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The Psychology of Money

The Pension Papers™

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Executive Summary

People need a secure financial future, and, according to recent research, it may also be the core reason why people work for corporations. While people are incented to work for a number of reasons, the psychology of money has an effect on the decisions made by both leaders and teams. This is because, as detailed in this paper, research shows that money creates the foundation for hoarding, for protection against feelings of success, inadequacy or failure and for the rejection of others who do not make as much money.

What is the relationship, then, between our relationship with money and the creation of optimal pension plans that motivate employees to perform?

This paper explores four primary theories and their sub-theories, which includes the expectancy theory of motivation, motivation-hygiene theory, self-determination theory and downward social comparison theory. It examines how we use money and why pensions are such a touchstone for employees. It presents best practices for using (or not using) money as an incentive in planning pensions. In this paper, we will explore the connections and disconnections, between what our team members think and feel about money and the process of engaging them, and rewarding them, in the workplace. We'll look at what leadership means when it comes to creating pension strategies that are based on what people actually think about with these rewards for a life of work.

Understanding The Psychology of Money

The use of and access to sources of money has been said to change people's motivation and their behaviour toward others, both for the better and, even more often, for the worse.[1] In fact, research shows that there may be a negative psychological impact of the act of reaching for financial success over the long term.[2] At the same time, research also shows that money can have a positive effect on a person's level of happiness, albeit a weak one.[3]

What is the relationship, then, between money and a person's choice with respect to pensions? How can companies create optimal pension plans that motivate employees to perform? Why do people strive to get money and then hoard it or use it as a tool?

Everyone knows that money is often used as a carrot in business. This is especially true when it comes to thinking about why and how to plan pensions. The promise of a safe and secure future, provided by a pension, is one of those carrots. While there are other short term financial incentives such as bonuses and stock options, pensions are the most likely direct financial benefit to be offered to the average worker in the Western world.[4] What this means is that most business leaders need to understand how their employees think about this form of money better.

But the answer isn't as simple as providing more money, or better pensions, for employees. In fact, research from the field shows that most people are not directly incentivized by money, and creating the right solution is not as simple as creating job security or even financial stability for the average employee. It's not about getting people to save more money themselves, at least directly. (We'll dig into that research in the next few pages.)

What does this mean for employee leadership, then? Are pensions really the incentive we have long believed them to be? And, if not, what can we do about creating the right financial framework for our teams?

Understanding the psychology of money will help leaders understand their employees better and therefore better appreciate what it takes to create a secure future in the workplace.

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[1] Vohs, K. D., Mead, N. L., & Goode, M. R. (2006). The psychological consequences of money. *Science, 314*, 1154-1156.
[2] Nickerson, C., Schwarts, N., Diener, E., & Kahneman, D. (2003). Zeroing in on the dark side of the American dream: A closer look at the negative consequences of the goal for financial success. *Psychological Science, 14*(6), 531-536.
[3] Dunn, E. W., Aknin, L. B., & Norton, M. I. (2008). Spending money on others promotes happiness. *Science, 319,* 1687-1688.
[4] Manoli, D., & Weber, A. (2016). Nonparametric evidence on the effects of financial incentives on retirement decisions. *American Economic Journal: Economic Policy*, *8*(4), 160-82. While there are other more frequent benefits such as extended and basic health care plans, these are not considered to be financial benefits.

Theory meets practice

Before we get to leadership and best practices, let's start with understanding just how money works in the mind of the average person.

There are a number of theories that seek to explain our relationship with money on a psychological level which can enhance the way that we apply leadership frameworks in pension management. These social psychological theories may be able to shed some light on the ways in which people interact with money and other capital resources, and how companies can best use incentives to inspire engagement.

Expectancy theory of motivation

Motivation theory is linked to our earliest beliefs about money and work. And it's a theory you've probably heard about all of your working life, in one way or another.

This theory suggests that people become motivated in relation to perceived rewards, and especially to money. The expectancy theory of motivation is closely aligned with Abraham Maslow's hierarchy of needs and what he calls self-actualization and peak experiences.[5] Essentially, every human being has to meet his or her fundamental needs (food and shelter) first before attempting to satisfy more sophisticated desires that relate to our higher reasoning, like self-actualization.

Money is the modern means by which fundamental needs have to be met.

