Investing in Yourself (Even When It Seems Irrational)

A couple years ago I read an article about a new online brokerage firm that was geared towards young people called Robinhood. It sounded intriguing so I opened up an account to give it a test run. The great thing about Robinhood is that all trades are commission free.

I trade infrequently but I'm always looking for ways to cut costs and it's pretty tough to find a better deal than $0. Trades are done through an app on your phone and the whole thing is very intuitive.

It sounds like I'm not the only one who likes the platform. According to a story at Fast Company yesterday Robinhood now has over 2 million users. Charles Schwab has more than 10 million brokerage accounts while E-Trade has 3.5 million. Considering Robinhood was launched in 2014 that's an unbelievable market share gain. The other neat thing about their story is the median age of their clients is just 28 years old.

The business model of allowing free trades doesn't seem to make much sense but they make up for it through a $10/month subscription service that allows users to trade on margin (just $2,000 of borrowed capital so not that much is allowed) and they also make money on the interest rate float on the cash in their users accounts.

The young founders of the company have big aspirations beyond the brokerage business:

Bhatt and Tenev, however, have an even loftier vision. As they see it, Robinhood's current iteration as a "Buy Stocks" button on users' home screens is just phase one. "Anything that you would be able to get walking into your local Bank of America branch office, you should be able to get faster, better, cheaper, with a much better user experience, from Robinhood," says Tenev.

There are, however, some downsides to the service:

Robinhood's detractors wonder if the company is, in a way, too good at communicating with users. Active customers check the Robinhood app 10 times per day, on average, often in response to push notifications. "Is it ethical to get people addicted to these bottomless wells?" says Lex Sokolin, global director of fintech strategy at the consultancy Autonomous Research, who likens Robinhood to apps like Instagram and YouTube, where the stream of content never ends. "Here you're not only using people's time, you're also putting their money at risk." Other experts caution that individual investors would be better off taking a passive approach to wealth management and parking their money in diversified index funds. After all, academic research suggests that less than 5% of people have the skill to beat the market.

I'm torn when I see stats that show users checking their accounts 10x a day. The financial blogger in me wants to scold these young investors and teach them how damaging it can be to constantly check your investments. But the realist in me sees this as a net positive development.

Almost 80% of Robinhood's users are under the age of 35. Getting young people interested in saving, investing and the stock market is no easy task. Even if these young investors lose their shirt by over-trading, using borrowed money or checking their performance too often, at least they're saving money. At least they enjoy paying attention to the stock market. This is a good thing.

A few of them are bound to get lucky and make some good money but even the ones who make huge mistakes with their capital are still far ahead of their peers who shun the stock market. Sometimes you have to pay your tuition to the market gods before you come around to the understanding that short-term trading is best left to the professionals (and even then it's an uphill battle).

You have to invest in yourself to get ahead in this world. That could be through losing money, taking the time to learn or simply spending more better yourself.

Last week there was a story by Jason Gay in the WSJ that discussed the changing landscape of working out. People are switching from large gyms, which don't cost very much, to smaller boutique gyms, which are much more expensive. These specialized gym memberships can cost in upwards of $200/month or $30 for a single class. On the surface this seems wildly irrational.

Why would you pay so much for a gym membership when you can just go for a run or buy free weights or do push-ups on your own?

And if we were all perfectly rational beings who have no behavioral flaws whatsoever it would be irrational to pay so much for a workout class.

But...

WE. ARE. NOT. RATIONAL.

How many people do you know who want (need) to get in shape but don't because they just can't force themselves to go to the gym? How many people do you know who get a gym membership in January, go for a couple weeks and then never go again for the rest of the year (while still dutifully paying their membership dues as if they'll return some day)?

Many of us need a psychological sleight of hand to force ourselves to get in shape. Here's how Gay puts it:

The Big Gym You Never Went To is under siege from The Tiny Gym You Actually Go To.

It makes sense. In exercise, as in weddings, 50% of success is just showing up. And specialized fitness—CrossFit, SoulCycle, Orangetheory and their countless cousins—is a far more effective workout than wandering into a gym, sitting down on a recumbent bicycle, and pedaling slowly while *reading Facebook on your phone.*

Maybe some of the young investors using Robinhood will blow themselves up with their constant trading and performance check-ups. But at least they're showing up to invest. I'm guessing (hoping) most of them will eventually learn solid investing habits along the way by first learning what doesn't work.

Sources:
How the Brokerage App Robinhood Got Millennials to Love the Market (Fast Company)
How Much Will You Pay For That Body? (WSJ)

Further Reading:
When Knowledge is Useless