

Financial Fragility in America

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Background

- The US has been hit hard by the financial crisis and Great Recession
- Data show that large segments of the population continue to face financial difficulties
- Several years after the Recession, many people feel they are not financially secure
- How can we build a more resilient society?

Contents

- Measuring financial fragility
- Data
- Qualitative research
- Implications for policy and programs

Measuring financial fragility

- How **confident** are you that you could come up with **\$2,000** if an unexpected need arose **within the next month**?
 - I am certain I could come up with the full \$2,000.
 - I could probably come up with \$2,000.
 - I could probably not come up with \$2,000.
 - I am certain I could not come up with \$2,000.
 - Don't know.
 - Prefer not to say.



People with these responses are classified as financially fragile.

Why this measure?

- Measuring ability to cope within one month, not immediately
- Measuring ability to cope with a midsize shock (e.g., medical bill or car repair)



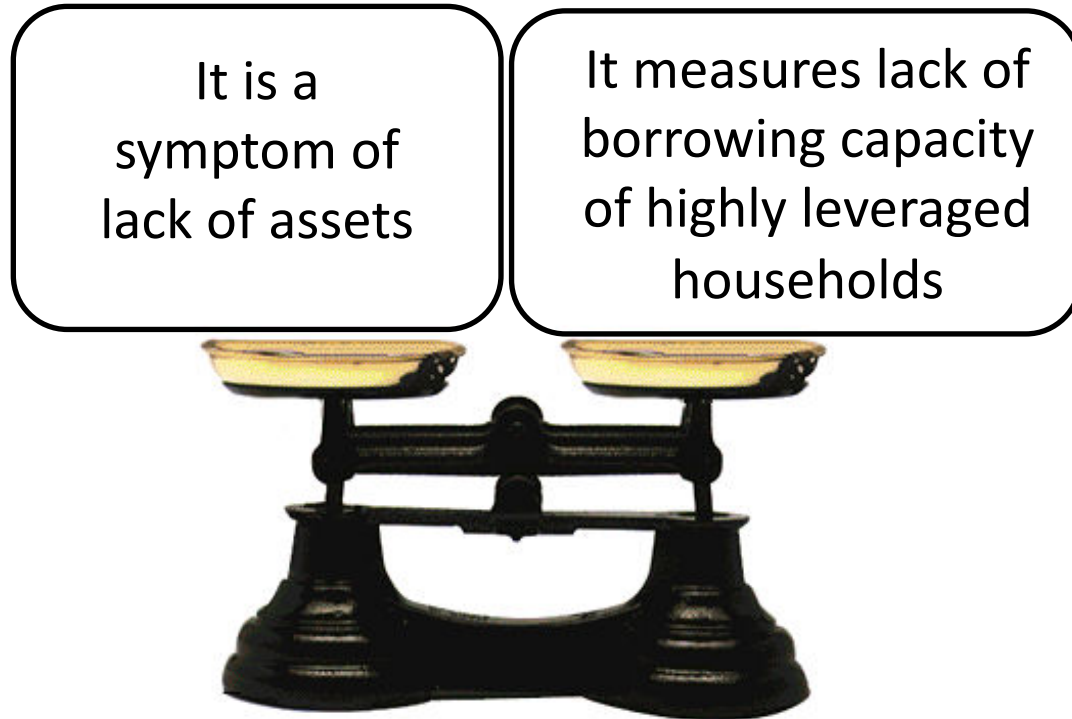
Why this measure?

- We allow for multiple ways to come up with the money, not only precautionary savings
 - Networks (e.g., family, friends)
 - Debt instruments (e.g., credit cards) can play a role



