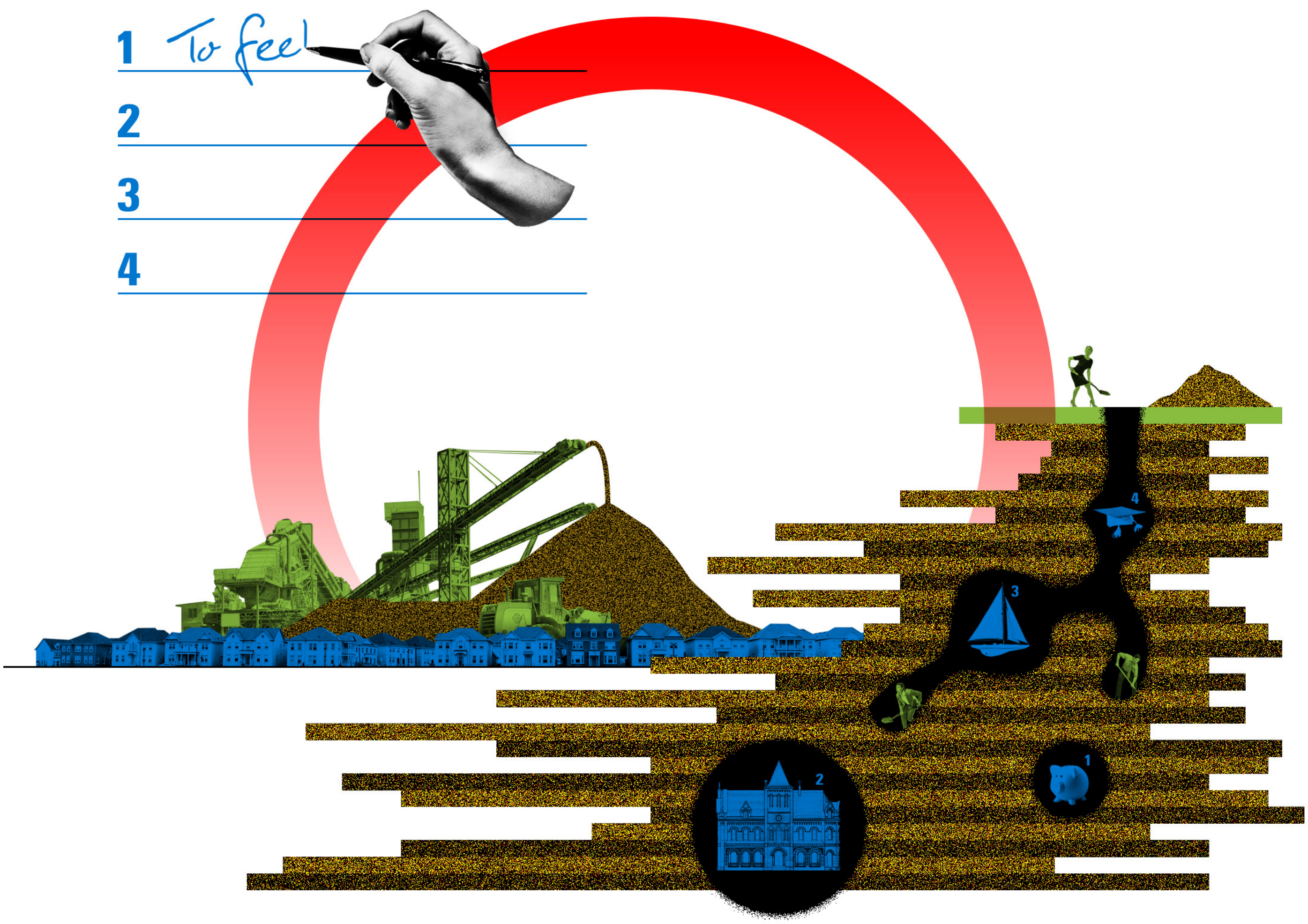
The Investor Success Project

MORNINGSTAR®

Mining for Goals

How Behavioral Nudges Can Help Investors Discover More-Meaningful Goals



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Top-of-Mind Goals Can Fall Short

