LIVING ON THE EDGE:
Financial Fragility in America

NATIONAL ENDOWMENT FOR FINANCIAL EDUCATION

ABOUT THIS EXECUTIVE SUMMARY

This summary presents key findings from *Financial Fragility in the US: Evidence and Implications* by Raveesha Gupta, M.A., Andrea Hasler, Ph.D., Annamaria Lusardi, Ph.D. and Noemi Oggero, M.Sc. at the Global Financial Literacy Excellence Center, The George Washington University School of Business.

The full report, available at NEFE.org, documents research funded by the National Endowment for Financial Education® (NEFE®) to explore the extent of financial fragility in American and to understand its determinants.

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Living on the Edge: Financial Fragility in America

Too many Americans are living on the edge of financial fragility, the inability to cope with unexpected expenses. No group is immune: Financial fragility affects all ages, income levels, genders and education levels. Overall, 36 percent of working adults in the United States could not cover the cost of a midsize budget shock, such as a car or house repair, a medical bill or a legal expense, within a month.

This study reveals that financial fragility is linked to having too few assets, too much debt and/or low levels of financial literacy. While this vulnerability is more prevalent among women and those with low income or low education, this study shows that a broad cross-section of the American population is at risk, including middle-aged and middle-income families.

The inability to deal with budget shocks matters. For some families, something as small as a traffic ticket can create a short-term crisis that can snowball for several months. In the long term, financially fragile families are less likely to plan for retirement, jeopardizing their future stability.

Increasing Americans' financial literacy can improve — and perhaps prevent — many situations of financial fragility. In fact, financial literacy significantly lowers the likelihood of individuals being financially fragile. Planning ahead and building precautionary savings can lower the need for using credit, borrowing from friends and family or working multiple jobs, improving not only the household's financial situation, but its quality of life as well.

Defining Financial Fragility

Financial fragility is measured by an individual's ability to cope with unexpected expenses in a short timeframe.

Specifically, the study examines individuals' ability to come up with $400 immediately in case of an emergency, and their capacity to come up with $2,000 in 30 days.

Coping sources for the immediate timeframe include:

- charging to a credit card and repaying the amount in full with the next statement
- using cash or savings currently in checking/savings accounts
- taking on long-term credit card debt and paying it off eventually
- using a bank loan or line of credit
- borrowing from a friend or family member
- using alternative financial services
- selling something they own

The 30-day timeframe allows individuals to assess potential income and debt and consider the different resources they would access to raise $2,000. It also helps study more nuanced factors such as respondents' confidence level and expectations for future finances.

This study uses two nationally representative surveys:

THE 2015 NATIONAL FINANCIAL CAPABILITY STUDY (NFCS)* ASKS:

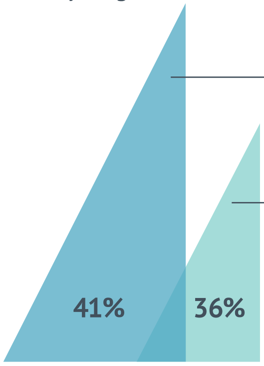
"How confident are you that you could come up with $2,000 if an unexpected need arose within the next month?"

Those who say they probably could not or certainly could not come up with $2,000 are considered financially fragile.

THE 2015 SURVEY OF HOUSEHOLD ECONOMICS AND DECISIONMAKING (SHED)* ASKS:

"Suppose that you have an emergency expense that costs $400. Based on your current financial situation, how would you pay for this expense?"

Those who respond with any but the first two coping strategies listed above (charging a credit card and repaying the amount in full with the next statement; using cash or savings currently in checking/savings accounts) are considered financially fragile.



Using the SHED, **41 percent** of American households are financially fragile.

Using the NFCS, **36 percent** of American households are financially fragile.

Focus Groups:

Additionally, data from the surveys were complemented with qualitative information from focus groups conducted in three American cities: Austin, Baltimore and Cincinnati. Focus group participants are classified as financially fragile and belong to vulnerable population subgroups: women, low-income workers and young people.