A measure that goes beyond assets

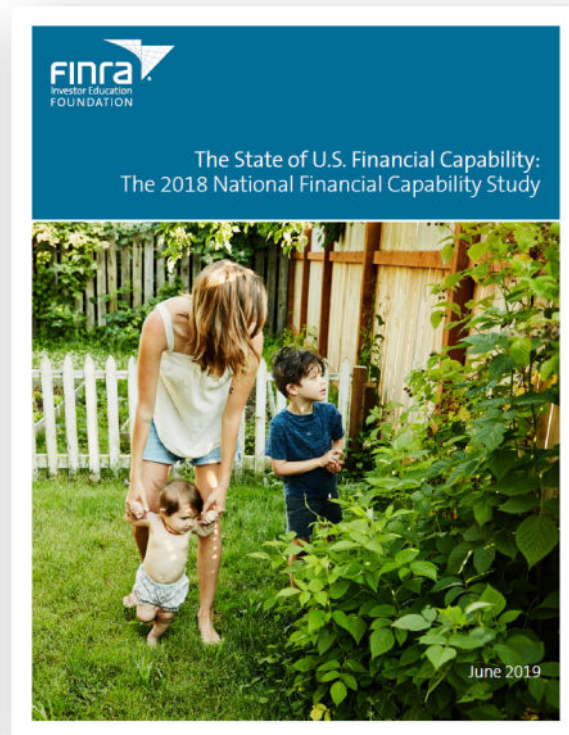
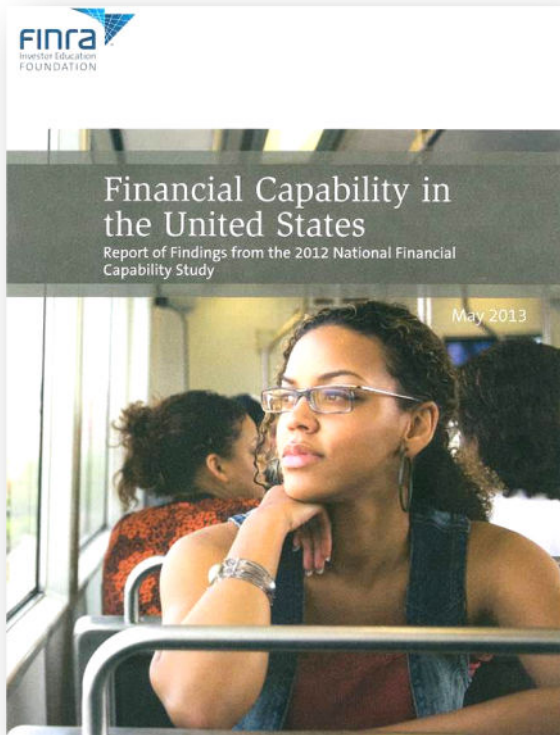
- Financial fragility measures at least 2 aspects of personal finance



Financial fragility and financial satisfaction

- Financial fragility goes beyond looking at one individual behavior, for example saving or borrowing
- Moving toward measuring well-being: this measure also correlates strongly with financial satisfaction
- Financial fragility has consequences!

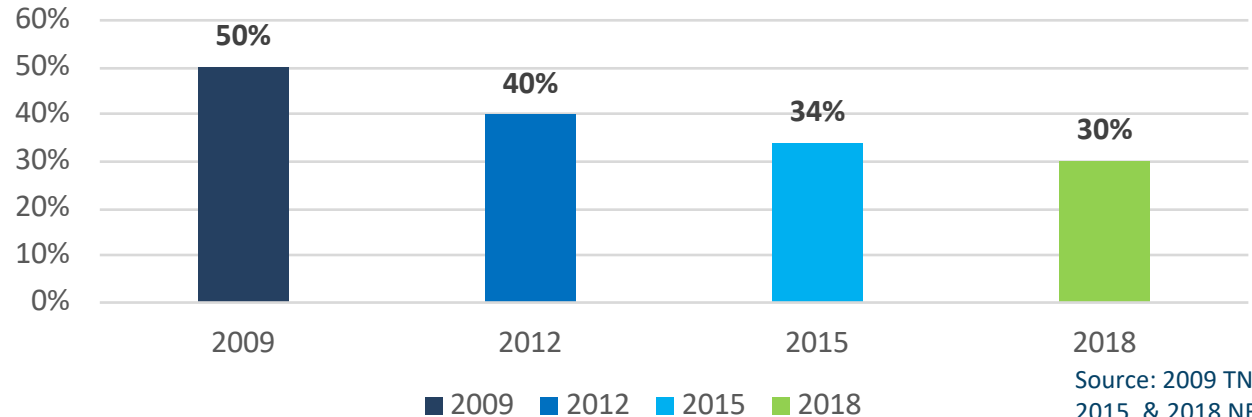
National Financial Capability Study (NFCFS)



