



WHAT IS THE RELATIONSHIP BETWEEN SPENDING AND FINANCIAL WELLBEING?

Key findings from a rapid evidence review

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Standard Life Foundation commissioned the University of Edinburgh Business School to conduct a rapid evidence review to understand the determinants of people's spending behaviour and how it impacts their financial wellbeing. This involved a structured, critical analysis of around 130 relevant items and an assessment of their methodological strengths and weaknesses.



KEY FINDINGS

- There appears to be a link between spending and overall financial wellbeing, with lower spending associated with higher financial wellbeing. However, the exact nature of this link may depend on how financial well-being is measured.
- It is possible to identify a number of determinants, particularly personality traits such as conscientiousness, to spending behaviour.
- The effects of such determinants on spending will be modified by the specific situation (for example, who else is present). Some determinants, such as materialism and behaviours associated with it, were also associated with compulsive spending. Impulsive spending may be more linked to situational factors.
- Evidence on how these determinants are distributed across the population is mixed, but greater spending restraint may be more common in men and older people.
- Poorer control over spending is linked to materialism and status-seeking, along with impulsivity and low self-control.

About the study

The purpose of this evidence review is to examine the evidence relating to spending and financial well-being. We use the term financial well-being to refer to what results from people's financial knowledge, skills and behaviours, giving an objective and subjective assessment of their financial status. The review focused on five key research areas:

- The impact of spending on financial well-being
- The key determinants of spending
- The key determinants of compulsive, impulsive and over-spending
- How the determinants of spending are distributed across different demographic and socio-economic groups
- The determinants of better or poorer control over spending.

It looked at various types of evidence, including experimental studies, qualitative studies and conceptual work, and drew evidence from a wide range of disciplines. Most of the evidence came from quantitative studies such as large-scale surveys. In total, 134 sources of evidence were reviewed. These came from a variety of different disciplines and therefore do not represent a coherent narrative on spending and financial wellbeing. It is worth noting that different definitions of financial well-being, along with differing terms such as financial health and financial capability, were found in the evidence reviewed. The limitations of this review are generally in the form of availability of relevant evidence, so it should be noted that relatively little empirical evidence was found that linked spending to financial well-being and that it would therefore be useful for more work of this type to be carried out.



KEY FINDINGS

What is the impact of spending on financial well-being?

The evidence indicates a link between people's spending and their financial well-being, with lower levels of spending associated with greater financial well-being, even when social and demographic factors (such as age and income) are controlled for.

What are the key determinants of spending?

The possibility of personality traits being determinants of spending behaviour was examined, including conscientiousness, extraversion, materialism (placing great importance on material items) and control/self-control. Conscientiousness was shown to predict money management, and was linked to more positive attitudes around money and a focus on finances in the future. Extraversion was linked to higher spending. Having a high level of materialism was related to higher spending, including on necessities. Interestingly, higher materialism has also been linked to lower satisfaction with purchases, a feature of compulsive spending, which is discussed below. Traits related to control, including self-control and impulsivity-control, were found to be negatively associated with spending, i.e. the more control a person displays, the higher their spending restraint.

Spending may also be influenced by stress and a sense of financial self-efficacy—the belief that one's financial circumstances are within one's control. One study detailing a series of experiments indicated that while certain types of stressful situations were associated with a preference for saving more, others were associated with increased spending on unnecessary items. One study showed that good financial management was impacted by a belief that a person's financial situation is largely due to external factors.

Spending also seems to be affected by peer-groups and other groups that individuals may compare themselves to. This may be particularly true for socially-excluded individuals who spend in line with group tendencies to achieve a sense of group affiliation, although this finding is based on one study with a non-representative sample. Conversely, the presence of family may have a constraining effect on spending.

There are also some behaviours that were linked to spending. Three studies showed that the use of mental accounting and budgeting are positively associated with a lack of spending restraint, perhaps contrary to expectations. It was suggested that these behaviours can lead to underspending, with leftover sums seen as a windfall to be spent freely. More intuitively, evidence suggests that reductions in income lead to reduced spending.