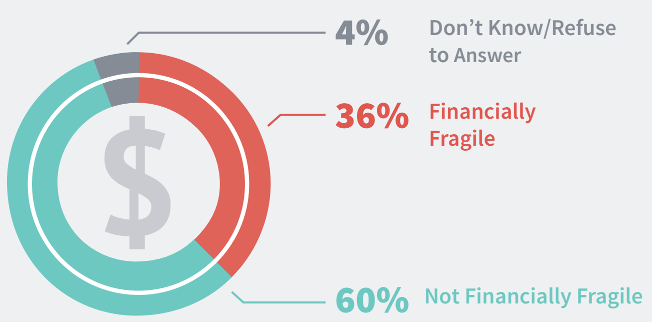
*Note: Researchers focused on 25- to 60-year-olds from each data set throughout this study. See "About This Study," back cover, for more information.

Who is Financially Fragile?

More than one-third (36 percent) of Americans are financially fragile. This number has dropped since 2009 during the Great Recession, when nearly 50 percent of working-age adults were considered financially fragile. However, given the steady recovery of the U.S. economy after the recession, the pervasiveness of weak personal finances is concerning.

Financial fragility is not a problem contained to those with low levels of income or low levels of education: It is prevalent among a broad cross-section of the population. To identify particularly vulnerable subgroups, researchers examined fragility among households by income, age, gender and educational attainment.

FINANCIAL FRAGILITY IN THE UNITED STATES

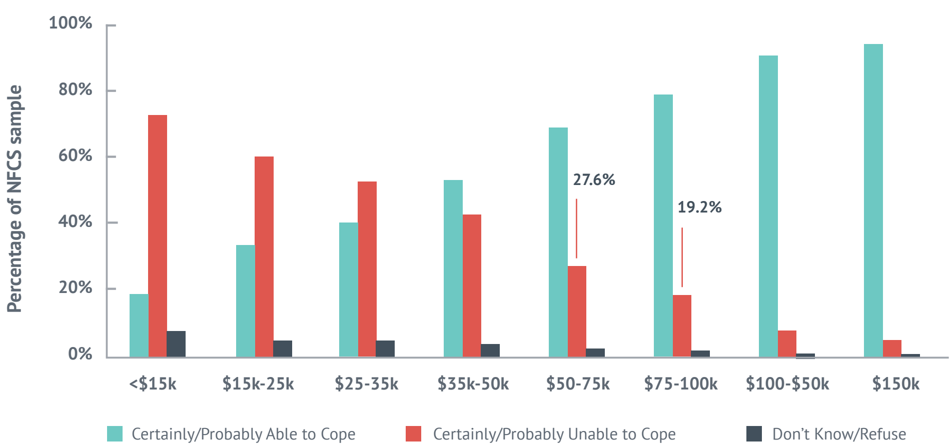


Source: NFCS 2015

INCOME

The likelihood of being financially fragile drops steadily with rising income levels. However, having higher income does not necessarily translate into being financially resilient. Rates of financial fragility are still high for middle- and high-income households.

Income Level and Ability to Cope



Source: NFCS 2015

INCOME LEVELS		
Low income	Middle income	High income
<$15,000	$35–50,000	$75–100,000
$15–25,000	$50–75,000	$100–150,000
$25–35,000		>$150,000

KEY FINDINGS:

- The data show a higher likelihood for financial fragility at income levels below the $50,000 mark.
- The likelihood of being financially fragile decreases steadily with increasing income, and all differences compared to the lowest income group are statistically significant.
- Almost 30 percent of middle-income households (with income in the $50,000–75,000 range) and 20 percent of those with income in the $75,000–100,000 range are financially fragile.

