How the Pandemic Altered Americans' Debt Burdens and Retirement Readiness

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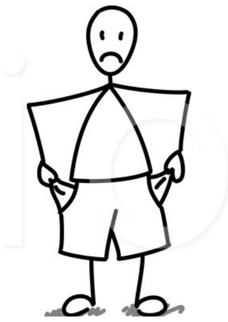
Motivation:

- Access to credit easier & more widespread:
    - Credit cards,
    - Floating and subprime mortgages,
    - Student loans,
    - Online apps,
    - Payday loans, rent-to-own, etc.
- Borrowing decisions increasingly in individuals' hands.
- Rising complexity of financial decisions and products.
- Failure to repay debt has consequences: bad credit scores, default, bankruptcy.

Pre-COVID-19, we found that:

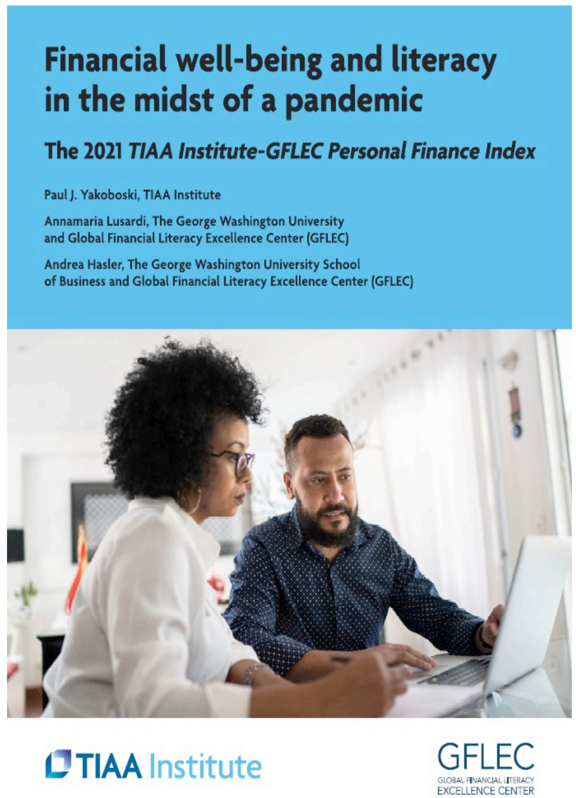
- About 1 of 3 families were *financially fragile*, i.e., could not face an emergency expense.
- A majority of Americans (61%) had not tried to figure out how much to save for retirement.
- Over time, more older people have carried debt into retirement.

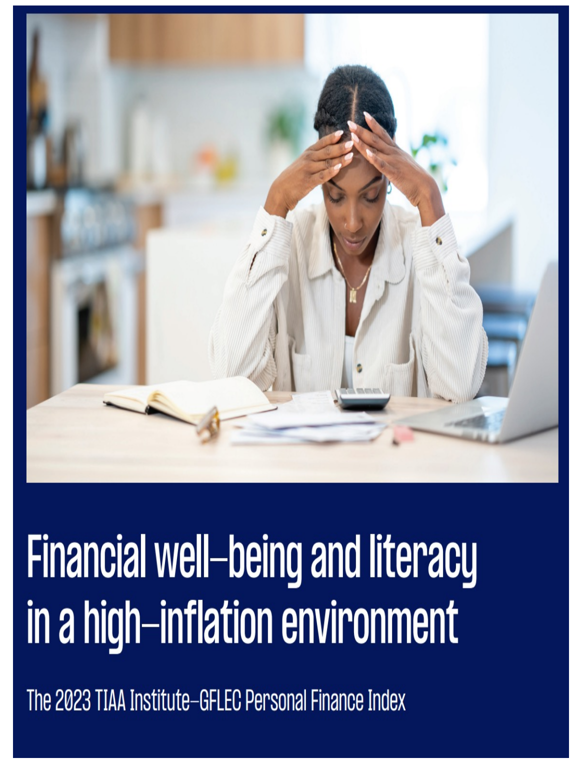
→ What about during the pandemic?



Our Dataset: the Personal Finance (P-Fin) Index

An annual barometer of knowledge and understanding to enable sound financial decision-making and effective management of personal finances among U.S. adults.





Research That Drives Thought Leadership | Institute (tiaa.org)

The P-Fin Index is based on 28 q's about 8 personal finance areas:

1. Earning
2. Saving
3. Consuming
4. Investing
5. Borrowing
6. Insuring
7. Comprehending risk
8. Go-to information sources

We also have the Big Three questions on Financial Literacy.

→ *Def*: Financial literacy: the ability to understand and process economic information.

Financial Literacy Measures we pioneered for the Health & Retirement Study (HRS) now in global use: *(Lusardi Mitchell 2007)*

- US: National Longitudinal Survey of Youth (NLSY); Rand American Life Panel (ALP); US Treasury/ FINRA survey on financial capability; Understanding Americans Study (UAS); TIAA P-Fin Index.
- Many others including the Netherlands; Germany; Italy; Russia; Mexico; Sri Lanka; Chile; global PISA test for HS kids.

