common health insurance claims problems.

The Psychology of Saving: A Study of Economic Psychology

Author: **Karl-Erik Warneryd**
Publisher: **Edward Elgar**
Northampton, MA[1]

Reviewer: Jean M. Lown
Human Environments Department
Utah State University

Rather than the current subtitle I suggest "A comprehensive review of the international literature on economic psychology." Written by a professor emeritus of Economic Psychology at the Stockholm School of Economics, this book is densely packed with a lifetime of his own research and that of others from many countries. It provides a comprehensive review of the research literature in a form readily accessible for graduate students. If you teach about saving, want to motivate higher rates of savings, or do research on any aspect of behavior related to saving, this book will be a guide and inspiration. Geared to researchers and graduate students, Warneryd states it is "intended to furnish ideas to stimulate research on savings behavior" (p. 1).

With the U.S. savings rate approaching zero, savings behavior should be a fertile field for researchers and policy makers. Although the author is an economist by training, the focus is on the psychology of savings behavior rather than economics. Other professionals who could benefit from selected segments of the book are Extension educators and policy makers who are developing programs to encourage savings. "Saving behavior is a function of perception of the future and the act of providing for the future, paying respect to social influences" (p. 2), a cogent reminder to the terminally rational who are attracted to the fields of financial management and consumer economics. This book would serve as an excellent text for a graduate course on the consumer economic psychology of savings or selected chapters could be used to enhance a family economics class. Of course, if a graduate student were planning a thesis or dissertation on the psychology of savings, Warneryd has saved you the time and trouble of searching the literature and gathering the journal articles. Better yet, because of the international focus, one is likely to find far more in this book than one would get from a review of American journals. Of course, the task of assimilating the material remains, but consider how much time has been saved in the search process. The primary motivation for agreeing to write a book review is the opportunity to keep up with the recent literature in one's field. Because the books are new you never know whether the author provides sufficient reward for the time investment. Warneryd provided a rich reward to this reader. This book could be the "only book you'll ever need"on the psychology of saving. Seasoned researchers will reap the benefits of a thorough history along with a generous helping of European work that may not be familiar to North American readers. Each chapter begins with a "purpose" and ends with a clear summary. Parts of chapter 1, "The Psychology of Saving," on history and definitions of economics and psychology are a bit dry but the summary comparing the two disciplines in Table 1.1 presents a clear overview and comparison. The "three meanings of economic psychology" round out the chapter.

Chapter 2, "What Savings Is and Is Not" begins with a review of the life cycle hypothesis (LCH) of savings, proceeds to differentiating among hoarding, saving and investing and on to stock measures of saving (wealth) and flow measures (changes in savings). The book is packed with definitions. Naturally the name George Katona emerges in the discussion on motives for saving. The international aspect of the author's experience begins to emerge in a discussion of how countries have different ways of calculating savings. Warneryd discusses the challenges facing researchers including decisions that they have to make and difficulties in problems with studying households rather than individuals. Contrary to assumptions of some researchers, typically there isn't just one financial manager in a household. This trend may due in part to the high rate of women's labor force participation. Warneryd provides a rationale for adapting the definition of savings to the purpose of one's study. Throughout the book he provides examples from the Dutch VSB longitudinal study of savings with which he was involved for most of the1990s.

Chapter 3, "A Historical Perspective on the Psychology of Saving" reaches back to the work of Aristotle and

1. *1999, Hardcover, 389 pages, ISBN: 184064 016 2*

Cicero, providing a hint as to the comprehensive nature and depth of this book. With due attention to Adam Smith, John Stuart Mill, Karl Marx and Alfred Marshall "Who wished he had been a psychologist" (p.106), the reader is offered a heavy dose of history and psychology of savings. So "what can we learn from the early economists about the psychology of savings?" The author provides six insights (hint: skip the history and go directly to page 117).

