



Moods and Money: How Emotions Affect Money Decisions

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How do you try to relieve the stress of a bad day on the job? How about that down-in-the-dumps feeling due to emotional issues in your life? Or even the melancholy you feel on a cloudy day? Many of us head to the mall for some retail therapy.

The study of behavioral economics, which includes how our emotional state affects our financial decisions, is a newer field that looks at the role that moods and emotions play in the decision-making process. In their book, *Why Smart People Make Big Money Mistakes and How to Correct Them: Lessons from the Life-Changing Science of Behavioral Economics*, authors Gary Belsky and Thomas Gilovich point out that consumer buying behavior often is based on reflexive financial thinking, rather than rational thought. Those of us using this reflexive thinking may spend money in impulsive bursts, and spend more for goods and services than we planned to. Our rational decision-making process regarding purchases has been impaired due to our emotional situations. Therefore, we make financial choices based on a need to uplift our moods, rather than on a logical need for the purchase itself.

If we as adults behave this way due to our rollercoaster of emotions, can you imagine how kids might feel and react in similar situations? Young children usually lack the emotional strength that adults have developed to help

them resist temptation and delay gratification. So when things don't go their way in life, kids can easily choose to go down the “buy it to feel better” path. A case in point might be that a child is tired of shopping in mom's favorite stores, and demands to buy something—anything—for himself. The item can be totally unnecessary, but the child's mood is lifted by the purchase and he is pacified. We've all been there, right?

Fortunately, there are ways to combat the behavioral tendency of buying to soothe our emotions. Once we learn these techniques and share our financial plan of action with kids, we can teach them a more logical way to react when their moods begin to take over. Here are some tips to make emotion-free financial decisions:

- Use a mental or written decision process to see if a purchase makes sense (Try our decision-making suggestions on page 18). Does the item satisfy a need? Is it important to buy it at this time? Is it affordable?
- Plan for temptation and know how to resist it. How will you handle yourself when you run onto the sale of the century? Make a plan to help you back away from an impulse purchase.
- Think of the opportunity cost of spending your dollars on a particular item. If you decide to buy it, what other good or service are you giving up? In kid terms—the toy you buy today will keep you from the video game you want tomorrow.
- Use a 24-hour rule before buying. Enforce a waiting period of at least one day so you can logically think about the potential purchase.
- Don't follow the herd. Just because an item is new, trendy or sought after, it doesn't

mean you have to make it yours today.

It's important to practice these behavioral techniques once you have shared them with your young shoppers. So take them to the mall as soon as they have some cash that's burning a hole in their pocket. Remind them of ways to keep on track if they suddenly develop the urge to splurge.

Behavioral economics can also be used to ingrain some important financial lessons you'd like kids to learn. Try using the concept of loss aversion, which says the pain of losing is twice as strong as the pleasure of winning. Instead of saying, "You should save your money in the bank," try, "You're losing money (interest on

funds) by not saving in the bank." This idea could spur them into depositing dollars on a regular basis.

One more behavioral economic concept to remember is default outcome, which is the tendency to be passive in changing any behavior. So push yourself into action to share these methods with kids to help conquer emotional spending.



Financial Education Resources

The Kansas City Fed is committed to promoting economic and financial literacy and greater knowledge of the Federal Reserve's role by providing resources for teachers, students and the public. Visit our website at KansasCityFed.org for more information. The resources below are a few of many available on this subject.

FEDERAL RESERVE RESOURCES

Once Upon a Decision Online Course for Consumers

<https://bts.stlouisfed.org/decision-making-elem/?p=yes>

Ella learns to make better decisions in her life by using a decision-making grid. For ages 5-8.

On the Court with Michael Jordan by Matt Christopher

http://www.stlouisfed.org/education_resources/assets/lesson_plans/MichaelJordan.pdf

This book describes the many decisions Michael Jordan made throughout his basketball career. The accompanying lesson highlights human capital and how to make logical choices.

For ages 9-12.

FICTION BOOKS

The Berenstain Bears Get the Gimmies

by Stan and Jan Berenstain

The bear cubs want everything in sight when they go shopping. Mama and Papa Bear teach them about the family budget and the importance of appreciating what they have.

For ages 3-7.

NONFICTION BOOKS

Financial Peace Junior

by Dave Ramsey

This kit gives kids a hands-on way to handle money and make financial decisions. For ages 6-12.

Why Smart People Make Big Money Mistakes and How to Correct Them: Lessons from the Life-Changing Science of Behavioral Economics

by Gary Belsky and Thomas Gilovich

This book looks at ways we spend, save, borrow, invest and waste money. Case studies illustrate common patterns of thinking and show readers how to protect and grow their assets.

For Adults.

Activity: How do I decide

It's not easy to make good decisions on how to spend your money

Try the ideas below to help you make better spending choices.

Take the decision quiz before making a purchase, but be honest. If you can answer "true" to four out of five statements, BUY IT!

- | | | | |
|----|--|------|-------|
| 1) | I need this item for my daily life. | TRUE | FALSE |
| 2) | I can't substitute anything I already have for it. | TRUE | FALSE |
| 3) | It's necessary to buy it today. | TRUE | FALSE |
| 4) | I'm not buying it because my friends have it. | TRUE | FALSE |
| 5) | I can afford to pay for it. | TRUE | FALSE |

Use the following tips to help you resist the urge to splurge. Add a new tip of your own.

Say "I won't buy it today, maybe tomorrow." Repeat three or more times.

Turn away from the item and walk to a different part of the store.

_____ (Your tip here)

List three items that you would like to save your money for. These are your savings goals.

Think of one or more of your goals when you are tempted to spend instead of save.