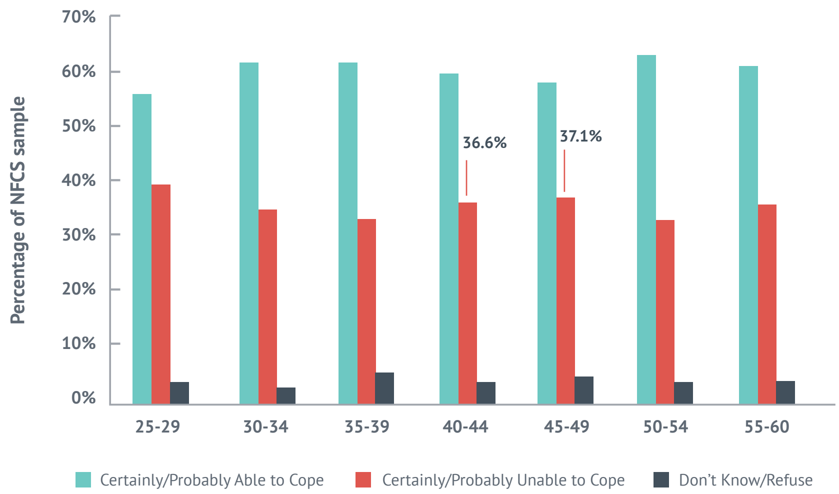
Note: The median household income for 2015 was close to $56,000. Household income includes:

- Wages
- Investment income
- Public assistance
- Retirement plan funds

AGE

Financial fragility is nearly equally distributed across all ages, although fragility is slightly higher in the middle age band of 40- to 49-year-olds.

Age Bands and Ability to Cope



Source: NFCS 2015

AGE BANDS		
Young	**Middle**	**Older**
25-29	40-44	50-54
30-34	45-49	55-60
35-39		

KEY FINDINGS:

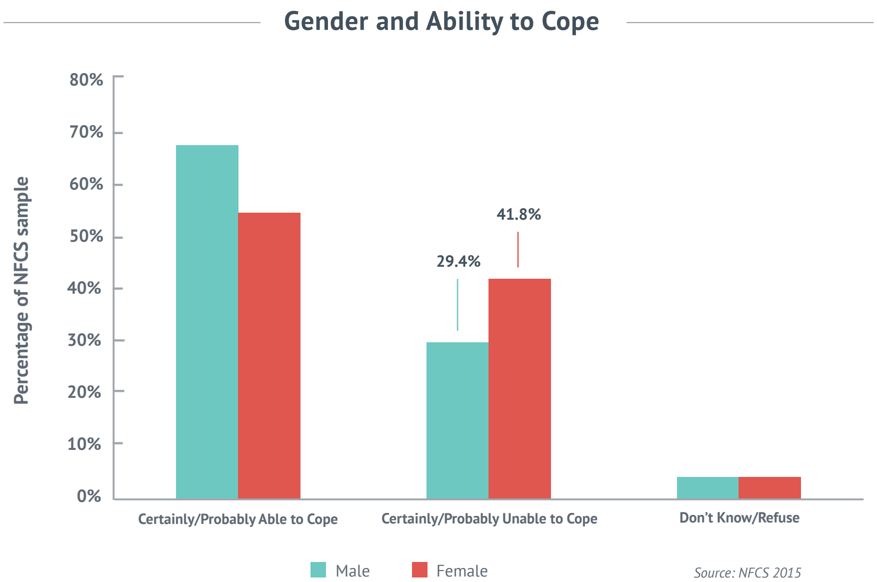
- People of all age bands are financially fragile at comparable levels, despite the expectation that people earn and accumulate more money as they get older.
- Only the middle age band has a significantly higher likelihood of financial fragility compared to the youngest age band, likely because these individuals are at the peak of financial obligations such as child care costs, student loan repayments and mortgage payments.
- Each dependent child makes middle aged respondents more likely to be fragile, compared to other age bands which are not significantly affected by financially dependent children.
- Income, up to the $50,000 mark, has the least effect on financial fragility for the middle age band.

"I would like to be comfortable and not walking on eggshells or sweating"

– Focus group participant, Austin

GENDER

Women are substantially more financially fragile than men.