Dusenberry and the "discounted utility model" (time value of money for the economically challenged) head up Chapter 4: "The Psychology of Saving in Modern Economic Theories of Saving." Here we find more on the life cycle hypothesis, the permanent income hypothesis (PIH), Fisher's theory of intertemporal choice, and Keynes' absolute income hypothesis. While this may sound a bit dry and intimidating for the educator or student, I found the review of historical theories a valuable reminder of how theory applies to my current work on bankruptcy education. Specifically, people compare their consumption level to selected reference groups, attempt to maintain the highest level of past consumption even when they experience a drop in income; the household resists a downward change in level of living. The term "habit lag" or "habit persistence" applies. Friedman's permanent income hypothesis (complete with indifference curves) and Modigliani and Brumberg's life cycle hypothesis are likely familiar to readers but recent work by Campbell and Mankiw concluded that there are two types of consumers: those who follow the PIH or LCH and those who spend what they earn according to the absolute income hypothesis. Kessler and Masson proposed three types of capital: S-capital for future consumption, K-capital for high returns, and H-capital or human capital. These recent research studies place a more understandable face on what may appear to students as dry theory. From there Warneryd launches into modern economic savings theories and the behavioral life cycle hypothesis (Shefrin & Taylor). Understanding self control, mental accounting and framing (how an individual perceives alternatives and chooses a reference point) brings us back to the practical application of the theory; so practitioners: don't be too quick to skip over the theory section. For those of us who lament the high proportion of Americans who overpay their income taxes each year in increasingly larger amounts, the discussion of how the source of money influences the propensity to consume can help us fine tune our appeals to curtail this practice. Consumers have different propensities to consume from different mental accounts. Warneryd points out the need for more research on time preference and savings, illustrating another value of this book for graduate students. It is chock full of research ideas.

Chapter 5, "Psychological and Other Behavioral Research on Household Savings" examines the four approaches to studying savings behavior: survey, segmentation, experimental, and qualitative research. Here is another area in need of theory development. Katona's contributions are reviewed in detail including his three categories of saving: contractual, discretionary, and residual. Again, food for thought for practitioners. The authors shed light on how the self-employed differ in savings behavior from employees. Economic socialization of children receives attention as well. The longitudinal Dutch VSB savings research, begun in 1993, yielded the "Hierarchal Model of Savings Motives" from cash management to emergency, goal achievement, and wealth management. Savers are grouped in six categories: residual, contractual, security, risk hedgers, prudent investors, and divergent strategies. Warneryd analyzes the pros and cons of experimental research on savings and how the studies of economists and psychologists differ. This section provides fruitful ideas for replicating studies conducted in other countries as full scale research or mini studies as student projects. Few qualitative studies have been published; there is room for contributions in this area. "The Use of Psychological Variables in the Study of Savings:

Chapter 6, “The Cognitive Concepts of Expectation, Uncertainty, and Decision Making" launches into a review of literature on microeconomic psychology with implications for understanding motivations for investing and consumer expectations and attitudes toward risk. Mental accounting comes into play again. In Chapter7,"The Use of Psychological Variables in the Study of Savings: Attitudes, Motives, Personalty and Social Influence", the author reviews modern attitude theory and how to motivate changes in attitudes. Here we get to the practical application of the research and another illustration of the wide appeal and value of this book. The link between attitudes toward savings and actual behavior is weak; attitude explains only a small proportion of variance in behavior. Changes in attitudes are what count. Understanding the motives for saving is critical to developing educational campaigns and public policies to encourage saving. The Dutch VSB panel study utilized the model for attitudes towards saving based on Ajzen and Fishbein's work on The Theory of Reasoned Action. Check out the model on page 262. Further work on personality and social influences on savings illuminate the current problem in the U.S. Reference groups certainly play a part in the decision to save.

Chapter 8, "An Integrative Framework for the Psychology of Saving" sums up the state of the art in the psychology of saving and presents an attempt to integrate `thrift', `forward-looking' (expectations) and action" (p.297). This chapter is geared to researchers. It presents a "schema" for psychological research on saving. Those interested in theory development will appreciate Warneryd's depth of experience in this area. The dominant economic model of savings, the LCH, has many weaknesses and can be improved by the addition of psychological variables. Warneryd offers a "schema" (not quite a model) to suggest variables and relationships for use in empirical research.

The last chapter, "Implications for Studying and Influencing the Consumer," provides 1. "Implications for policy makers and marketers of financial products and services. 2. Implications for consumers who want to save more. 3.Implications for research, basic as well as applied" (p. 329) On the one hand the author predicts increased savings as a result of uncertainty about public retirement plans (Social Security), reduced levels of unemployment benefits, more attractive investment options, and increased attention to environmental problems. However, since the savings rate in the U.S. is approaching zero while the bankruptcy rate continues to climb, at least for the present perhaps Warneryd's"countervailing pressures" against savings are more powerful: taxes and low interest rates discourage savings, spending habits are hard to overcome, and the belief that goods will only cost more in the future. While the LCH is not effective at explaining individual or household behavior, the modified LCH is useful in providing ideas for marketers and policy makers. While the theory and applications for research were rewards enough for the investment in time reading this book, the practical applications in the last chapter were the icing on the cake. You'll have to read the book to enjoy the dessert!

