Life differences make women less risk tolerant when investing

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Prior research has long shown that women are, on average, less risk tolerant in their financial decisions than men. This is a concern as investors with low levels of risk tolerance might have greater difficulty reaching their financial goals and building adequate retirement wealth because they are unlikely to invest in stocks. Now, a researcher from the

University of Missouri has found that men and women do not think about investment risks differently. Instead, income uncertainty affects men and women differently, which leads to differences in risk tolerance.

"Risk tolerance is one of the most important factors that contributes to wealth accumulation and retirement," said Rui Yao, an associate professor of personal financial planning in the MU College of Health and Environmental Sciences. "It is important to understand what causes women to be less risk tolerant so that financial planners can better serve their needs as women, on average, live longer than men and often need more retirement savings."

For her study, Yao examined data from the Survey of Consumer Finances. The survey is conducted every three years and supported by the Federal Reserve and U.S. Department of the Treasury. By analyzing data from nearly 2,250 unmarried American individuals, Yao found that women are more likely to have uncertain incomes from year to year. Life events such as child birth, child care and care-giving often contribute to women's income uncertainty.

Yao also found that, on average, women had lower net worth than men. This may have resulted, in part, from women keeping funds in accounts with low returns to buffer the risk of negative income shocks.

One-quarter of women and one-fifth of men in the sample reported using a financial planner for saving and investment decisions, but the advice given to women may not be in their best interest. Yao suggests that financial planners need to understand the differences in income uncertainty and net worth between men and women and the way in which these differences relate to risk tolerance.

"Simply telling women to be more risk tolerant is ineffective," Yao said. "In fact, it might encourage women to take more financial risks than they can tolerate, which could lead to more problems in the future. The difference in investment advice received by men and women requires further investigation, particularly given the new fiduciary standards for financial advisors."

Yao's advice to women is to plan for income uncertainty by creating a financial strategy that fits their needs. For example, when anticipating child-rearing or care-giving periods in the near future, women can and should be more conservative in their investing. When those periods are coming to an end, women should work with their financial planners to make riskier investments.

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