An extension of this hierarchy is what is known as expectancy-value theory. In this theory, the guiding principle is that expectancy times value equals motivation.[6] In other words, a person needs to experience both expectancy and value in order to reach a state of motivation to complete a task. For example, the task might be work or with the time it might take to bid on a work project. Then, the person assigns value to the work, such as how much money he or she deserves to make on an hourly basis on the job. Finally, the ideas and their corresponding values as modified according to experience. For example, a worker may decide that a job at a coffee shop is worthwhile for a wage of eleven dollars per hour, but not at a wage of ten dollars per hour. Thus, the individual can decide on his or her level of motivation to complete the task based on the value of this money.

In a recent large scale study about work and motivation in the United States, however, results of a poll of currently employed workers show that money may not be directly related to decisions about pensions and retirement. In fact, the strongest predictors for leaving a company were connected to employees' need for change, boredom or a feeling of being tired of working at a company, regardless of their pension plan or how many benefits they have accrued.[7]

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[5] Maslow, A. H. (1943). A theory of human motivation. *Psychological Review, 50*(4), 370-396.
[6] Wigfield, A. & Eccles, J. (1992). The development of achievement task values: A theoretical analysis. *Developmental Review, 12*, 265-310.
[7] Knoll, M. A. (2011). Behavioral and psychological aspects of the retirement decision. *Soc. Sec. Bull.*, *71*, 15.

Employee motivation, therefore, may not always be linked to positive incentives.

But let's dig further.

Motivation-hygiene theory

Maslow's theory was only the first that looked in depth at motivation and external factors.

Frederick Irving Herzberg, the developer of motivation-hygiene theory, was an American psychologist who became one of the most influential names in business management because he was able to delve more deeply into how job satisfaction, job dissatisfaction and motivation are connected.

Herzberg showed business leaders that the task of motivating employees was a lot more complex than simply providing them with money and other benefits.

What he means by hygiene, by the way, has nothing to do with keeping clean. It's about separating out the causes for satisfaction from dissatisfaction in the workplace. Herzberg was able to demonstrate that these are two entirely different things and that they are fundamentally unrelated to one another.

Let's start with what satisfies the average employee.

Factors that are likely to be related to an increase in an individual's motivation include task achievement, recognition for achievement, intrinsic interest in the task, increased task responsibility, advancement and the possibility of occupational growth, all of which result in the acquisition of money. An increase in salary or an increase in pension benefits, results in satisfaction because it is an indicator of something that goes along with a person's achievement on the job. In essence, motivational factors result in financial growth for an individual.

Dissatisfaction factors may, however, be more important to motivation than those related to satisfaction, strangely enough.

Dissatisfaction factors can include the imposition of a worker's company's administration and policy, supervision, working conditions, limits on salary, status, job security and interpersonal relationships, all of which can lead to a lack of money or money security. These factors are therefore associated with the pain avoidance linked to financial risk. The more that a person is placed in a situation of financial risk, then there is a greater potential for upset. There is therefore a definitive connection that can be observed between hygiene factors and psychological issues such as stress and depression in the workplace.

Field research in recent years, however, has shown that while there is a strong connection between motivation and happiness, financial strength in pension plans are n*ot* the key factor that lead to employee motivation.

The factors that *do* matter to employees planning for the future include retirement goal clarity, financial goal strength and alignment between their personal values and self-beliefs around their pensions.[8] In other words, the focus of employee motivation linked to the motivation-hygiene theory has to do with creating a plan upon which an individual can rely and then working towards that goal, rather than the provision of an exceptional amount of money. Although every penny counts, what seems to count more is having a sense of control over one's future plans.

Self-determination theory

Given the need for personal control, self-determination theory may help to reveal even more about the link between motivations and pensions.

This theory is grounded in the idea that the quality of motivation is more important than the quantity of motivation. Two primary types of motivation exist: autonomous and controlled motivation. Autonomous motivation involves recognizing the value of the activity itself; this value can consist of financial value or personal value. Controlled motivation involves external regulation, such as a supervisor at a job or a financial reward for performance, as well as the external influences that affect behaviour and finally the idea of interjected regulation, in which one's intrinsic motivation to complete a task is mediated by outside influences such as approval from others or avoidance of negative consequences, such as the loss of money or a punishment for doing a poor job at work.