What are the key determinants of compulsive spending, impulsive spending, and over-spending?

There was a limited amount of evidence on this topic, so in most cases findings are based on only one or two sources. None of these were based on people in the UK. Issues of compulsive spending—where an individual spends money on items without deriving pleasure or other benefit from their purchases—have been shown to be moderated by self-control, frugality and effective money management (such as budget-setting), the latter of which having been linked to conscientiousness. People with high self-control are less likely to engage in compulsive buying and less likely to get into debt. Those who see themselves as frugal or employ money management strategies are also less likely to spend compulsively.

Impulse buying, on the other hand—where an individual tends to make unplanned purchases—is likely to be influenced by situational factors like social influence. Social influence may be in favour of the purchase, in which case the impulse purchase is more likely to be made, or against the purchase, which reduces the likelihood of purchase. The combination of situational factors and a disposition towards impulse buying seems to have the greatest influence on impulse buying, rather than any one factor alone.

How are these determinants of spending distributed across the population?

Age and gender appear to be related to spending and some associated behaviours. Males and older people appear to be better at controlling spending whereas females tend to be better at keeping track of spending. The apparently contradictory findings around females' spending and keeping track of money perhaps echoes the finding stated earlier around use of budgeting techniques and increased spending.

There is some evidence that younger people are more prone to making impulse purchases. In general, however, evidence around specific demographic factors (such as age) and spending was not strong. In all cases the relationship between demographic factors and determinants of spending may be affected by country and culture, and there were few studies that were of sufficient scale to draw firm conclusions about different sub-groups within the population studied.

What are the determinants of better or poorer control over spending?

Similarly to the determinants of spending, individual factors that appear to be linked with poorer control over spending are: being high in materialism, impulsivity and having low control. Materialism has also been linked to an increased tendency to spend overall. Impulsivity refers to a person's tendency to act spontaneously. Control of impulsivity has been linked to other aspects of self-control (such as the degree to which people tend to feel their situation is determined by themselves or by external factors) which studies have found to be a determinant of better control over spending.

The tendency towards behaviours aimed at attaining a certain social status and the related issue of conspicuous consumption are also linked to poorer control of spending.

There is some evidence from interventions to improve control over spending that suggests it might be possible to improve spending habits, mainly through financial education (including training classes and behavioural nudge interventions). Seven studies were identified that looked at the effect of interventions which were generally based around financial education and not focused specifically on improving spending. While these studies tended to show an improvement in spending, only one used a comparison group and long-term changes were not examined, so the evidence is not strong.

In an age rich with payment options, an area ripe for research is that of how one's chosen or habitual method of payment affects spending patterns. As might be expected, it seems that using a credit card is associated with higher spending and those using cash tend to spend less, although it is not clear whether this is due to the planning of purchase methods according to intended purchases, or other factors. More research would be useful on spending methods such as contactless payment.

The relationship between spending, borrowing and saving in relation to financial well-being

While few studies have looked at the relationship between spending, saving and borrowing, the review found some evidence that lower levels of individual spending were often associated with higher levels of saving behaviour or lower levels of borrowing. The relationship between spending and saving may be moderated by stress, with one study showing that increased saving can be used as a means to gain a sense of control in some situations, and increased spending used to reduce stress in others.

Recommendations

This review has shown that there are some significant gaps in our understanding of problematic spending and its determinants. Moreover, much of the existing research used small sample sizes and/ or is focused on specific cultural contexts that cannot be generalised to the UK.

There is a real need for UK-based quantitative research that explores in detail the wide range of potential influences on aspects of problematic spending, including various demographic factors and incorporating data on participants' actual spending. This would require a large sample in order to allow for generalisation to the population and comparisons between different groups within the population. To complement this it would be very valuable to create a rich picture of actual spending habits and motivations through qualitative research. This will help us to better understand the reasons for some of the findings, such as the link between mental accounting and spending and would ideally include some work capturing information over a period of 12 months or more.

In addition, there is scope to make more use of emerging data sources as a result of Open Banking, using real financial transactional data.

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