Goals-based financial planning is probably here to stay, and for good reason. Using a goals-based framework in financial planning led to an increase in client wealth of more than 15%, according to research by David Blanchett, Morningstar Investment Management's head of retirement research,[1] and beyond returns, investors get a sense of motivation and satisfaction with their financial plans when advisors focus on a client's personal goals versus arbitrary benchmarks.[2] But for goals-based planning to succeed, investors need goals that are important and achievable, as Michael Kitces and others have cautioned.[3]

Just asking clients what their goals are isn't the solution. Clients might respond with answers that are seemingly reasonable, but research indicates many of these on-the-spot statements reflect top-of-mind priorities that might not represent the goals that are truly important to them. These *thinking blind spots*[4] can stem from behavioral biases we all share, and biases can wreak havoc on the best-laid goals-based plans. These blind spots can prevent investors from reporting their true goals and lead to financial plans that don't accurately represent their preferences and motivations.

These blind spots are obviously a huge barrier to successful planning, so we conducted an experiment to see if a simple behavioral nudge—a master list of common goals—could help investors better identify what's really important to them. Our results suggest that there's indeed a gap between the goals investors initially think they want and the goals that are truly relevant and important to them. This nudge can help investors find deeper insight into their overarching long-term aspirations and in doing so potentially improve their chances of reaching their financial goals.

1 Research suggests that an optimal, goals-based strategy can add more than 15% in utility-adjusted wealth. Blanchett, David. "The Value of Goals-Based Financial Planning." *Journal of Financial Planning* 28, no. 6 (2015).
2 Locke, Edwin A., and Latham, Gary P. *A Theory of Goal Setting & Task Performance.* Prentice-Hall, Inc., 1990.
3 Kitces, Michael. (2014). "The Problem With Goals-Based Financial Planning." Nov. 16, 2018. *Nerd's Eye View at Kitces.com.* https://www.kitces.com/blog/goals-based-financial-planning-is-impossible-without-first-evaluating-the-possibilities/
4 Benartzi, Shlomo, and Lewin, Roger. *Thinking Smarter: Seven Steps to Your Fulfilling Retirement…and Life.* Penguin, 2015.; Tversky, Amos, and Kahneman, Daniel. "Judgment Under Uncertainty: Heuristics and Biases." *Science* 185, no. 4157 (1974): 1124–1131.

Blind Spots Are the Goal-Killers

Everyone has behavioral biases, and some of these biases pop up when we look for financial goals because of the emotions involved, the complexities of the decision, and the difficulty of forecasting our future desires. Many investors rely on mental shortcuts, such as the availability heuristic — focusing on readily available information when making judgments about what's important.[5] For example, a client who recently attended a housewarming party might say that her top financial goal is to buy a house, simply because that's top of mind and easy to remember. Such mental shortcuts can overlook other financial goals that may actually have greater importance. Research suggests that without proper guidance, individuals often fail to identify as many as half of the goals that they later recognize to be central to their plans.[6] In a moment, these knee-jerk goals may not paint the full picture of a financial life that really is important to the person.

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To prompt more-thoughtful goal identification, past research suggests that a carefully curated list — a master list — of common objectives can be effective. Master lists have been shown to improve preference identification across a variety of areas.[6] Our research tested the effectiveness of lists for identifying financial goals. We wanted the answer to the question: How can we help investors identify their true financial goals, and not only those that are top of mind?

Overcoming Blind Spots

We examined a range of different issues in goal setting and prioritization; the study most relevant for this paper included 318 people in the United States. To mimic the typical goal-identification process, we asked research participants to list and rank their top three financial goals. We then added their self-reported goals, in a random order, to a master list of common financial goals, creating a combined list (Exhibit 1). After viewing this combined list, participants were then asked to rank all the financial goals in order of importance.

