

WEALTH & INVESTING



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By Raluca Filip

Beyond risk profiling: Overcoming biases to become resilient investors

Advisors must recognise and coach clients through the emotional biases that distort investment preferences

THE purpose of risk profiling is to match an investor's portfolio with both their ability and willingness to take risk. But "willingness" isn't stable. It shifts with markets, headlines, and emotional reactions. It also varies depending on how a question is phrased in the risk-profiling survey.

That's why advisors should not stop at assessing risk preferences. To make risk profiling useful, they must also recognise and coach clients through the emotional biases that distort those preferences.

I first encountered the critical distinction between risk tolerance and risk attitudes in Michael Pompian's *Behavioral Finance and Wealth Management*. His explanation, that true risk tolerance is a stable, personality-based trait, while risk attitudes are volatile and emotionally driven, was both revelatory and practical.

Yet it was only years later, after training in coaching, that I fully understood how emotional bias can be addressed, and how language can reshape what a client perceives as their "willingness" to take risk.

Understanding the trio: risk capacity, tolerance, and attitudes

Most advisory frameworks adjust portfolio recommendations when there's a mismatch between risk capacity (what the investor can afford to lose) and risk tolerance (what they're emotionally comfortable withstanding).

And here's where it gets nuanced. While both determine an investor's overall risk appetite, it is essential to distinguish between actual risk tolerance and behavioural risk attitudes.

Risk tolerance refers to a client's *stable* preference for risk. It reflects the client's enduring preferences about risk, often grounded in experience, values and life stage.

Behavioural risk attitudes are *unstable* and highly context-dependent. They reflect short-term reactions to volatility, recent losses or market headlines. While real, they are often poor guides for long-term decisions.

When risk appetite falls short of risk capacity, the advisor's job is not simply to reduce exposure. It is to understand if there have been any emotional triggers that might be contributing to



While both determine an investor's overall risk appetite, it is essential to distinguish between actual risk tolerance and behavioural risk attitudes. PHOTO: PEXELS

that low-risk appetite, and address these triggers. Allowing these unstable attitudes to dictate portfolio design risks producing an emotionally "comfortable" solution today that could fail the client in the long run.

Coaching investors through common emotional biases

Advisors often see the same emotional patterns play out when markets shift.

Here are some of the most common biases and ways to reframe the conversation so clients can stay grounded in their long-term strategy.

■ Loss aversion

Investors often say: "I can't afford to lose anything right now," or "I should pull my money out until things calm down."

A more helpful frame: The real risk isn't just losing money; it's missing the growth that secures future goals. The question becomes, "Are you trying to avoid short-term discomfort, or are you aiming for long-term financial security?"

■ Overconfidence

Investors may say: "I've got a good feeling about this sector."

A more helpful frame: A strong instinct de-

serves a strong process. Even good calls benefit from strategy. The question is, "What would this decision look like if we stripped out the emotion and focused only on the data?"

■ Self-control bias

Investors may say: "I know I should invest more, but I just haven't gotten around to it."

A more helpful frame: "You clearly care about your financial future. How does delaying investing align with that priority?"

■ Status quo bias

Investors may say: "Let's leave things as they are for now."

A more helpful frame: Sometimes standing still is the riskiest move. Ask, "What happens if nothing changes? What opportunities are lost by waiting?"

■ Endowment bias

Investors may say: "I've had this stock for years, it's been good to me."

A more helpful frame: "If you didn't already own it, would you buy it today?" Explain that honouring past success might mean taking profits and reinvesting wisely, rather than holding on out of habit.

■ Regret aversion

Investors may say: "What if I invest and the market drops tomorrow? I don't want to make a mistake I'll regret."

A more helpful frame: Diversification helps protect capital while still moving forward. "Think of it this way: refusing to plant seeds because it might not rain tomorrow means missing an entire growing season."

From profiling to partnership

Advisors today must do more than understand markets; they must help clients navigate their own internal markets.

Providing behavioural finance resources can help, but the greatest impact comes from the financial advisor who can respond in real time with empathy and perspective. Emotional biases are not flaws to eliminate; they are facts of human nature. The difference lies in whether those biases dictate portfolios or whether advisors coach clients to see beyond them.

By aligning risk attitudes with true risk capacity, advisors can help clients become resilient investors rather than reactive ones.

The writer, CFA, PRM, is a decision-making coach and trainer who works with leaders and institutions to sharpen critical thinking and align decisions with long-term goals. Her investment background of more than 15 years includes risk management, equity analysis, and fund management.

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