader context, it becomes easier to discern whether a problem is best solved by a formal insurance product, by saving, by a social strategy or an adaptation strategy, or some mix of these. Acknowledging the full range of strategies allows individuals to better deploy their finances in a way which reflects what matters most to them. More importantly, it helps them manage the inevitable trade-offs that come from knowing that the resources available to any individual or family are limited.

We can no longer continue advising individuals on the basis that financial decisions are treated as stand-alone problems. Financial decisions fit into a broader context – of both objectives and strategies – and incorporating these aspects can only enrich our ability to advise individuals appropriately

Article tags

[FINANCIAL WELL-BEING](#)

[UNDERSTANDING TRADE-OFFS](#)