5 Tversky, Amos, and Kahneman, Daniel. "Availability: A Heuristic for Judging Frequency and Probability." *Cognitive Psychology* 5, no. 2 (1973): 207–232.

6 Bond, Samuel D.; Carlson, Kurt A., and Keeney, Ralph L. "Generating Objectives: Can Decision Makers Articulate What They Want?" *Management Science* 54, no. 1 (2008): 56–70.; Keeney, Ralph L. "Identifying, Prioritizing, and Using Multiple Objectives." *EURO Journal on Decision Processes* 1, no. 1–2 (2013): 45–67. https://doi.org/10.1007/s40070-013-0002-9; Siebert, Johannes, and Keeney, Ralph L. "Creating More and Better Alternatives for Decisions Using Objectives." *Operations Research* 63, no. 5 (2015): 1144–1158. https://doi.org/10.1287/opre.2015.1411

Exhibit 1: Master list of financial goals

1 To be better off than my peers
2 To pay for personal self-improvement (e.g., go back to school, learn a skill)
3 To experience the excitement of investing
4 To start a new business
5 To buy a house
6 To help pay for my kids' college education
7 To stop working and do something I love
8 To go on a dream vacation
9 To relocate in retirement
10 To care for my aging parents
11 To give to charity or other causes I care about
12 To feel secure about my finances in retirement
13 To feel secure about my finances now
14 To leave an inheritance to my loved ones
15 To retire early
16 To pay for future medical expenses
17 To not be a financial burden to my family as I grow older

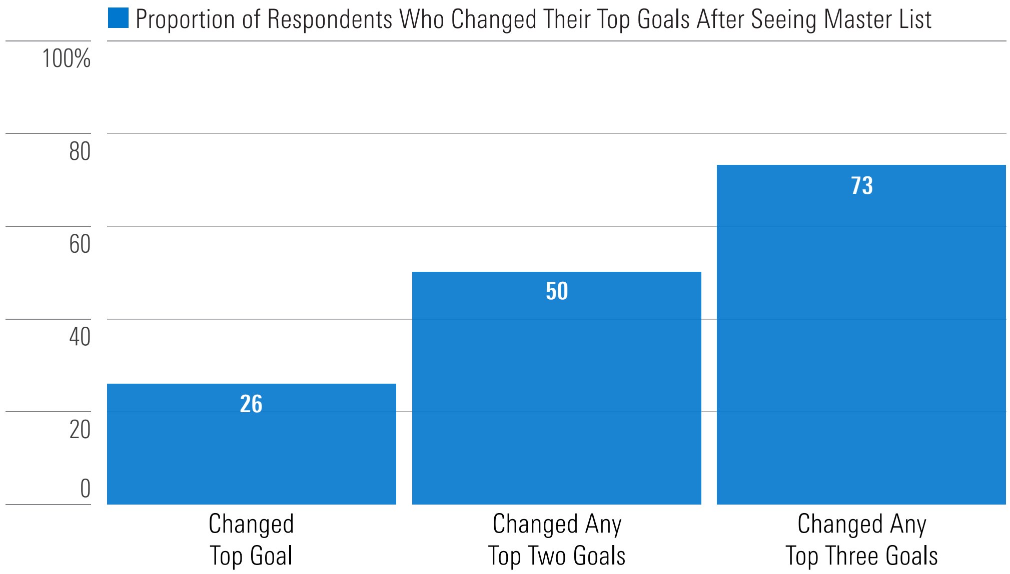
Source: Morningstar.

Master lists may help investors unearth unexpressed goals

To analyze the data, we mapped self-reported goals to those already on the master list and grouped similar self-reported goals together. This process helped us pinpoint only goals that changed substantially after seeing the master list.

If the master list had no impact on goal identification, then we would expect people to choose the same top goals that they self-reported compared with the goals they identified after seeing the master list. That wasn't the case. On average, 26% of participants changed their top goal after seeing the master list. The master list was even more impactful in a multiple-goal scenario: About 73% of participants substituted at least one of their top three goals with goals from the master list (Exhibit 2). That means only about 26% of participants retained all of their top three initial financial goals, and this highlights a flaw in the traditional goal-setting approach used by financial professionals.