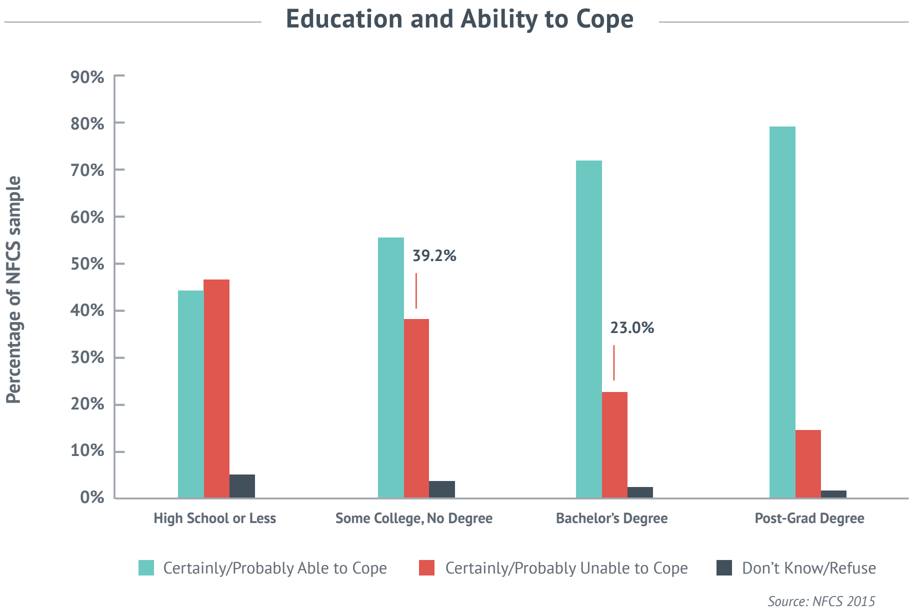


KEY FINDINGS:

- 42 percent of women versus 29 percent of men are financially fragile.
- Women in the 40- to 44-year-old age group are more likely to be financially fragile than women in the youngest cohort (ages 25–29).
- Marriage makes women less likely to be financially fragile, while there is no significant effect for men.
- Employment of any kind makes women less likely to be financially fragile.

EDUCATIONAL ATTAINMENT

Increasing education levels reduce the likelihood of being financially fragile.



KEY FINDINGS:

- The higher the educational attainment, the lower the probability of being financially fragile.
- Having a college degree reduces financial fragility over high school only, assuming that all other household characteristics are identical.
- There is a substantial divide between those who earn a bachelor's degree and those who attend college but do not get a degree. Specifically, 40 percent of those who have some college education (but no degree) versus 23 percent of those who have a bachelor's degree were classified as financially fragile.
- The effect of education is observed even after controlling for income, implying that there are components of education that can affect financial fragility beyond an increased earning potential.

OTHER KEY VARIABLES

ETHNICITY: Financial fragility ranges from an average of 24 percent among Asians to 34 percent among whites to 37 percent for Hispanics to 47 percent for African-Americans.

MARRIAGE: Marriage affects financial fragility. More than 68 percent of married individuals are not financially fragile, compared to 50 percent of unmarried individuals.

CHILDREN: Compared to those without financially dependent children, the ability to cope with an unexpected expense rises slightly for those who have up to two dependent children and then begins to fall. The average likelihood of a household being financially fragile rises for those with three or more financially dependent children.

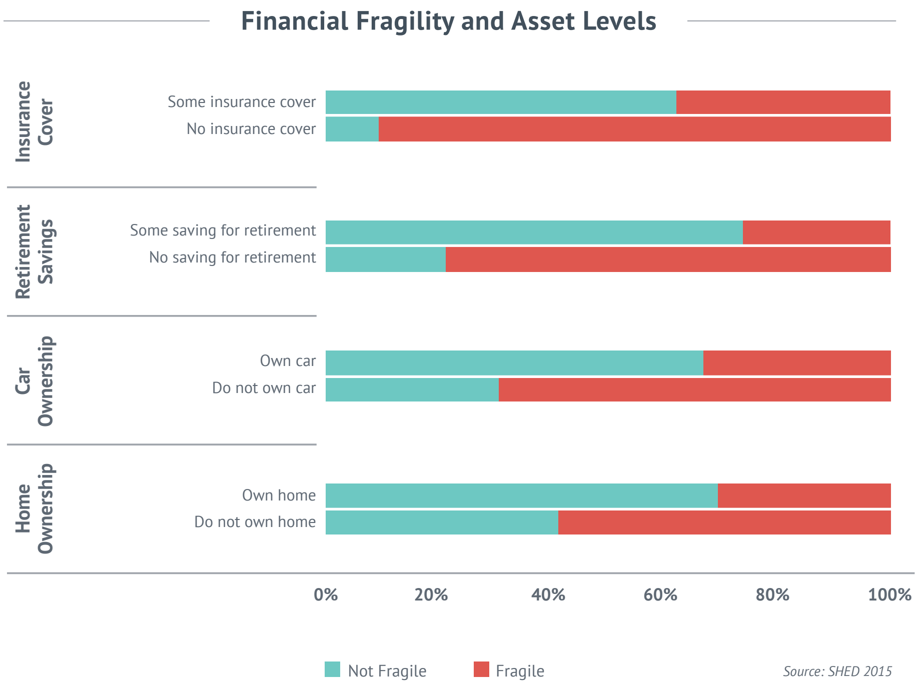
EMPLOYMENT: 54 percent of unemployed individuals are financially fragile, compared with 28 percent for those who are employed.

