Habit and Regular Saving: An Intertemporal Analysis

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What is the relationship between habit and saving? The many public calls for consumers to establishing a habit of saving indicate that it is a desired behavior, but, obviously, a difficult one to achieve. Savings habits are frequently practiced behaviors, done without a particular sense of awareness, with the goal of freeing up funds for saving or debt reduction. Using the self-reported habit index (Verplanken & Orbell, 2003) and applying it to saving for the first time, survey data were collected to (1) validate the role of habits in regular savings; (2) test whether participation in a savings program aids in the formation of savings habits; and (3) examine the role of habits in the perception of financial strain.

The treatment group included participants in a federally funded, multi-year savings program that provides incentives for low-income individuals to save toward purchasing a home, financing higher education, or capitalizing a small business. The comparison group consisted of low-income individuals in the general population who lived in counties served by the network but who were not savings program participants. Nearest-neighbor matching without replacement was used to pair comparison group with treatment group observations to account for demographic differences (N=128). Saving habits were measured with the Self-Report Habit Index, which was developed to reflect the different facets of habit, including the frequency, lack of awareness and control, and mental efficiency of behavior.

Study findings document the role of habit for regular saving and the success of targeted educational and behavioral interventions on developing savings habits. Admittedly, the idea that long-term savings may be achieved by habitualizing behavior is controversial in the behavioral economics literature, which favors commitment devices that reduce the behavioral component to a minimum. Examples include auto-enrollment condition in retirement plans, payroll deduction in combination with dollar-cost averaging, the use of life-cycle investment funds, automatic schedules of slow retirement contribution rate increases, employer-sponsored matched savings. In contrast, our analysis focuses on the financial behaviors in every day life – and they appear to be ideal candidates for habits. Many of these decisions tend to occur frequently, tend to affect small amounts of money in the "peanuts" range, and are targeted toward the greater goal of freeing up funds for saving or debt reduction. These savings habits may funnel funding toward the institutionalized commitment mechanisms or develop independently of it, but both help achieve the greater goal of asset building for the short-term emergency as well as the old age.

References

Verplanken, B., & Orbell, S. (2003). Reflections on past behavior: A self-report index of habit strength. *Journal of Applied Social Psychology, 33*(6), 1313-1330.

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