Exhibit 2: The impact of the master list



Source: Authors' analysis.

How Did the Goals Change?

Once we discovered that the master list had a significant impact on investment goal priorities, the next question we asked was, "What happened?" What changes did the master list trigger? We found that many people seemed to prioritize goals that were more personalized, detailed, and emotionally grounded after viewing the master list, and the use of a master list also seemed to nudge investors toward more-specific goals.

Retirement: still king

Consistent with previous research,[7] we found that "retirement" was the top financial goal. It was ranked as the top goal two and a half times more often than any other goal, with the residual category "others" and "financial security" trailing far behind. For many investors, retirement is a necessary focus, especially given the looming retirement crisis.[8] Given the impact of the master list intervention, a notable concern is steering investors away from objectively important goals, such as retirement, but our results suggest that the master list didn't seem to have this effect. Among those who initially self-reported retirement as a top priority goal, only 16% changed it after

7 Accenture. 2017. "New Face of Wealth Management in the Era of Hybrid Advice." https://www.accenture.com/t20170403T223757Z__w__/us-en/_acnmedia/Accenture/Conversion-Assets/DotCom/Documents/Global/PDF/Consulting/Accenture-New-Face-of-Wealth-Management-Hybrid-Advice.pdf; Ameritrade. 2016. "Goal Planning Survey." https://s1.q4cdn.com/959385532/files/doc_downloads/research/Goal-Planning-Survey-2016.pdf; Raconteur. 2018. "What Investors Want." http://rcnt.eu/c3emw; Schroders. 2016. "Global Investor Study." http://www.schroders.com/en/sysglobalassets/digital/insights/pdfs/2016/sgis-2016/sgis-investment-outcomes-full-report.pdf

8 Ellis, Charles D., Munnell, Alicia H., and Eschtruth, Andrew D. *Falling Short: The Coming Retirement Crisis and What To Do About It.* Oxford University Press, 2014. Jeszeck, Charles A., Shields, Margie, Augeri, Justine, Cantor, Christina, Fernandez, Gustavo, Gregory, Jennifer, Wendel, Adam, and Wentworth, Seyda. "The Nation's Retirement System: A Comprehensive Re-Evaluation Is Needed to Better Promote Future Retirement Security." Washington, D.C: U.S. Government Accountability Office. (2017). Retrieved from https://www.gao.gov/assets/690/687797.pdf; Rekenthaler, John, Spiegel, Jake, and Szapiro, Aron. (2017). "Small Employers, Big Responsibilities." Chicago, IL: Morningstar, Inc. Retrieved from http://www.morningstar.com/content/dam/morningstar-corporate/pdfs/policy/SmallEmployersBigResponsibilities.pdf; for an alternative perspective on the retirement crisis, see Biggs, Andrew G., and Schieber, Sylvester J. "Why Americans Don't Face a Retirement Crisis." AEI Economic Perspectives. (2015). Retrieved from https://www.aei.org/wp-content/uploads/2015/03/Why-Americans-Dont-Face-a-Retirement-Crisis.pdf

seeing the master list. Those who were impacted by the master list commonly moved toward emotionally based goals. The next two sections provide insight into how people's goals changed after seeing the master list.

Sharpened focus

In cases where investors changed their top goal, 27% made it more specific. For example, investors who previously listed "grow wealth" as the top goal swapped it out for goals that better encapsulated their motivations, such as achieving financial security or increasing social status. Many investors tend to think of goals as overarching milestones that won't be reached for years—which leads them to set goals that might be too broad or vague. But clear, detailed financial goals resonated with investors. So, the use of a master list seemed to help investors reflect on the underlying intent of their initial goals, leading them to better-refined priorities.