Our long term research



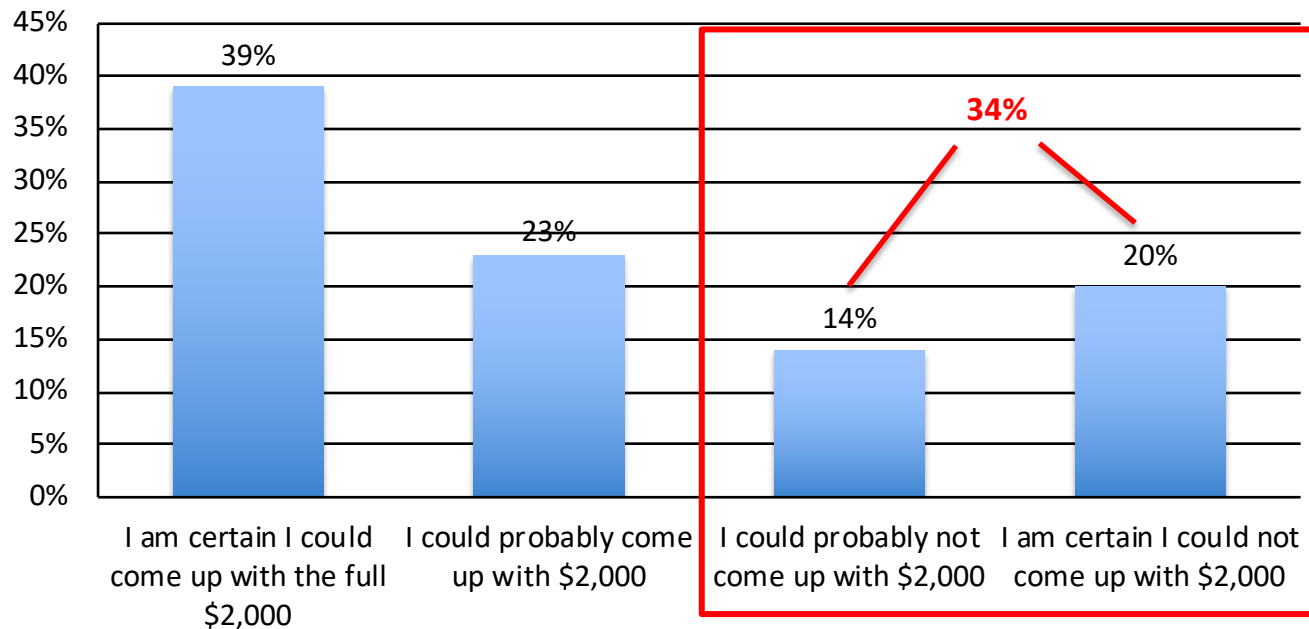
Financial Fragility Over Time



Combining 2009 TNS data with 2012, 2015 and 2018 NFCS data

- Financially Fragile Households: Evidence and Implications. Lusardi, Schneider, and Tufano (2011)
- Document how American households cope with shocks

Financial fragility in the US in 2015



Note: Percentages do not total 100 percent because “do not know” and “prefer not to say” answers are not reported in the figure.

Who are the most financially fragile?

Millennials (age 18-34)

- 43% of Millennials are financially fragile



Women

- 39% of American women are financially fragile vs. 28% of men

Middle-Income (income \$25K-\$75K)

