ASSOCIATION FOR CONSUMER RESEARCH

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Helping Consumers Get Out of Debt Faster: How Debt Repayment Strategies Affect Motivation to Repay Debt

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Effect of debt repayment strategies on motivation to repay debt is examined. Low self-control consumers exhibit greater motivation when paying off their debt accounts sequentially (versus simultaneously). Effect persists whether the strategy is chosen or assigned, is strengthened by a recommendation, is moderated by attainability of getting out of debt.

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Goal-Driven Financial Decisions: Understanding the Role of Consumer Goals in Financial Decision Making

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SESSION OVERVIEW

Reports abound throughout the media regarding a plethora of financial hardships being faced by consumers. Regardless of recent turmoil in various economic markets, a consistent factor contributing to lowered consumer financial well-being resides in the debt repayment and investment decisions consumers make individually. One underexplored question is the role that consumers' goals play in their financial decisions. The purpose of this session is to provide insight into consumers' goal-driven financial decisions and each of the four papers examines a different aspect of this question.

The first paper by Kettle, Trudel, and Häubl reports three studies that examine how debt repayment strategies influence consumers' motivation to repay debt and show that paying down debt accounts sequentially (versus simultaneously) increases the motivation of low self-control consumers, who are most likely to have debt in the first place. The second paper by Gal and McShane analyzes data from a leading U.S. debt settlement company to show that completing discrete debt management subgoals motivates overall goal attainment. These authors find that closing debt accounts early in a debt management program, regardless of the size of the debt accounts, is predictive of eliminating one's debts. The third paper by Salisbury and Nenkov presents two studies featuring US adult consumers, which examine how borrowers' future- versus present-oriented debt repayment goals interact with credit card information disclosures to influence debt repayment behavior and perception of progress toward paying off debt. They find that the effects of repayment goals on perceived progress differ from the effects on repayment behavior, even when accurate goal-related information is provided. Finally, the fourth paper by Cho offers four experiments that provide evidence that setting a minimal, conservative financial goal (vs. high goal) and achieving it leads to a spike in the level of risk taken in subsequent financial decisions due to a persistent loss frame. All four projects included in this session are at advanced stages of completion, and the working manuscripts for all four of the papers, as well as all of the cited references, are available upon request.

This symposium is a model of "appreciating diversity," and therefore embodies the theme of 2012 ACR, because the researchers featured in the session study the role of goals in financial decisions by spanning various theoretical domains, multiple methodological approaches, and sample characteristics. Researchers will discuss lab-based experiments as well as large-scale studies with real US consumers, and actual field debt settlement data to provide insight into consumers' goal driven financial decisions and choices.

Beyond being of interest to academic researchers studying financial decision making and goal pursuit and motivation, the work presented in this session will have important implications for individual consumers repaying their debts, individual investors managing their portfolios, public policymakers, financial services firms, as well as the fiduciaries responsible for structuring financial instruments and investment options in general.

Helping Consumers Get Out of Debt Faster: How Debt Repayment Strategies Affect Motivation to Repay Debt

EXTENDED ABSTRACT

Consumers with multiple debts can choose among different strategies for paying down their debt accounts (Amar et al. 2011). In particular, they can repay their accounts sequentially (one at a time) or simultaneously (allocating the same amount to each account). We propose that paying down accounts sequentially (versus simultaneously) differentially affects the motivation of individuals with low (versus high) trait self-control.

By closing down individual accounts, a sequential strategy enhances the appearance of progress toward the long-term goal of becoming debt-free, and can thus increase goal commitment and motivation (Kivetz, Urminsky, and Zheng 2006). We predict that using a sequential strategy will increase motivation - and thus lead to people becoming debt-free sooner - but only for individuals who chronically lack self-control.

Results from three studies support this prediction. Participants began each study in debt (divided into 5 equal accounts). They earned money in a word-generation task, and had to first pay off their debt before they could keep any earnings. Participants completed 10 performance rounds; accounts were updated after each round.

In study 1, half of the participants were randomly assigned to a debt repayment strategy, and the other half chose a strategy. Low self-control individuals earned more money when paying off their debt accounts sequentially (versus simultaneously) whether they were randomly assigned to a strategy or chose it.