Emotions matter

We found that about half of the people who changed their top goal focused on emotions instead of outcome. Using a master list drew an important parallel between emotional returns and financial returns. Many people who changed their goals settled on outcomes that revolved around emotional security, such as "to feel secure about my finances now" and "to not be a financial burden to my family as I grow older." While emotions are often seen as anathema to sound financial decisions,[9] our results suggest that there's a big emotional component to holistically defining financial goals.[10]

The List Is the Thing

Behavioral science shows that people can sometimes be strangers to themselves.[11] Many investors are attracted to the level of personalization of goals-based planning, and this approach is more popular every day, but it hinges on investors really knowing their investment goals and being able to communicate them clearly. This may be a lot more difficult than just straight-up asking clients to identify their major goals off the top of their heads.

Helping investors make good choices and develop plans that make long-term objectives possible should be one of a financial planner's key missions, and our research found that master-list nudges might help guide investors toward the goals they really want. Our experiment found that:

- Master lists may help investors identify their goals: The majority of people we studied changed one of their self-selected goals after considering the master list, so we see clear benefits for advisors when they use a master list to identify and discuss goals with clients during onboarding and discovery.

9 Ariely, Dan. (2008). *Predictably Irrational: The Hidden Forces That Shape Our Decisions.* New York: Harper Collins; Bailey, Warren, Kumar, Alok, and Ng, David. "Behavioral Biases of Mutual Fund Investors." *Journal of Financial Economics* 102, no. 1 (2011): 1–27. https://doi.org/10.1016/j.jfineco.2011.05.00; Kahneman, Daniel, and Egan, Patrick. *Thinking, Fast and Slow.* Vol. 1. New York: Farrar, Straus and Giroux, 2011.

10 Statman, Statman, Meir. *Finance for Normal People: How Investors and Markets Behave.* Oxford University Press, 2017.; Zelizer, V.A., and Dodd, N. *The Social Meaning of Money: Pin Money, Paychecks, Poor Relief, and Other Currencies* (Reprint edition). Princeton, New Jersey: Princeton University Press, 2017.

11 Wilson, T. D. *Strangers to Ourselves: Discovering the Adaptive Unconscious* (New Edition). Cambridge, Mass London: Belknap Press: An Imprint of Harvard University Press, 2004.

- Master lists may help investors refine and focus their goals: People's self-reported goals were often vague in our experiment, and that's a recipe for disengagement. The introduction of a master list seemed to help people understand the underlying purpose of their goals, and this led to them adjusting their goals to ones that were clearer and more precise.

- Master lists may help investors uncover meaningful emotional connections to their goals: We found that many investors updated their goals to ones that were both sensible and aligned with emotionally driven motivations after viewing the master list. This showed that viewing the master list might have stirred up personal connections to goals that they might not have realized when they listed goals off the top of their heads.

About Ray Sin, Ph.D.

Ray Sin is a senior behavioral scientist at Morningstar. His research draws from psychology, economics, and sociology to better understand investor behavior. His goal is to leverage data, guided by social science theories, to generate and experimentally test interventions that help improve investors' success by avoiding common behavioral obstacles. To that end, he has developed subject-matter expertise in two areas: (a) sustainability, aiming to learn how investors think about environmental, social, and governance factors when they invest; and (b) the relationship between financial and non-financial goals, understanding if the pursuit of non-financial goals may lead to positive financial outcomes. Recently, he, together with others, completed an experiment with a nationally representative sample on fee sensitivity and perception of fees.

Ray holds a bachelor's degree in sociology from National University of Singapore, and received his Ph.D., also in sociology, from the University of Illinois at Chicago.

About Ryan O. Murphy, Ph.D.

Ryan O. Murphy, Ph.D., is head of decision sciences for Morningstar Investment Management LLC, a registered investment adviser and subsidiary of Morningstar, Inc., and part of the behavioral insights team. Murphy's research is interdisciplinary, bringing together methods from experimental economics, cognitive psychology, and mathematical modeling to understand how people make decisions and develop ways to improve decision-making.