What Causes Financial Fragility?

To uncover the root causes of fragility, researchers studied nondemographic factors of financial fragility: lack of assets, too much debt and lack of financial literacy. Indebtedness and too few assets in particular play a significant and complementary role in explaining financial fragility, indicating that the likelihood of being financially fragile may be driven by both the asset and the debt side of a household's balance sheet.

LACK OF ASSETS

Financial fragility can be attributed to a combination of low savings and assets, as well as a lack of insurance coverage.



KEY FINDINGS:

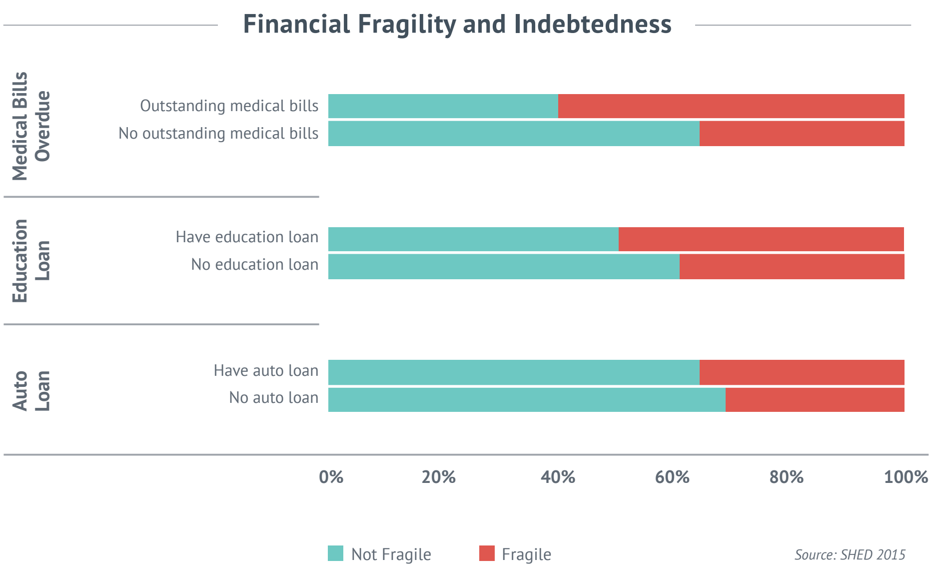
- The majority of financially fragile individuals have fewer assets. This is not limited to lack of a house or car, but also includes the lack of a bank account, credit card, insurance or retirement account.
- Financially fragile people have a much lower borrowing capacity. Many do not use a credit card and were either denied credit or given less than the amount they applied for, rather than having unrestricted access to credit.

“It’s like being on a balance beam.”

– Focus group participant, Austin

DEBT

People who are highly indebted or have large payment obligations also have difficulty managing unexpected expenses.

