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Linking self-esteem with the tendency to engage in financial planning

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ABSTRACT

A strong positive relationship between self-esteem and an individual's decision to engage in various forms of financial planning is empirically demonstrated using a unique data sample. These results yield interesting implications for the possible effect of self-esteem interventions on financial planning choices and pave the way for future psychological and economic research in this area.

1. Introduction

The present analysis is motivated by the following question: When an individual has a relatively lower level of self-esteem, does he or she block out information on personal finances in order to decrease the possibility of distress (a form of psychic cost)?[1] In other words, does this individual attempt to safeguard himself or herself against possibly negative information and distress by an avoidance of tracking his or her finances?[2]

The theoretical model and results presented in this analysis are in keeping with the idea that low self-esteem individuals do indeed misrepresent their environment due to a failure to be cognizant of and to track their finances.[3] This result is in keeping with the notion that high self-esteem individuals are more perseverant in the face of defeat, with a tendency to continue their efforts after failure rather than admitting defeat. It would follow that low self-esteem individuals, by trying to block out information from their environments that could represent a failure, may be acting to safeguard themselves from possible defeats from which they will have a harder time recovering psychologically.[4]

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[1] Distress could be represented by rates of depression or unhappy realism, both more likely in the lower self-esteem individual. See Butler, Hokanson and Flynn (1994) and Campbell and Fehr (1990).

[2] For a discussion of the literature and relationships between self-esteem and emotional decision making see Rawn, Mead, Kerkhof, and Voh (2007).

[3] In a sense, this is in keeping with the notion that lower self-esteem individuals are actually "less" in tune with their environments in representing and filtering reality correctly. See for example Campbell and Fehr (1990).

[4] Opinions vary as to whether higher self-esteem causes individuals to persist "optimally" or for too long in the face of defeat. Regardless, there appears to be relative agreement that higher self-esteem individuals do persist in the face of failure. See for example McFarlin (1985) or Di Paula and Campbell (2002).

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The empirical portion of the analysis uses a Rosenberg-type self-esteem measure, i.e. self-esteem is empirically conceived of as a sense of self-worth and hence a positive or negative attitude towards one self. This definition of self-esteem has also been the most prevalent historically with approximately one-fourth of empirical studies on self-esteem at present employing the Rosenberg scale (Mruk, 2006).[5]

While the theoretical interpretation employed here is in keeping with the empirical results, it should be noted that data restrictions make it unclear as to whether the documented relationship is in fact definitively causal, and the size of endogeneity and selection issues in the analysis.

One particular issue is the possible relationship between self-esteem and socioeconomic status, with better financial planning causing an individual to have more money and hence experience a rise in self-esteem. While I cannot strictly rule out this interpretation, I am able to control for the factor of height which should have a correlation with SES as well as serving as a proxy for multiple other lifelong indicators such as sociability, health, cognitive ability and optimism.[6] Height itself will also be predictive of self-esteem as well as correlated with other variables important in the self-esteem relationship. A relationship between self-esteem and financial planning after controlling for height thus implies that the self-esteem–financial planning relationship has been cleaned of portions of such factors as cognitive ability and the perceptions others have of one's success which would operate to affect self-esteem through their relationship with height.[7] I additionally employ age and gender as well as several other important control factors as discussed in detail in the data analysis section. In the future, it will be fruitful to extend the current analysis to use formal tests for endogeneity that build upon the current initial work which paves the way for research on the link between self-esteem and financial planning.

One final point I would like to address is the concern that the self-reported nature of survey data and its relationship with self-esteem will make it possible that any observed empirical relationship is biased by over or underreporting conditional on the esteem of the individual in question.[8] I will first note that recent research on self-reports vs. other reported data has shown support for the use of self-report data.[9] I will also note that several different measures of financial planning were used in determining whether individuals are more likely to engage in financial planning and results from all measures were consistent in showing a large and significant relationship between self-esteem and financial planning. This consistency implies that if misrepresentation is a problem, it is invariant to measures used, or else the true positive relationship between higher self-esteem and higher financial planning has indeed been captured.

As Mruk (2006) points out, self-esteem is perhaps one of the most popular topics of research today, and findings in this area have varied greatly. Some recent meta-analysis has shown that most of the correlational results do not represent a causal relationship between self-esteem and the factors of interest.[10] The current analysis, by considering information of financial planning as a psychic cost mediated by self-esteem, adds an interesting and entirely new dimension to the study of self-esteem, thus providing a basis for future research and development.

2. Data

In this paper, I use a selected subset of the population composed of individuals who took the Emode or Tickle popular online tests during the years 1999–2005 to test for a relationship between self-esteem and the tendency to engage in financial planning.[11] The analysis reveals important patterns for individuals prone to taking these online tests. This type of individual constitutes an increasingly large fraction of today's population as evidenced by the fact that over 2 million individuals took one of the personality tests included in this analysis.

Three variables are chosen as representative of a person's use of financial information and involvement in the financial planning process. Specifically, I test for a relationship between the level of self-esteem and a person's likelihood of (1) planning retirement ahead of time, (2) keeping track of their budget, and (3) keeping track of their credit card charges.

[5] Kernis (2006) contains a series of papers employing a similar breakdown and structure to the one explicated here. As mentioned above, the Rosenberg self-esteem is used in the present analysis rather than the alternate popular measure of "self efficacy." Although the efficacy measure has been used in some situations for individuals of this age group, notably in a paper by Froman and Owen (1991) examining how high school students' perceptions of self-efficacy are related to various measures of health, in the current analysis it is not the best choice.

[6] For more on the significant and clear relationship between height and income see Mankiw and Weinzierl (2010), Judge and Cable (2004), Persico, Postlewaite and Silverman (2004), Case and Paxson (2008). Korniotis and Kumar (2009) present the case for using height as a proxy for multiple indicators of lifelong experiences.

[7] Korniotis and Kumar (2009) discuss this issue at length for the very appropriate issue for the case at hand since they are looking at portfolio choice.

[8] See for example Campbell and Fehr (1990).

[9] See for example Paunonen and O'Neill (2010).

[10] See Baumeister, Campbell, Krueger and Vohs (2003).

[11] Tickle Inc., was a media company, formerly known as Emode.com created for the purposes of social networking services. This website provided online test-taking capability. Tickle was immensely profitable at the beginning of the current decade after surviving the dot com bubble burst in 2000. Tickle was taken over in 2008 by Monster Worldwide and Tickle began shutting down its site in 2008. In 2009, a new form of tests is currently available on the Monster network which includes a revised subset of the personality and IQ tests formerly available on Tickle.