We tested our goal-pursuit account in study 2 by manipulating the amount that individuals earned per word. In the attainable-goal condition (in which all participants were able to get out of debt), we replicated the results of study 1. However, in the unattainable-goal condition (in which it was nearly impossible to get out of debt), debt repayment strategy did not affect the motivation of low self-control individuals.

In study 3, participants received a recommendation for either the simultaneous or sequential strategy (82% followed it). Low self-control individuals performed better when paying off their debts sequentially (versus simultaneously), and they also performed better when they followed the recommendation. Thus, the motivation of low self-control consumers was greatest when they followed the recommendation to repay accounts sequentially.

This research is the first to examine how debt repayment strategies influence consumers' motivation to repay debt. Paying down

debt accounts sequentially (versus simultaneously) increases the motivation of low self-control consumers - precisely those who have difficulty achieving long-term goals (Baumeister, Vohs, and Tice 2007) and are most likely to have debt in the first place (Meier and Sprenger 2010).

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Can Small Victories Help Win the War? Evidence from Consumer Debt Management

EXTENDED ABSTRACT

Globally, consumer debt is measured in the trillions of dollars, with U.S. credit card debt alone amounting to approximately $1 trillion and with U.S. residents, on average, holding five credit cards each (Experian 2009). How best to reduce and eliminate debt is therefore an important question for consumers in a modern economy.

The popular and influential American personal finance guru Dave Ramsey advocates an approach to reducing and eliminating debt that involves paying off small debt balances before larger ones because he believes that paying off the smaller balances can motivate an individual to subsequently pay off the larger balances. Ramsey terms this approach the "snowball method," arguing that consumers need "some quick wins in order to stay pumped enough to get out of debt completely" (Ramsey 2009b,a). Ramsey is not alone in this view, with advocacy of this approach common among consumer financial advisors (Hamm 2007; Think Money, Ltd. 2009).

However, from a normative perspective, the size of the account balance consumers pay off first should not matter to their ability to reduce or eliminate their debt. Rather, consumers should focus on paying higher interest balances first regardless of the size of the account balance (after making minimum payments on all accounts to avoid penalties and surcharges). This approach is thus advocated by the U.S government.

We obtained a highly unique data set that allows us to examine this question on a time horizon measured in years with real world behavior and high stakes consequences for the individuals concerned. In particular, we obtained data from a leading U.S. debt settlement company that allow us to examine the question of whether closing accounts early in a debt management program predicts whether consumers succeed in eliminating their debts independent of the size of the closed account balances. That is, is closing a greater number of outstanding balances early in a debt repayment program predictive of debt elimination regardless of the size of the closed account balances?

Our main finding was that closing off debt accounts—independent of the dollar balances of the closed accounts—was predictive of eliminating one's debts at any point in time during participation in a debt settlement program. In fact, the fraction of debt accounts paid off appeared to be a more powerful predictor of whether or not one eliminates one's debts than the fraction of the total dollar debt paid off, despite the latter being a relatively more objective measure of progress towards the debt elimination goal. More striking still, the dollar balance of closed debt accounts was not predictive of debt elimination when accounting, nominally, for closed debt accounts.

In addition to specific implications for how different forms of goal progress affect goal pursuit, our findings make a more general contribution to research on goals by highlighting possible temporal shifts in the importance of different determinants of goal pursuit in the short run versus the long run. Specifically, whereas prior research has identified important psychological processes whereby attainment of a subgoal demotivates individuals from persisting in pursuit of their goal (Amir and Ariely 2008; Fishbach, Dhar, and Zhang 2006; Khan and Dhar 2006), our research suggests that the impact of these processes might be attenuated over a longer time horizon. Given that many important goals are pursued over long periods of time, our findings call for more research examining how psychological processes affect goal pursuit over long time horizons.

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The Influence of Debt Repayment Goals on Repayment Decisions and Perceived Progress

EXTENDED ABSTRACT

Managing personal debt is an ongoing challenge for many consumers. Average credit card debt amongst U.S. consumers was approximately $6,600 per household in mid-2011. Managing that debt load can be difficult, and it can be very expensive – U.S. consumers paid $94 billion in credit card interest in 2009 alone (Meijer et al. 2011).