- 33% of middle-income people are financially fragile*

* Age 25-60, 2015 NFCS



Source: 2015 NFCS

...but also



Upper Middle Class

29% of people with income between \$50K and \$100K are financially fragile¹

¹ Sample age 25-60



College Graduates

25% of college graduates age 25-60 are financially fragile



Fully Employed

31% of fully employed people are financially fragile²

² Sample age 25-60

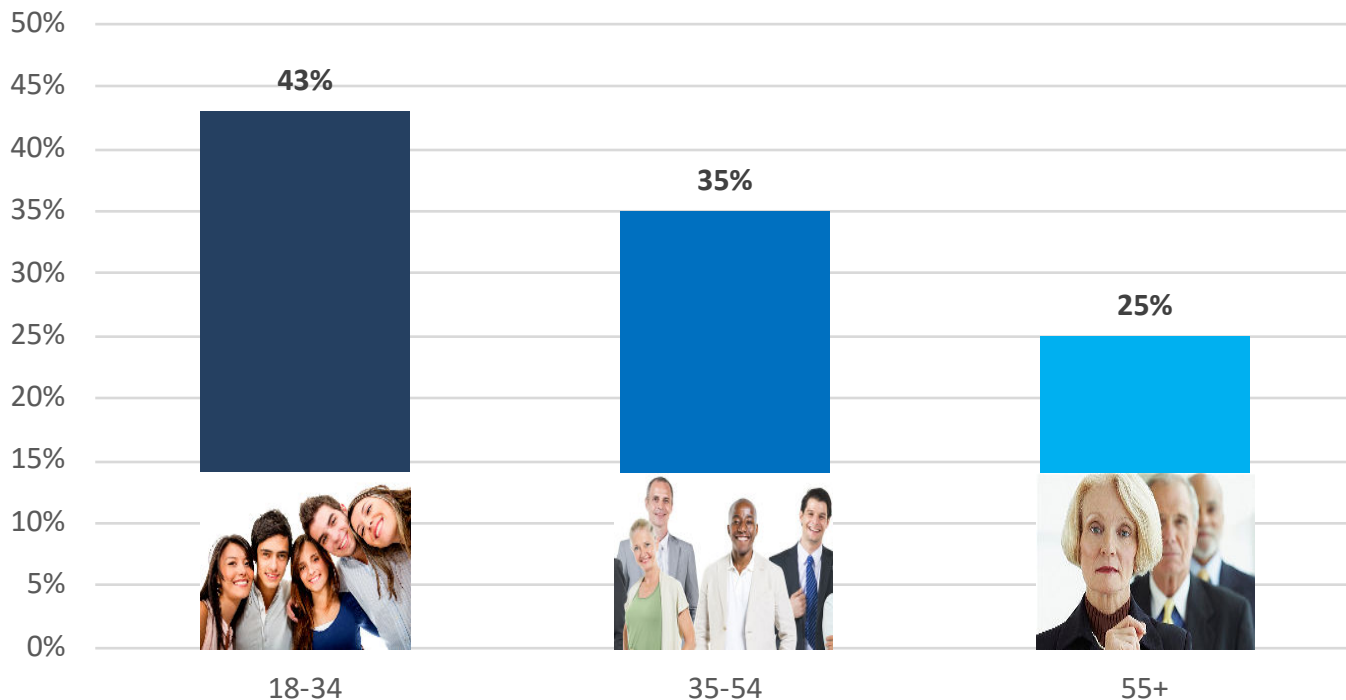


The Unbanked

72% of the unbanked are financially fragile

Financial fragility by age

% of respondents certainly or probably unable to come up with \$2,000 in case of unexpected emergency



Source: 2015 NFCS

Contributing factors for middle-income households

Family size



Debt burden



Financial literacy levels



Contributing factors for middle-income: Family size

- Increasing living costs and tuition fees means raising children requires more financial resources from household
- Across all income categories households with more children are more likely to be financially fragile
- Households with more income have more children
- Higher number of financially dependent children for middle- and high-income households helps explain financial fragility



Contributing factors for middle-income: Debt burden

- 30% of financially fragile households spend more than their income, thus accumulating debt
- 70% of middle- and high-income households state that they have too much debt
- Middle-income households have more assets but these assets are highly leveraged
- Higher proportion of middle-income households overdraw their checking account and have unpaid medical bills
- Close to 40% of financially fragile families across all income categories use costly alternative financial services



Financial fragility and financial literacy



LOW FINANCIAL LITERACY

- **40%** of people who do not know at least 1 of the 3 basic financial literacy concepts (interest, inflation, risk) are financially fragile

Contributing factors for middle-income: Financial literacy

- Financial literacy of financially fragile families is very low
- Low level of financial literacy makes it harder for financially fragile families to manage their many financial demands
- Sharp difference (11%) in level of financial knowledge among households who are fragile and those who are not
- Although financially fragile families carry debt, only 40% know how long it takes for debt to double at a given interest rate.
- Financial literate households are significantly less likely to be financially fragile