Before joining Morningstar in 2016, he was the chair of decision theory and behavioral game theory at the Federal Institute of Technology in Zurich, Switzerland, and a visiting professor in the University of Zurich economics department. Previously, he served as associate director of the Center for the Decision Sciences at Columbia University in New York. Murphy has written extensively about human decision-making and has been published in *Management Science*; *Experimental Economics*; *Decision; Judgment and Decision Making*; *Personality and Social Psychology Review*; and the *Journal of Behavioral and Experimental Finance*. He's taught university courses in decision theory, behavioral economics, negotiation analysis, experimental game theory, and statistics.

About Samantha Lamas

Samantha Lamas is an behavioral researcher at Morningstar. She focuses on developing content and conducting research to better understand who investors are and how we can help them reach their financial goals. She began her career at Morningstar as a product consultant working directly with the individual investor and advisor audience segments. Samantha holds a bachelor's degree in business with a concentration in finance from Dominican University.

Morningstar Goal-Identification Worksheet

Here's a printable exercise that advisors can use to nudge their clients toward deeper consideration of what goals are most important to them. This can prompt a meaningful discussion around goal-setting and help people avoid top-of-mind, but superficial, goals.

The desired outcome of this exercise isn't to know, definitively, what a client's top financial goals are. It's designed to begin a conversation that ends with a better understanding of client needs and wants.

Insights gained from this worksheet should not be regarded as prescriptive. They are also not recommendations or endorsements. **Read "Mining for Goals" to find out more about the research behind this worksheet.**

The Worksheet has been reviewed by Finra. A copy of the Finra's corresponding review letter is available upon request

Do You Know Your Financial Goals?

Understanding your financial goals is central to financial planning, but identifying goals that truly matter can be tough. Morningstar's behavioral science team built this exercise to help you identify your top financial goals and uncover goals you might have overlooked.

Instructions

Step 1: List your top three financial goals. We suggest doing this privately, so you don't feel anchored to what first comes to mind or embarrassed if you decide to change your mind later.

Step 2: Take a look at the master list of common financial goals. Are any of the goals on the list important to you? If so, check the box next to those goals.

Step 3: Look at your initial list and master list. Consider the goals you wrote down and the goals you checked. Of these goals, what are the top three? Write them down in order of importance.

Step 4 (optional): Revisit the master list of common financial goals and cross out the goals that are least important to you. Sometimes identifying what you don't care for can help clarify what really drives you and lead to a fruitful conversation with your advisor.

1 What are your top three financial goals?

Most important goal:

Second most important goal:

Third most important goal:

2 Here's a master list of common financial goals. Are there any goals here that are important to you? If so, check the box next to those goals. (Check five at most)

- ☐ To be better off than my peers
- ☐ To pay for personal self-improvement (e.g., go back to school, learn a skill)
- ☐ To experience the excitement of investing
- ☐ To start a new business
- ☐ To buy a house
- ☐ To help pay for my kids' college education
- ☐ To stop working and do something I love
- ☐ To go on a dream vacation
- ☐ To relocate in retirement
- ☐ To care for my aging parents
- ☐ To give to charity or other causes I care about
- ☐ To feel secure about my finances in retirement
- ☐ To feel secure about my finances now
- ☐ To leave an inheritance to my loved ones
- ☐ To retire early
- ☐ To pay for future medical expenses
- ☐ To not be a financial burden to my family as I grow older
- ☐ To manage my debt

3 Look at your initial list and master list. Consider the goals you wrote down and the goals you checked. Of these goals, what are the top three? Write them down in order of importance.

Most important goal:

Second most important goal:

Third most important goal:

The Investor Success Project

Beginning in 2018, Morningstar started rolling out new research on investors—who they are, what their goals are, and how the advisors and asset managers that serve them can make the most impact in helping them reach those goals.

We don't know what we'll find, but we'll share everything we learn. We believe every bit of data that's uncovered can move the industry toward a future that emphasizes investors' front-and-center role in the markets and helps them succeed.

Learn More About The Investor Success Project
morningstar.com/company/investor-success