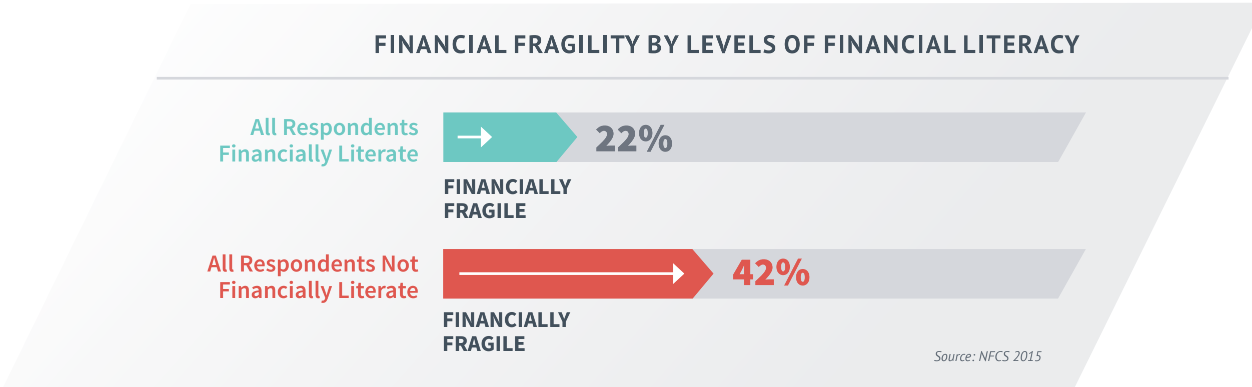


KEY FINDINGS:

- Medical debt makes respondents more likely to be financially fragile.
- Almost 50 percent of those with education debt do not have the liquidity to deal with a $400 emergency expense, versus 39 percent of those without education debt.

LOW FINANCIAL LITERACY

Financial literacy significantly lowers the likelihood of being financially fragile, independent of education levels.



KEY FINDINGS:

- People who are financially literate are significantly less likely to be financially fragile: 22 percent of those who are financially literate are financially fragile, compared to 42 percent of those who are not financially literate.
- The effect of financial literacy is independent of the effect that overall educational attainment has on fragility.
- Financial literacy improves respondents' chances of being able to cope with emergency expenses over all age categories.
- Financial literacy seems to be highly beneficial for women, decreasing their chances of being financially fragile at higher rates than for men.

Consequences of Financial Fragility

The short-term effects of financial fragility are immediate and ongoing. It is not hard to imagine how a sudden, unexpected expense such as a medical bill, car repair or home maintenance emergency could ripple through a household's finances. Such an expense also can lead to a chain of events that perpetuates the fragile state — for the individual and, potentially, their children.

For example:

- An inability to pay medical bills leads to avoidance of medical care and declining health, which ultimately affects job prospects.
- A car accident leads to the loss of a vehicle and potentially to job loss due to lack of transportation to work.
- An inability to pay rent affects creditworthiness and results in higher interest rates on future loans.

But the long-term consequences of fragility are equally worrisome. Financially fragile households are significantly less likely to plan for retirement. With more and more Baby Boomers reaching retirement age every day, and Gen Xers not far behind, the effects of fragility likely will be widespread.

FINANCIAL FRAGILITY UNDERMINES RETIREMENT PLANNING

Those who are financially fragile are almost 18 percentage points less likely to plan for retirement.

INCOME AND INCOME SHOCKS

- Planning for retirement rises with increasing income.
- The highest income levels are more likely to plan for retirement than the lowest income level.
- Respondents are more likely to plan for retirement if they have experienced financial distress such as an income shock or outstanding medical bills.
- Experiencing an income shock within the past year increases the probability of planning for retirement.

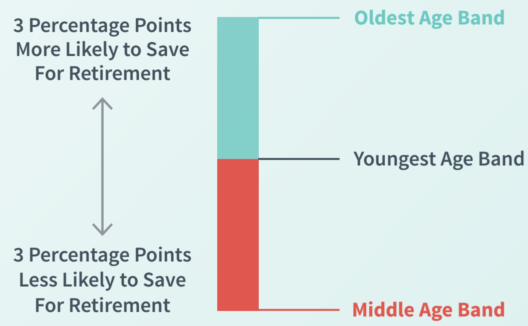
EDUCATION

- Higher education — even when not completed — improves retirement planning.
- Those with a bachelor's degree are more likely to plan for retirement than those with a high school education or less.
- Those who attend college but do not receive a degree are more likely to plan for retirement than those with a high school education or less.