A recent study by the U.S. Federal Reserve Bank suggests that many Americans underestimate how much credit card debt they owe, with an estimated 34% gap in aggregate (Brown et al. 2011). This is likely to have adverse effects on the debt repayment goals consumers set for themselves, as well as on their actual repayment behavior. For instance, this gap in perceptions could lead consumers to underestimate the time needed to pay off their debt as well as the amount they will pay in interest, causing them to adopt present-oriented goals and spend more instead of repaying their debt, potentially incurring more debt than they can comfortably shoulder

Public policymakers encourage lenders to disclose loan cost information to enable borrowers to make more informed debt repayment decisions (e.g., the CARD Act). In the current research we examine how the presence of information about loan interest cost and payoff time interacts with consumers' repayment goals to influence debt repayment decisions and perceptions of debt repayment progress.

Two experimental studies, with 570 adult U.S. consumers, examined the effect of repayment goals and loan information on repayment decisions and perceived debt payoff progress. In both studies, participants were shown a hypothetical credit card bill and asked how much of the credit card balance they would repay. Study 1 included three experimental conditions in which we manipulated the loan payoff time information participants received on their credit card bill: 1) only loan balance, interest rate, and minimum payment required information, 2) additional information about how much time it will take to pay off the loan if the minimum required amount were repaid each month, and 3) additional information about how much time it will take to pay off the loan if an amount larger than the minimum were repaid each month. Study 2 used a similar procedure, but had seven information conditions presenting information about either the interest cost participants would incur if the minimum required or some larger amount were repaid each month, and/or loan payoff time information similar to study 1. We further measured whether borrowers had a future-oriented (i.e., pay off debt balance fast to have more money for other purposes in the future) or a present-oriented (i.e., pay the least amount possible to have more money for other purposes in the present) repayment goal. Finally, we assessed participants' repayment decisions as well as their perceived progress toward paying off the loan balance. A series of analyses were conducted to test the effects of goal type and information type, controlling for participants' income, financial knowledge, attitude toward debt, temporal orientation, and credit card repayment habits.

Results indicate that repayment goals had a robust effect on repayment amount. Participants with a future-oriented goal to pay off the balance fast tended to repay *more*, while participants with a present-oriented goal to repay the least amount possible repaid *less*. Interestingly, the negative effect of holding a present-oriented goal was larger when payoff time information was present. The loan cost information and payoff time information manipulations had little direct impact on repayment amount.

Repayment goals also influenced participants' perceived progress toward paying off their loan, and these effects were moderated by the type of information present on the credit card statement. A future-oriented goal to repay the loan balance fast had a significant positive effect on perceived progress, after controlling for repayment amount, suggesting a kind of optimism toward achieving loan payoff. This positive effect on perceived progress was further enhanced by the presence of payoff time information on the credit card bill. This suggests that, while disclosing payoff time information may not increase repayment amount (and therefore speed up loan repayment), it has the potential to increase consumers' perceptions of progress toward paying off the loan. In other words, for borrowers with a future-oriented payoff goal, providing loan payoff time information does not change goal-oriented behavior, but it does change (i.e., increase) perceptions of goal progress.

We found no significant main effects of payoff time information on perceived progress. On the other hand, the presence of loan cost information had a significant negative effect on perceived progress (after controlling for repayment amount); this was the case regardless of repayment goal type. Thus, disclosing loan cost information may lead borrowers to feel more pessimistic about making progress toward loan payoff.

Finally, a present-oriented goal to repay the least amount possible had significant effects on perceived progress, after controlling for repayment amount, but the valence of the effect varied across information conditions. Having a present-oriented goal had a significant *positive* effect on perceived progress in all conditions, except one: when participants were provided with information about the loan payoff time associated with repaying only the minimum each month, a present-oriented goal had a significant *negative* effect on perceived progress. Thus, having a present-oriented goal to pay the least amount possible *decreased* perceived loan payoff progress when time information was present and *increased* perceived progress otherwise.

Our findings regarding the effects of repayment goals and information disclosure on perceived debt repayment progress are noteworthy because past research has shown that perceptions of goal progress (even progress that is illusory and artificial) increase consumers' effort toward achieving the goal (e.g., Kivetz, Urminsky, and Zheng 2006; Nunes and Dreze 2006). We add to this literature stream by providing insight into the differential effects of having present- versus future-oriented goals and receiving time- versus money-related information on perceived goal progress.

