MarketWatch

As Robinhood IPO nears, critics say app design includes ‘subliminal messages’ to make users trade more

Chris Matthews

March 25, 2021

Regulators must decide how aggressively to police mobile trading apps

As the online brokerage Robinhood prepares for its IPO, the company must contend with a new push by lawmakers and regulators to examine its user interface after critics have alleged that the company employs techniques that cause users to trade more often than is in their financial interest.

“Robinhood seems to have perfected the gamification of trading, providing the user with the perception that investing through the app offers recreational game playing with little or no downside risk,” said Rep. Nydia Velazquez, a Democrat from New York, during a Financial Services Committee hearing last week, echoing the concerns of other Democrats who’d like to see stricter regulation on application interfaces so they don’t manipulate users into trading more frequently than they otherwise would.

Read more: Robinhood back in Capitol Hill spotlight amid surge in GameStop shares

But Robinhood and its supporters contest the notion that the application utilizes gamification techniques at all. Robinhood did not respond to requests for comment for this story, but spokesperson Jacqueline Ortiz Ramsay told MarketWatch last week that the term gamification is vague and that those using it are “short on details” when they do try to define it.

“What’s more, when you look at traditional and newer brokerage firms across the industry, you’ll find similarities: some have confetti, some show most traded stocks,” she added. “But when you consider what gamification actually means, it includes elements like badges, leaderboards, points or other forms of competition. These are elements Robinhood does not have. So it’s a bit of a stretch to say that a modern interface somehow equates to gamification.”

Vicki Bogan, an economist at Cornell University’s Dyson School of Applied Economics and Management and founder of the Ithaca, N.Y., university’s Institute for Behavioral and Household Finance, told MarketWatch that the term gamification can be confusing and encompasses more than an application encouraging forms of competition. “When we talk about these online brokers engaging in gamification, it’s really a situation where they’re setting up their user interface so they can try to exploit natural tendencies and biases to maximize the number of trades,” she said.

She pointed to Robinhood’s use of push notifications that pop up on users’ phones when a stock they own moves more than 5% or when there’s breaking news about a stock as ways the app gets users to engage with it. The more users engage, the more they will trade, and the more revenue Robinhood will earn, she argued.

Robinhood makes the majority of its revenue from payment for order flow, whereby market makers pay Robinhood for the privilege of executing its customers' orders.

Other features of the app that could be seen as encouraging more trading are graphical confetti appearing on the screen when a user makes his first trade, or design elements within the app that make it less likely a user will cancel a trade than proceed with it when asked to confirm the decision.

Dennis Kelleher, CEO of Better Markets, a nonprofit organization that argues for stricter oversight of the financial-services industry, went further, arguing that everything from the user-experience design to the colorful nature of the app to its lists of most popular stocks should be investigated by the Securities and Exchange Commission and the Financial Industry Regulatory Authority, or Finra.

"Regulators need to unpack the subliminal messages that are built into the app that cause people to unconsciously and thoughtlessly do things that they would not do if they had the space for deliberate consideration," he said.

Those in the online brokerage industry are quick to point out, however, that any blanket ban on gamification by regulators could also ban practices that encourage investors to engage in healthy investment behavior. For instance, the trading platform All of Us Financial uses gamification techniques to reward customers who reduce their portfolio risk.

Stephen Mathai-Davis, founder and CEO of the investing app Q.ai, said that a company's overall business model matters more than whether or not it uses gamification techniques. His firm charges a monthly subscription fee that enables users to invest in one of many trading strategies and doesn't earn money per transaction as Robinhood does.

"Robinhood — they've done a good thing by democratizing finance. If you go back over 10 years it was really hard to invest," he said. "It's not the app design itself that's causing the issues; it's the engagement strategies."

Matthai argued that Robinhood's practice of giving away free low-cost stocks to first-time customers could encourage users to invest more in penny stocks, which can be very risky. "It's gone a little too far where nobody is thinking about risk," he said. "I think it's great that Robinhood has made options trading easy, but is there any education being done?"

Jennifer Schulp, director of financial-regulation studies at the conservative Cato Institute, argued against sweeping new rules that would dictate how trading apps' interfaces can operate. She noted that the SEC and Finra already have rules governing communication between brokers and clients, and that Finra announced in February it would be investigating mobile-application design to determine whether app-based brokers are complying with existing regulations.

“Caution is definitely warranted here not only because gamification can have beneficial outcomes in investor education but also because we are talking about a very broad range of design elements, and we should not be imposing artificial regulatory hurdles to prevent people from having an efficient, happy, enjoyable user experience,” she said. “It’s not in anyone’s interest for the SEC to be regulating how much confetti is too much confetti.”