Financial Fragility in the US: Evidence Beyond Asset Building

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Financial fragility is the inability to cope with *emergency expenses* (such as a car or house repair, medical bill, or small legal expense) in a short timeframe

**Background:**

- This measure was piloted in the 2009 TNS Global Economic Crisis Study.
- In 2009 almost 50% of U.S. households were classified as financially fragile.
Online nationally representative sample of more than 27,500 respondents.

Commissioned by FINRA Investor Education Foundation.

Offers unique information on financial literacy and capability.

It started in 2009, financial fragility question asked in 2nd wave in 2012 and 3rd wave in 2015.

Sample restriction: Non-retired individuals age 25-60. “Do not know” and “refuse to answer” responses for the fragility question are excluded.
The measure of 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

Financially fragile
Financial fragility in the U.S.

Response to financial fragility question ($2,000/30 days)

35.7% are financially fragile

Financial fragility is still **prevalent** in a recovering economy and not only a result of the recession.

Source: NFCS 2015
Financial fragility across age

- A similar fraction of individuals across all ages are financially fragile.
- Fragility is slightly higher in the middle age group of 40- to 49-year-olds. (Confirmed in regression results)
- Middle-aged individuals are at the peak of financial obligations such as child care costs, student loan repayments, and mortgage payments.

Source: NFCS 2015
Financial fragility across education levels

- Significantly lower likelihood of being financially fragile with increasing education.
- Effect is highly significant even after controlling for income.
- Substantial educational divide between those who attended college but did not receive a degree and those who received at least a Bachelor’s degree.

Source: NFCS 2015
Financial fragility across household income

- Financial fragility falls with income but is still high for the middle-income households.
- Nearly 30% of middle-income and 20% of high-income households are financially fragile.
- This is notable, especially when comparing the relative magnitude of the emergency expense ($2,000) to a household’s income level. Thus, financial fragility is not only caused by a lack of assets.
Contributing factors for relatively high financial fragility rates among middle-income households:

(A) Family size:
- Households with more children are more likely to be financially fragile – fixed family budgets and financial obligations (child care costs and education).
- Financially fragile middle- and high-income households are more likely to have more children.

(B) Debt and debt management, in addition to asset levels, affect ability to manage short-term shocks:
- Middle-income households have assets, but they are often highly leveraged.
- Debt does not decrease, but in fact increase with income.
(B) The importance of debt and debt management

### Homeownership

<table>
<thead>
<tr>
<th>Household income</th>
<th>Homeowner</th>
<th>Home mortgage*</th>
<th>Late with mortgage payments*</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;$50K</td>
<td>33%</td>
<td>55%</td>
<td>36%</td>
</tr>
<tr>
<td>$50-75K</td>
<td>79%</td>
<td>57%</td>
<td>34%</td>
</tr>
<tr>
<td>&gt;$75K</td>
<td>86%</td>
<td>70%</td>
<td>33%</td>
</tr>
</tbody>
</table>

### Retirement Savings

<table>
<thead>
<tr>
<th>Household income</th>
<th>Retirement savings (DB, DC, IRA)</th>
<th>Loan*</th>
<th>Hardship withdrawal*</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;$50K</td>
<td>30%</td>
<td>13%</td>
<td>13%</td>
</tr>
<tr>
<td>$50-75K</td>
<td>68%</td>
<td>20%</td>
<td>14%</td>
</tr>
<tr>
<td>&gt;$75K</td>
<td>83%</td>
<td>25%</td>
<td>17%</td>
</tr>
</tbody>
</table>

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**Financially fragile respondents**

<table>
<thead>
<tr>
<th></th>
<th>Income</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>&lt;$50K</td>
</tr>
<tr>
<td>Unpaid medical bills</td>
<td>38%</td>
</tr>
<tr>
<td>Expensive credit card behavior*</td>
<td>68%</td>
</tr>
<tr>
<td>Use of alternative financial services</td>
<td>42%</td>
</tr>
</tbody>
</table>

Source: NFCS 2015
Contributing factors for relatively high financial fragility rates among middle-income households:

(A) Family size:
   • Households with more children are more likely to be financially fragile – fixed family budgets and financial obligations (child care costs and education).
   • Financially fragile middle- and high-income households are more likely to have more children.

(B) Debt and debt management, in addition to asset levels, affect ability to manage short-term shocks.
   • Middle-income households have assets, but they are often highly leveraged.
   • Debt does not decrease, but in fact increase with income.

(C) Financial literacy levels are very low especially among financially fragile households.
(C) The importance of financial literacy

First three questions correct (interest, inflation, risk)

- Financial literacy is low overall. Even among high-income and non-fragile.
- Significant difference between financially fragile and non-fragile.
- Financially literate households are significantly less likely to be financially fragile and this holds for all income levels.
- This effect is independent of the effect that overall education has on fragility.

Dependent variable: Financial fragility (dummy = 1 for financially fragile respondents)

Income

<table>
<thead>
<tr>
<th>Household income</th>
<th>Non-fragile</th>
<th>Fragile</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;$50K</td>
<td>26%</td>
<td>17%</td>
</tr>
<tr>
<td>$50-$75K</td>
<td>33%</td>
<td>23%</td>
</tr>
<tr>
<td>&gt;$75K</td>
<td>50%</td>
<td>30%</td>
</tr>
</tbody>
</table>

Financial literacy:

First three questions correct (interest, inflation, risk)

<table>
<thead>
<tr>
<th>Income</th>
<th>0.097***</th>
<th>0.046**</th>
<th>0.043***</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;$50K</td>
<td>(0.017)</td>
<td>(0.019)</td>
<td>(0.010)</td>
</tr>
<tr>
<td>$50-$75K</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt;$75K</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Controls

<table>
<thead>
<tr>
<th>Yes</th>
<th>Yes</th>
<th>Yes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Observations</td>
<td>6,874</td>
<td>3,519</td>
</tr>
<tr>
<td>R-squared</td>
<td>0.085</td>
<td>0.075</td>
</tr>
</tbody>
</table>

Source: NFCS 2015. Robust standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1
Financial fragility is prevalent in a recovering economy and not only a result of the recession.

A broad cross-section of the population is financially fragile. It is not only a problem of the young, low-income, and low-education.

Financial fragility has short- and long-term consequences. It is associated with a lower likelihood of planning for retirement.

Recommendations:

- Financial education in schools, colleges, and the workplace, especially targeting the vulnerable subgroups.
- Tools that incentivize precautionary savings: Institutionalizing short-term savings in a manner similar to retirement accounts.
- Promoting financial planning to help reduce debt levels.

Conclusion
Thank you!

Questions? Contact me at ahasler@gwu.edu