What self-determination theory shows is that there is a need to recognize the fact that there is a social component to the psychology of money and its links to motivation. The idea of gaining approval from others or avoiding the possibility of negative consequences can be connected to the idea of social network theory, in which our ability to navigate social networks successfully may allow us to gain access to money. In this way, we may feel positive or negative emotions based on our ability to achieve this goal. According to this theory, social events that support feelings of competence when performing a task, such as rewards like the award of money for performance at a job, a contest or for displaying a specific skill, may be more important than money. Other social factors include freedom from negative evaluation as well as support for desirable challenges and constructive feedback that supports performance.

Similar to motivation-hygiene theory, self-determination theory shows that there may be a very indirect connection between financial success and motivation.

[8] Hershey, D. A., Jacobs-Lawson, J. M., McArdle, J. J., & Hamagami, F. (2007). Psychological foundations of financial planning for retirement. *Journal of Adult Development*, *14*(1-2), 26-36.

In fact, recent research into pension motivation shows that those who are actually interested in money over social reward are few and far between.[9] When self-gain acts as the fundamental motive, this translates to a focus on financial goal achievement, and money might foster a mindset that increases disregard of those who do not facilitate self-gain and achieving a goal. In other words, if individuals are only provided with financial incentives, this may actually lead to poor teamwork at the office. Increasing social rewards in the workplace may offset employee demands for benefits or other financial incentives.

Downward social comparison theory

The psychology of money and its links to motivation may be connected to the psychological construct of downward social comparison.

Downward social comparison is the act of looking down on others who have a lower income or less social capital. Essentially, downward social comparison allows individuals to create a more positive mood and outlook on the future because of the fact that one can realize that there is always someone else worse off. This process allows one to defend oneself against feelings of inadequacy or failure.

If an individual is in need of proof of their own financial achievement, then they will be moved to compare themselves to those who either do or do not achieve in that same way. Likewise, if they are motivated to be seen as part of a collective group such as a corporate department which includes members who are high performers, they will perhaps be more likely to compare themselves with the goal of affiliation with that group. If an individual is feeling guilty about their own decisions or experiences in life, then knowing that others have experienced similar or worse situations, such as bankruptcy, is likely to decrease that individual's sense of regret for their choices.

In essence, the process of downward social comparison makes it possible for individuals to forgive themselves for anything they have done in their lives to make their future insecure, or forgive themselves for the lack of financial success that they have achieved at work. By looking at others who have achieved less, some individuals will feel better about themselves.

The core thing for leaders to know is that downward social comparison theory may explain why people act differently when they have more (or less) money than their peers.

When people have access to money they may become more distant from those around them, and more likely to reject requests for assistance from people close to them.[10] When they have less money, they feel as if they have done something wrong.

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[9] Wang, X., & Krumhuber, E. G. (2017). The love of money results in objectification. *British Journal of Social Psychology*, *56*(2), 354-372.
[10] Vohs, K. D., Mead, N. L., & Goode, M. R. (2006). The psychological consequences of money. *Science*, *314*, 1154-1156.

There may be two psychological reasons for this to occur. The first reason is that individuals with money may not want to risk not having money in the future, and therefore they develop a hoarder mentality that prevents them from being able to share their wealth with others. The second reason is that downward social comparisons may result in an individual's negative perception of those around them, and may present the individual with money with an unconscious risk that if their money is shared, the recipient of that money may rise socially in comparison.

In other words, gaining access to money is more *symbolic* than it is p*ractical*.

For leaders, therefore, what is important is the recognition that money matters, but not money itself. What is important than money itself, therefore, is what money represents to people.

What does all of this mean?

From the point of view of pension leadership, the biggest takeaway from both motivation theories and field research into pension aims is that money is not everything.

Research into the psychology of money shows that our reliance on currency as an indicator of success and the focus of our lives' work is not necessarily a healthy one, or one that actually works. In fact, while money can have a positive effect on a person's level of happiness and work effort, this effect is very limited.

In fact, what this shows is that creating a high-output pension plan should not be treated as the only objective, or even the most important objective, in helping employees plan for retirement.

Should leaders view pensions as a place of motivation?

