NATIONAL ENDOWMENT FOR FINANCIAL EDUCATION

Partnering for Financial Well-Being

Quick Takeaways

Cognitive Capabilities, Decision-Making Ability, and Financial Outcomes Across the Lifespan
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Primary Purpose: To explore how differences in decision-making traits translate to real-world financial outcomes.
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Key Findings

- Fluid intelligence – the set of cognitive abilities related to generating, transforming and manipulating new information – falls significantly from age 20 to 70. But a person's accumulation of knowledge and experience, particularly in the financial domain, provides an alternative pathway to making sound financial decisions. In fact, financial literacy's effect on financial decision-making outcomes is more than twice the effect of fluid intelligence.
- This study is the first to combine credit report data with multiple standard measures of fluid intelligence, crystallized intelligence (including financial literacy) and economic preference assessments, such as how much risk people are willing to take and how patient they are in making decisions. Three factors were shown to affect credit scores: age, fluid intelligence and financial literacy, a domain-specific measurement of financial crystallized intelligence. By far, financial literacy had the greatest impact.
- Financial literacy is not just financial experience. To differentiate mere experience from knowledge and expertise, models showed that after separating out financial experience as self-reported on 20 different types of financial instruments, the effect of financial literacy remains significant. This suggests that good financial decisions require understanding financial products, not just experience using them.
- When it comes to economic preferences, people with greater cognitive ability are more patient and more willing to take risks. Additionally, older adults become more risk averse with age, but less loss averse, whereas the relationship between time preference and age is U-shaped: middle-aged adults are more patient than both younger and older adults. Ultimately, the study finds that among these preferences, only patience is relevant to financial outcomes.
- Credit scores are higher for people with patient time preferences.
- The effects of fluid intelligence and financial literacy outweigh personality traits.

For more information and to read the executive summary and final report, visit www.nefe.org.