A third follow-up study is planned, aimed at clarifying the theoretical mechanisms underlying the effects observed in studies 1 and 2. In this study participants' future- and present-oriented goals, as well as actual progress towards debt repayment, will be manipulated. Perceived progress toward goal achievement, as well and perceived feasibility and desirability of goal achievement, will be measured.

The key contributions from these studies will inform our understanding of how consumer goals interact with information disclosure to influence consumer debt repayment behavior and perception of progress toward paying off debt. These findings have important implications for consumers, public policy makers, as well as for lenders. They are particularly timely given recent legislation (e.g., CARD Act) related to the types of disclosure information that must be revealed to consumers of credit, which often involves the provision of cost- and time-related loan payoff information.

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Consequence of Motivated Goal Setting on Sequential Goals in Investment Decision Making

EXTENDED ABSTRACT

Imagine that you have decided to invest in the financial stocks of emerging markets. Markets have been rather volatile with much fluctuation. Given the uncertainty of the financial markets, you de-

cide that you would be happy as long as it returns a little over what you would get from a bank deposit, and allocate your money into the conservative stocks with low risk. At the year's end you find that your portfolio has done better than the bank rates, but also finds out that many other stocks have done even better, achieving double the rate of return. For the next period, what would be the level of risk you take? Would you take on greater risk? Stay the course with the same set of stocks? Or take on less risk since you achieved your goal? Given how often decisions are made in a sequence of decision periods, surprisingly little attention has been given to understanding investment decisions and judgments within its sequential decision making context.

In this research, we examine the relationship between what we term "strategic goal setting," confirmation of the goal, and the subsequent level of risk taken, in the domain of investment decision making. More specifically, our research investigates the consequence of setting a minimal, conservative performance goal (vs. high goal) on the subsequent target setting for a risky decision when the goal is successfully obtained. Whereas individuals often set lower investment targets assuming they will be happy if only the target is met, this assumption is often unfulfilled because the reference point is no longer the initial goal but a higher, "could-have-been" performance level (Cho and Johar 2011). We predict and find that, due to the upward shifting reference standard, low-goal setters are likely to find themselves in the domain of losses, and become more risk seeking in their subsequent investment decisions. Our hypothesized process model is as follows:

Goal Level → Feedback (confirmed) → Outcome compared to higher reference point than goal → domain of losses → Risk at T2

Across four studies involving investment decisions, we asked individuals to set return goals for their investment portfolios, pick three stocks in a simulated investment task, confirm their goals (feedbacks which match the performance to their return goals), then ask them to set another goal for the next period. Respondents were induced to pick low or high goals via priming tasks (approach-avoidance orientation, delight vs. disappointment) then were told that their investment goals were met for that period (goals confirmed for all conditions), followed by satisfaction measures, then the key measure: target goal for the next investment period. We found that the low-goal setters set target performances that were consistently higher (greater magnitude of increase) than the high-goal setters (studies 1 and 4). This pattern was observed even when the actual performance level was controlled for (studies 2 and 3).

We adopt the framework of prospect theory to conceptualize our finding (Kahneman and Tversky 1979). A central concept within prospect theory is the framing effect: individuals tend to avoid risks when perceiving an outcome as gains or exceeding a reference point, and they seek risks when an outcome is perceived as losses or performing below a reference point. In other words, when one achieves the goal one set out to achieve, or when one's targeted performance has been obtained, this should put the person in a domain of gains. Based on this model, a corresponding prediction would be that on the subsequent risk-taking decision, one would be less inclined to risk the gain already obtained (Heath, Larrick and Wu 1999). In short, confirmation of goal should lead to risk-aversion. We demonstrate that confirmation of goal leads to greater risk seeking in the subsequent decision among those who set conservative goals due to the tendency to upward compare. Because individuals tend to compare their outcome to a higher reference standard, and this upward comparison process creates a loss frame in which the low-goal setter perceives a more intense loss frame than the high-goal setter. Our finding is consistent with the literature on misprediction of future affect and more broadly, lend insight into the topic of unstable risk preferences.

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