FINANCIAL LITERACY

- The effects of financial literacy are noticeably significant; regardless of education levels, financially literate respondents are more likely to plan for retirement.

**FINANCIAL FRAGILITY:
RETIREMENT PLANNING BY AGE GROUP**

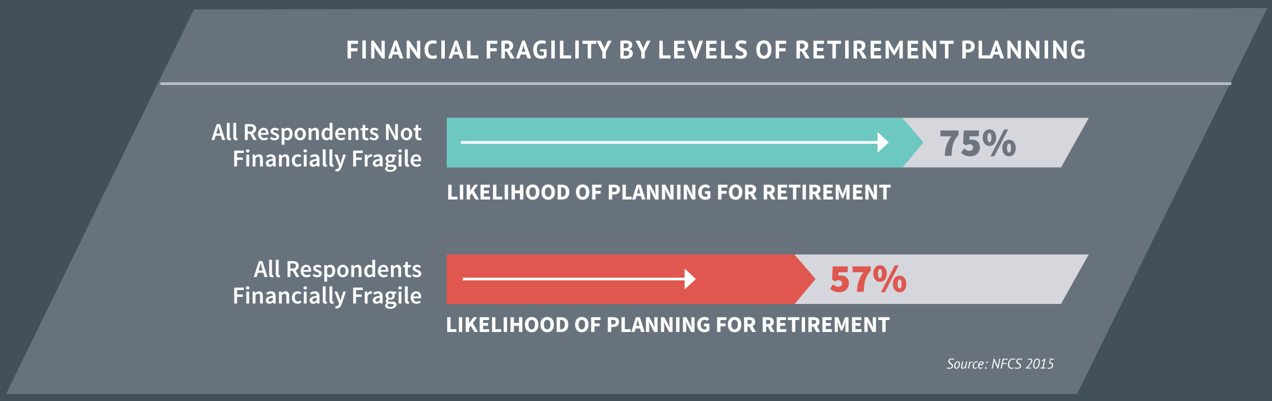


AGE

- The oldest cohort (ages 55–60) is more likely to plan for retirement than the youngest cohort.
- The middle age band is less likely to plan for retirement than the youngest cohort.
- There is a drop in the likelihood of planning for retirement between those in the 35–39 age band and individuals who are 45 to 49 years old.

GENDER

- Women are less likely to plan for retirement than men.



Implications and Takeaways

Despite ten years of economic recovery since the Great Recession, people of all age bands and income levels are struggling. Financial fragility is a pervasive and complex problem that affects nearly 40 percent of the U.S. working-age population.

Households living on the edge of financial fragility spend more time and money dealing with income shocks and save less for retirement, affecting both short-term and long-term financial stability. Vulnerability to small and midsize income shocks is linked to too few assets, too much debt and/or low levels of financial literacy.

Many intermediaries in financial capability are working closely with American families to reduce their debt and increase their assets. Personalized guidance can lead to significant success for individuals and households, particularly when it includes financial education.

It is encouraging and significant that higher financial literacy reduces the likelihood of financial fragility for people of all incomes and education levels. Many excellent financial education resources are available in communities and on the internet, and are delivered in schools, universities and colleges, and workplaces. Financial education can be delivered to many people at once; it does not require one-on-one instruction to be effective.

> “I think paranoia is a good word for it. I can make it through the month if nothing goes wrong.”
>
> *— Focus group participant, Baltimore*

REAL PEOPLE, REAL CHALLENGES

Focus groups were conducted among financially fragile individuals from particularly vulnerable subgroups to enhance understanding of the data results.

INCOME SOURCES

- Many had income consisting of multiple low-paying, part-time jobs.
- Others had full-time but seasonal or hourly employment, often supplemented by additional side jobs.
- There was inherent vulnerability in respondents’ income if they were unable to secure the hours they needed.