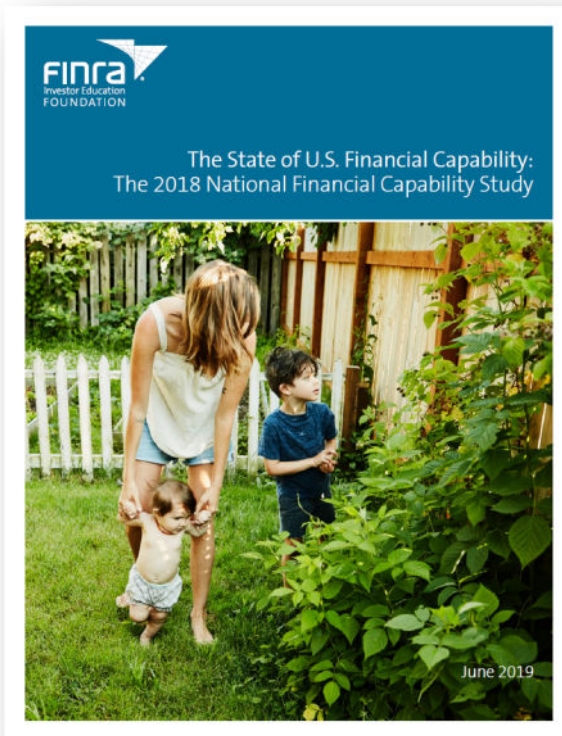


Overall findings

- Women are more fragile
- Those with low income and low educational attainment and the unbanked are financially fragile
- Even the middle class and upper middle class feel fragile
- Having a college degree and a full time job are not guarantees of financial security

2018 NFCS main findings

- For the majority of Americans, financial capability, stability, and confidence are no longer improving in step with the economy.
- Signs of persistent or widening divides between those who are struggling financially and those who are prospering
- More than half (53%) agree that thinking about their finances makes them anxious
- Among student loan holders with payments due, 42% have been late with a payment at least once in the past year
- Percentage of savers with annual incomes under \$25,000 was lower in 2018 than it was in 2009.
- The amount and quality of financial education correlate positively with behaviors indicative of financial capability.



Qualitative in addition to quantitative data



If My Wallet Could Talk

Financial Literacy Month Interview Series



- The financial fragility question was asked in on-the-street interviews

Focus Groups: Financial Situation

- We did focus groups in 3 cities (Austin, Baltimore, Cincinnati) among young, women, and blue collar workers

- **Income:**

- Variability in income and employment = Uncertainty
- Various forms of public assistance



- **Expenses:**

- Rent/mortgage biggest expense (~50%)
- Spending on potentially avoidable expenses
- CC debt is a large burden on the balance sheet

- **Making ends meet:**

- Constant balancing act
- Increasing expenses, stagnant income
- Prioritizing and cutting expenses



Focus Groups: Coping with Fragility

- **Methods:**

- Working longer hours/additional job
- Borrowing
- Retirement account withdrawals



- **Capacity:**

- Ability to pay emergency expense with checking/savings account
- Over 50% cannot cover a \$100 emergency expense



- **Mechanisms:**

- Unable to pay (40%)
- CC debt paid over time (24%)
- Borrow from friends/family (13%)



Focus Groups: Savings behavior

Difficult to save for a number of reasons:

- Desire to save but unable due to unforeseen expenses
- No desire to save (focus on the short-term)
- Saving for the long-term, but not emergencies
- Spending as reward for fragility coping difficulties
- Difficult to budget expenses due to income variability
- No incentive to save any windfall



Case Study: 2019 Government Shutdown

Federal workers line up for free meals, visit food banks as shutdown hits Day 28



62% of federal workers say they used up all or most of their savings during the government shutdown

The Shutdown Showed How Precarious Americans' Finances Really Are



Government shutdown exposed Americans' deep savings crisis



Implications for financial education

- Financial fragility is pervasive
 - Need robust interventions
- People use many methods of coping
 - Need to move away from targeting one behavior
- Some of the methods people use are very expensive and do not provide insurance
 - Credit becomes expensive when most needed
- Do not underestimate the power of family, friends, people around us. After all, we insure by pooling resources!

Implications for financial education (cont.)

- Importance of targeting women
 - Multiplier effect
- Importance of equipping the young with the skills to succeed in today's complex financial markets
 - Importance of financial education in school

Additional implications

- Implications for policy
 - Incentives for short-term savings
 - Stress test for households' financial capability
- Implications for research
 - Financial fragility question could be used in many surveys
- Implications for pension design: people do not have liquidity to deal with short-term shocks
- Moving toward measuring well-being: this measure also correlates strongly with financial satisfaction

Life sometimes is a storm



The Storm on the Sea of Galilee
Rembrandt, 1633

**Should financial resilience be
part of public policy?**