



the Observer

The Psychology of Money

Money talk is tricky business. Like religion and politics, it is a sensitive topic of conversation.

You just don't know who you can trust or how your money will be perceived by others, even close family members. The following story demonstrates. Several years back, my 5th grade daughter asked, "Are we rich?" She asked this question because a classmate had assumed this to be true when her parents noted that we lived in a large home. Her

Happiness is not in the mere possession of money; it lies in the joy of achievement, in the thrill of creative effort.

—FRANKLIN D. ROOSEVELT

question exposed a reality that needed to be acknowledged and discussed in a meaningful way. It was time to talk about values, both personal and fi-

nancial. We acknowledged that we did have a nice home, nicer than most. We then pointed out that our good fortune was largely due to our hard work. We felt this was a real family teaching moment, but in reality, our daughter only wanted a yes or no answer. Herein lies the conundrum. Comprehensive, meaningful money talk is as much a subjective exercise as it is objective. It is not just about numbers. It is also about the feelings, values and attitudes that effect what we think and do regarding money. But as the story above illustrates, most don't readily perceive money in terms of values. The question then is what can we do about this? How can we impact our children's attitudes and values—their *psychology of money*, if you will? We suggest that financial literacy is the first step.

What is financial literacy? Consider this definition taken from a study:

Personal financial literacy is the ability to read, analyze, manage and communicate about the personal financial conditions that affect material well-being. It includes the ability to discern financial choices, discuss money and financial issues without (or despite) discomfort, plan for the future, and respond competently to life's events that affect everyday financial decisions,

*including events in the general economy.*¹

Now let's look at some statistics regarding financial literacy in our country. Of the 4,000 students who took the Jump \$tart personal finance survey in 2004, 65.5% received failing scores. According to the 2007 Retirement Confidence survey by the Employee Benefit Research Institute and Matthew Greenwald and Associates, 50% of respondents felt they only needed five to 10 times their annual salary to retire comfortably (this would equate to earning up to a 20% annual return on investments to avoid spending any principal). At the end of the last decade, only 21% of our youth ages 16-22 reported that they had taken a personal finance course at school. Other statistics show the very low savings rate in the United States. This, coupled with the fact that sub prime mortgages will begin to adjust next year, points to the possibility that many may be forced to abandon their homes and declare bankruptcy—All because they did not understand that their mortgage interest rate could adjust up causing significant negative personal cash flow.

This scenario becomes even more dismal as corporations continue to terminate the funding of defined benefit plans,

¹ Page 50 November 2004 *Journal of Financial Service Professionals*



which pay out a monthly pension upon retirement. Over the past 30 years, there has been a gradual shift toward employees being responsible for funding their own retirements through 401(k) plans. Those who retired in the 1960s, 70s or 80s did not have to be concerned with or understand the stock market. Upon retirement, they just received monthly pension checks from their employers. Their employers managed large stock and bond portfolios to meet the requirements of their pension payouts. Things have changed. Twenty-first century workers now need to understand how to invest their 401(k)s in the stock and bond fund investment choices provided by their company. But good, solid money decisions about financial products and strategies require personal financial literacy. Unfortunately, our schools do not provide this kind of education.

Financial literacy happens when financial education is met with a desire to learn and apply financial concepts. This becomes problematic when money decisions are clouded by emotion. Professional mar-

Economy is half the battle of life; it is not so hard to earn money as to spend it well.

— C.H. SPURGEON

keters understand and use this psychology to their advantage. Credit card commercials list itemized costs —then add on love, memories and relationships with the punch line

“priceless.” We are coaxed to buy, based on an emotional desire for things that we covet. This is how we get into trouble. Without firm dedication to financial literacy standards, we tend to rationalize spending decisions, not considering the financial consequences. Let’s look at an example.

You have been driving a minivan to ferry the kids around for the past 10 years and now it’s time to buy a real car. Great, it’s time to go car shopping! You know you can afford a car in the \$25,000-\$30,000 range, equating to car or lease payments of \$350 per month. The current van you drive is coming off lease at this same monthly cost and money is tight. You visit the Ford, GM and Daimler/Chrysler dealerships and find plenty of reasonable choices, but the quiet voice of unreason begs consideration as well. Your next-door neighbor just bought a Lexus. You would really like a Lexus. Who wouldn’t? It’s the Lexus Experience! So, you drive to the nearest Lexus dealership and are taken in immediately. The cars are much nicer; there is espresso and child care; and their service bay floors are cleaner than your kitchen table. You are captivated! You test drive the new model, it purrs like a kitten, and has an orchestra hall sound system with every feature imaginable. You ask the price—a four-year lease for \$750 per month. Come on, you can handle that. There is a raise coming in the future, and if not, there is still \$10,000 available on the home equity line of credit to make

up the shortfall. It is only \$400 per month. Deep down, alarm bells are ringing. You are not really feeling comfortable. But the alarm is ignored. Heck, you deserve it (greed). Your neighbor has one (envy/jealousy). It will look great in the driveway (pride). You love all of those wonderful features (lust). And so good sense is dismissed. You sign the lease agreement and drive home your brand new Lexus.

I believe you just committed five of the seven deadly sins (sloth and wrath are the other two), or as Flip Wilson’s character, Geraldine, used to say, “The devil made me do it.” Because we are a consumer-based society, this scenario plays out over and over again. One would hope that when faced with these lease choices, we would make a values-based decision grounded on financial literacy, recognizing the danger of spending beyond our means. Such a rational understanding should lead us to buy the affordable car. But, as this story shows, we are typically not driven by rational understanding when it comes to money. Too often we are seduced down the wrong path, captive to our emotions. And if we take this seductive road too often, we risk becoming addicted.