MAKING ENDS MEET

- Overall, respondents appeared to be engaged in a constant balancing act to make ends meet.
- There was a shared perception that the cost of living continues to rise, but incomes are not increasing.
- A common strategy for making ends meet was prioritizing which bills to pay and when to pay them.
- In general, respondents seemed to think they could manage their “normal” expenses, but did not appear to plan for “unexpected” expenses, which occur fairly frequently.

EXPENDITURES AND DEBT

- Housing was a large part of their expenses. Respondents also mentioned auto-related expenses and health insurance costs.
- For respondents who had them, children were a major expense category.
- Many respondents also were burdened by credit card debt, with student loans as another frequently cited source of debt.

SPENDING VERSUS SAVING

- Respondents found it difficult to save for a number of reasons. Among them, respondents felt that there were other expenses that would need to be taken care of first.
- Others preferred to focus on the short term and did not see the point in saving.
- Respondents tended to rationalize nonessential spending as "rewards" that they deserve for their hard work.

PAYING FOR UNEXPECTED EXPENSES

- Working more and borrowing were the most common strategies for covering unexpected expenses.
- Some respondents could count on family and friends to help.
- Loans from various sources were another strategy for covering an unexpected expense.

TALKING ABOUT FINANCIAL FRAGILITY

- Respondents spoke of the stresses and struggles of getting by.
- Some used imagery of working hard to maintain financial "balance."
- Others evoked images of being overwhelmed or submerged, while others spoke of feeling depressed or embarrassed.
- Younger respondents were relatively more optimistic about the future.

FINANCIAL ADVICE AND EDUCATIONAL RESOURCES

- Respondents overwhelmingly thought financial advisors were for people with money, and therefore not applicable to their own situation.
- Respondents appeared to be open to the idea of financial education help for their particular situation, although most did not believe that this currently exists.

Key Opportunities for Action

Financial education is our strongest weapon against financial fragility. Community leaders, parents, educators and intermediaries can:

- Promote and implement effective financial education that contains five key factors:
  - Well-trained educator and/or tested e-learning protocol
  - Vetted/evaluated program materials
  - Timely instruction
  - Relevant subject matter
  - Evidence of impact (evaluation)
- Identify and share approaches that are effective, and experiment and evaluate new and innovative approaches.
- Supplement school-based financial education with financial education in family and community settings.
- Encourage future planning as one of the educational concepts. Emphasize the benefits of short-term and long-term savings. Encourage automatic savings through paycheck deductions or apps that transfer funds to savings.
- Consider the unexpected financial fragility of certain groups, such as middle aged and middle income. For example, even in their prime earning years, Gen Xers manage increased financial responsibilities, potentially leading to new vulnerabilities. Prepare at-risk learners to expect and plan for financially fragile circumstances.

ABOUT THE STUDY

This study, funded by the National Endowment for Financial Education® (NEFE®), analyzes two nationally representative data sets:

The National Financial Capability Study (NFCS) — 2015 data

- A nationwide survey conducted every three years commissioned by the FINRA Investor Education Foundation
- 2015 survey sample was 27,564 American adults
- Includes a question on coming up with $2,000 in 30 days, as well as financial literacy questions

The Survey of Household Economics and Decisionmaking (SHED) — 2015 data

- Online survey conducted annually since 2013 by the Federal Reserve Board
- 2015 survey sample was 5,642 American adults
- Includes a question on the $400 immediately measure

From these data, the researchers focused on individuals who are in their prime working years (ages 25–60) and not retired. (Those who are younger or older are excluded from the sample as their characteristics, financial behavior and needs can be very different. People under 25 may be students with no labor income, while those over 60 may be retired and receiving Social Security benefits.) The 25- to 60-year-old population comprises a more homogenous sample.

The research team also supplemented the quantitative data with six focus groups in three cities — Baltimore, Cincinnati and Austin — where financially fragile groups of low-income workers, women and young people were interviewed about their personal finances and coping methods.

The study's investigators are Raveesha Gupta, M.A., Andrea Hasler, Ph.D., Annamaria Lusardi, Ph.D., and Noemi Oggero, M.Sc., of the Global Financial Literacy Excellence Center (GFLEC) at the George Washington University School of Business.

See the final report at **www.nefe.org/what-we-provide/research** for complete methodology.

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