Yes, but only insofar as pensions are, like money, symbols of what really matters. **A pension can be seen, more than anything, as a corporate endearment, but one that is very important to employee well-being.** Having a pension makes people feel safe, and having the same pension and benefits as everyone else makes people feel like they are at least as valuable as the person at the next desk. Not having a pension makes people feel at risk, because, as we've discussed in earlier papers, the social context of money is changing and people have fewer sources of retirement funds upon which they can rely.

What actually works?

Given these findings, when we're planning pensions, leaders need to focus on a few key standards of management that will help build the right kind of incentive in the workplace.

1. ***Building monetary intelligence***. As a recent international study suggests, business leaders ought to shift from a focus on financial pension planning to, instead, a focus on monetary

intelligence for employees through active training.[11] Like emotional intelligence is used to improve business relationships, monetary intelligence aims for a more nuanced understanding of economics and finance among team members in a business, so that they will make better decisions for their own financial futures as well as that of the company. The authors of this study suggest that workers will benefit from feeling as if they are stewards of their own financial choices, if they have the right knowledge to make those choices in a way that benefits them. Positive stewardship of money, they write, results in better coping behaviours for changes in the status quo, as well as decreased avoidance of challenges that arise at work and at home. On the flip side, without monetary intelligence, people feel afraid for their futures, and this short term financial mentality will affect their ability to make the right choices for themselves and the businesses in which they work.

2. ***Developing heterogeneity in pensions based on individual employee needs***. Because financial incentives are secondary to personal values placed on money, additional new research in the Netherlands has shown that replacing full-time pension schemes with schemes that offer gradual retirement opportunities induce workers to retire one year later on average, and increase productivity and knowledge management in companies, especially for teams with workers who have lower than average wages.[12] In other words, creative pension planning can include a varying work and retirement schedule in which people can gradually increase their draw from their pension money and decrease their working hours.
3. ***Supporting equity and quality of life at work***. As noted above, because people feel as if they are being constantly compared to each other at work, they may have difficulty with downward (or upward) social comparison. Employees need to feel as if they have the same options and benefits as others at work. This is where pensions, in being framed as a standard for all employees, can serve to motivate employees in a way that sales bonuses or stock options, which are often reserved for certain work groups, cannot. As a result, leaders ought to communicate the benefits of pension plan on a regular basis, and use it as a key touchstone for employees in showing teams how the business is supporting their future happiness and quality of life.

What all of this means is that employees need to be taught how to use, understand, or optimize their own pension and figure out how to plan for their future life after retirement. They then have to be given the flexibility to use these skills and life choices on their own, so that they feel safe and secure.

Ultimately, if employees feel as if they have active choices in planning for their futures through self-determination, and they feel like they are receiving the same benefit as others at work, they are more likely to feel motivated in their work.

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[11] Sardžoska, E. G., & Tang, T. L. P. (2015). monetary intelligence: Money attitudes—unethical intentions, intrinsic and extrinsic job satisfaction, and coping strategies across public and private sectors in Macedonia. *Journal of Business Ethics*, *130*(1), 93-115.

[12] Elsayed, A., de Grip, A., Fouarge, D., & Montizaan, R. (2018). Gradual retirement, financial incentives, and labour supply of older workers: Evidence from a stated preference analysis. *Journal of Economic Behavior & Organization*, *150*, 277-294.

Let’s break it down to brass tacks

All of this means that pension managers would be best served by looking at how they can:

- Address employees’ real retirement concerns and objectives, which include quality of life, equity and feeling valued
- Help develop monetary intelligence in their workforce so that people can make definitive plans for their futures through an active education plan
- Support positive changes in work-life balance so that employees’ relationship with money is not the driving force in creating positive outcomes for corporate teams
- Build capacity for retirement planning at every level of the organization so people feel secure and satisfied

Leaning into monetary intelligence and flexibility in pension options will serve employees and the organization alike. It will allow for teams to negotiate better pension plans on both the management and employee sides of the table. It will create happier and more secure employees who feel as if they are prepared for every eventuality.

This approach is a positive leadership choice, rather than a financial choice, but it’s also the right way to create alignment with how the psychology of money really works.

That’s because the true motivation equation is just this: To build purpose and quality of life into organizations with a purpose, to treat people as human beings who can’t simply be bought by a lump sum and to create shared values while simultaneously delivering business results.