Jesse O’Neil knows this addiction process all too well, and wrote her own personal biographical account of it in *Affluenza*. She describes being raised by a nanny in a third-generation wealthy family, feeling isolated and emotionally deserted by her parents. She grew up in a vacuum,

with no moral guidance. Easy money led to excess, but did not bring happiness. Yet, money became more addictive than any drug as she continued to seek happiness with its easy availability. Jesse reflected on this life and observed the risks associated with deficient moral rearing. This is how a family can fall from rags to riches....to rags, in three generations.

First-generation wealth may disappear by the third generation if core values are not passed on within the family. Lacking clear direction, the second generation is not equipped to assimilate or grow the wealth they inherit, preferring to hoard and live off their income, and in many cases, even the principal. Lifestyle choices then become progressively worse with the third generation, who often exhaust family fortunes. All this can be avoided if proactive measures are taken by the first generation.

Unrestrained spending can cause great suffering. We have all seen countless celebrity lives jeopardized or destroyed by their wealth. Anna Nicole Smith is an example. Her recent death was followed by months of media coverage, displaying all the ugly details of her sad demise. She married a wealthy man 40 years her senior, becoming wildly famous. She died leaving an infant daughter whose paternity could only be determined through DNA testing.



"Thanks, Pop, but today's kids don't want money, they want leadership."

Anna lived a life of fortune and fame, but her lasting legacy is one of scandal and tragedy. Her story is certainly a cautionary tale. The lesson: We risk becoming tragic figures ourselves if we avoid or ignore wealth's destructive power. The task at hand, then, is to help future generations learn this lesson so they can live happy, productive lives. Our children and grandchildren face a daunting challenge. They will inherit a great amount of wealth, by some accounts between \$15-30 trillion over the next 30 years. If their financial education is sub par and their core values are not solid, rabid financial spending and ruined lives may result. Jessie O'Neil had the courage to tell her story and turn her life around. Things did not end so well for Anna Nicole Smith.

Some simple tools can help ensure sound financial decision-making. We understand that we are preaching to the choir, as most of you reading this newsletter understand

and practice wise financial decision-making. But we think it beneficial to highlight three important guidelines—*sufficiency, sustainability and appropriateness*.

Sufficiency is about answering the question, "Do I have enough?" This is the first question we ask anytime we consider taking on a new expense or a new financial commitment. We ask this question when paying monthly bills, making large, one-time purchases, buying a first or second home, paying for a child or grandchild's college education, or taking a vacation.

A second important guideline is *sustainability*, or how long will my money last? Pre-retirees often ask this question as they contemplate retirement. Sustainability requires that we be well informed about our assets, cash flow and taxes. Without sufficient earnings from our assets, there may not be sufficient income to pay our ongoing expenses. Will you have enough slack in the rope to not have to fret over marginal purchases, or will you have to go without? Can you afford to travel, maintain two homes, or provide financial assistance to your grandchildren? Can you do all of this without depleting your assets? All spending decisions must be considered and balanced in light of *sustainability*.

A third important financial decision-making guideline is *appropriateness*, or "How do I

stay out of financial trouble?” You must always consider whether an expenditure, financial strategy, or investment opportunity is appropriate for you. Appropriateness was an important consideration in our earlier car-buying story, and it is certainly a key question when buying a second home. This question is easily answered by those with surplus income who have already addressed sufficiency and sustainability. But sometimes a financial decision may pass the sufficiency and sustainability tests, but fail to pass the appropriateness test. Buying a red convertible BMW for a grandchild’s high school graduation gift may be inappropriate if the grandchild hasn’t yet learned how to be a responsible, productive citi-

zen—a “tough love” decision.

As always—it is not about the money and it is all about the money. A lifetime spent wisely answering money questions is the best way to master financial decision-making. But first you must determine what matters most to you, your core values. It is doubtful that if asked about any regrets on your deathbed, you would answer, “I wish I could have accumulated more wealth.” Rather, your answer would probably be about relationships. Perhaps you might say, “I would have liked to have been a better father,” or “I wish I had made peace with my mother before she died,” or “If only I had more time to help guide my grandson in his life decisions,” or “I wish I

could have done something important and been remembered for it.” But if values guide all your decisions, you needn’t worry about facing any of these regrets concerning your family. With values as your compass, your family, your community and the world will be the better for it.

In the 1996 movie, Jerry McGuire, Cuba Gooding, Jr. keeps asking his agent Tom Cruiseto “Showmethemoney!!” Throughout the course of the movie these two men are transformed into different, happier, healthier people by learning to not focus on the money, but rather on taking care of each other. Focus on passing on your values, and the money will take care of itself.



Edward J. Kelly, Jr



Gary W. Klaben



Kevin T. Coyle

*Securities Offered Through
Coyle Securities, LLC. Member
NASD/SIPC K. T. Coyle, G. W.
Klaben, E. J. Kelly*

This newsletter is designed to provide our friends and clients with information regarding the various subject matters covered. It is not designed to take the place of legal, accounting, or other professional advice. If expert assistance is required, the services of a competent professional should be sought.



Coyle | Asset Management Company

Financial Counsel ~ *founded 1972*

2700 Patriot Blvd., Suite 440, Glenview, IL 60026
847 441-5644 | toll free 800 480-7913 | fax 847 441-5258
www.coyleasset.com | email camco@coyleasset.com

© 2006 Coyle Asset Management Company