Financial Literacy: The "Big Three"

__Interest Rate:__ Let's say you have \$100 in a saving account paying 2% interest/year. How much would you have in the account at the end of 5 years?

<\$102; =\$102, >\$102; DK; refuse

__Inflation__: Imagine that the interest rate on your savings account was 1% per year and inflation was 2% per year. After 1 year, with the money in this account, would you be able to buy*: > today, = today; < today*

__Risk Diversification__: True or false? Buying a single company stock usually provides a safer return than a stock mutual fund.

Why these questions?

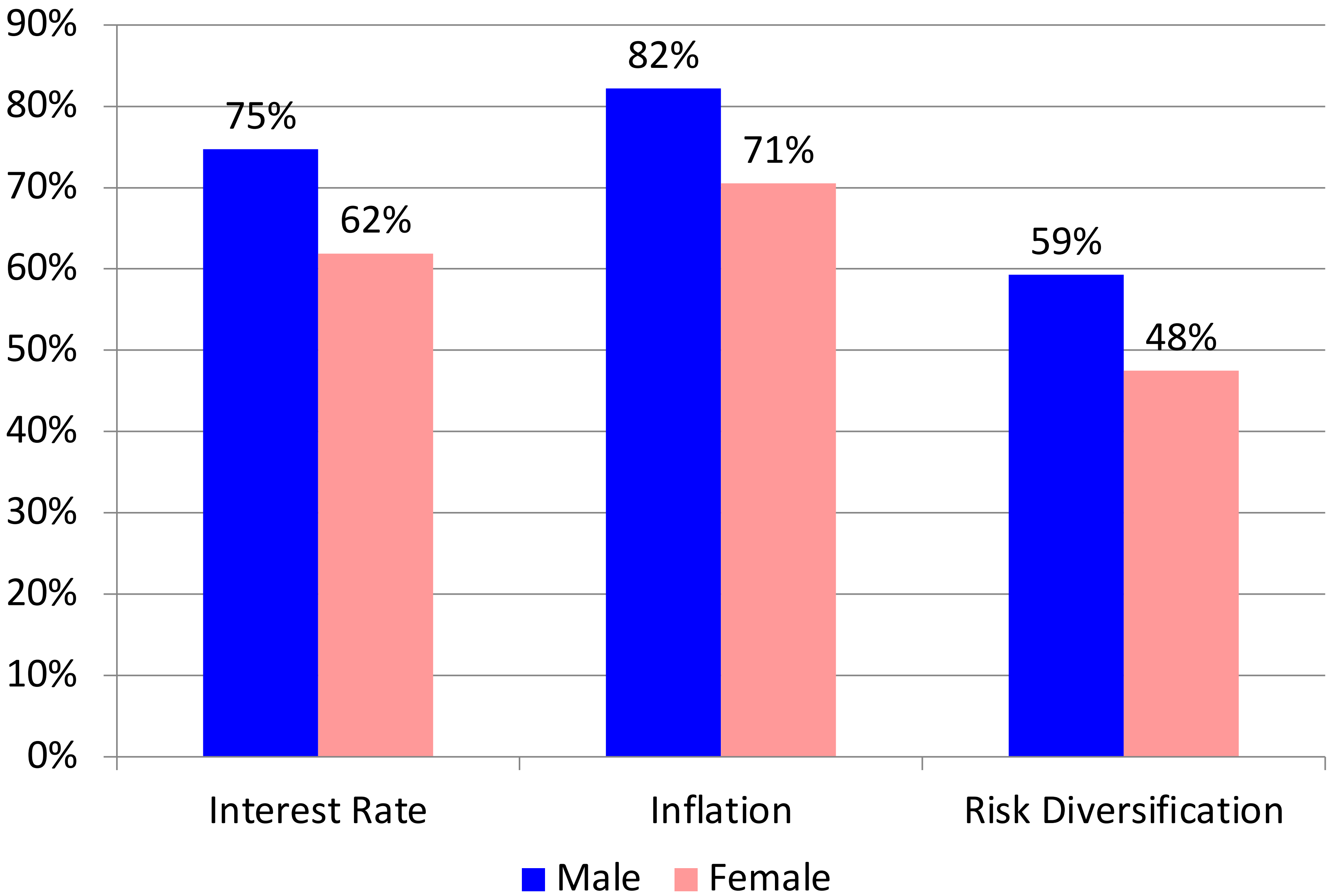
- 4 goals: simplicity, relevance, brevity, and capacity to differentiate.
- Measure knowledge of the key building blocks for financial decision-making in an intertemporal setting (simplicity).
- Relate to concepts pertinent to peoples' day-to-day financial decisions over the life cycle (relevance) and capture general rather than context-specific ideas.
- Few in number to secure widespread adoption (brevity) and to differentiate across peoples in terms of their financial knowledge (capacity to differentiate).

How much do older people (age 50+) know *(HRS)*?

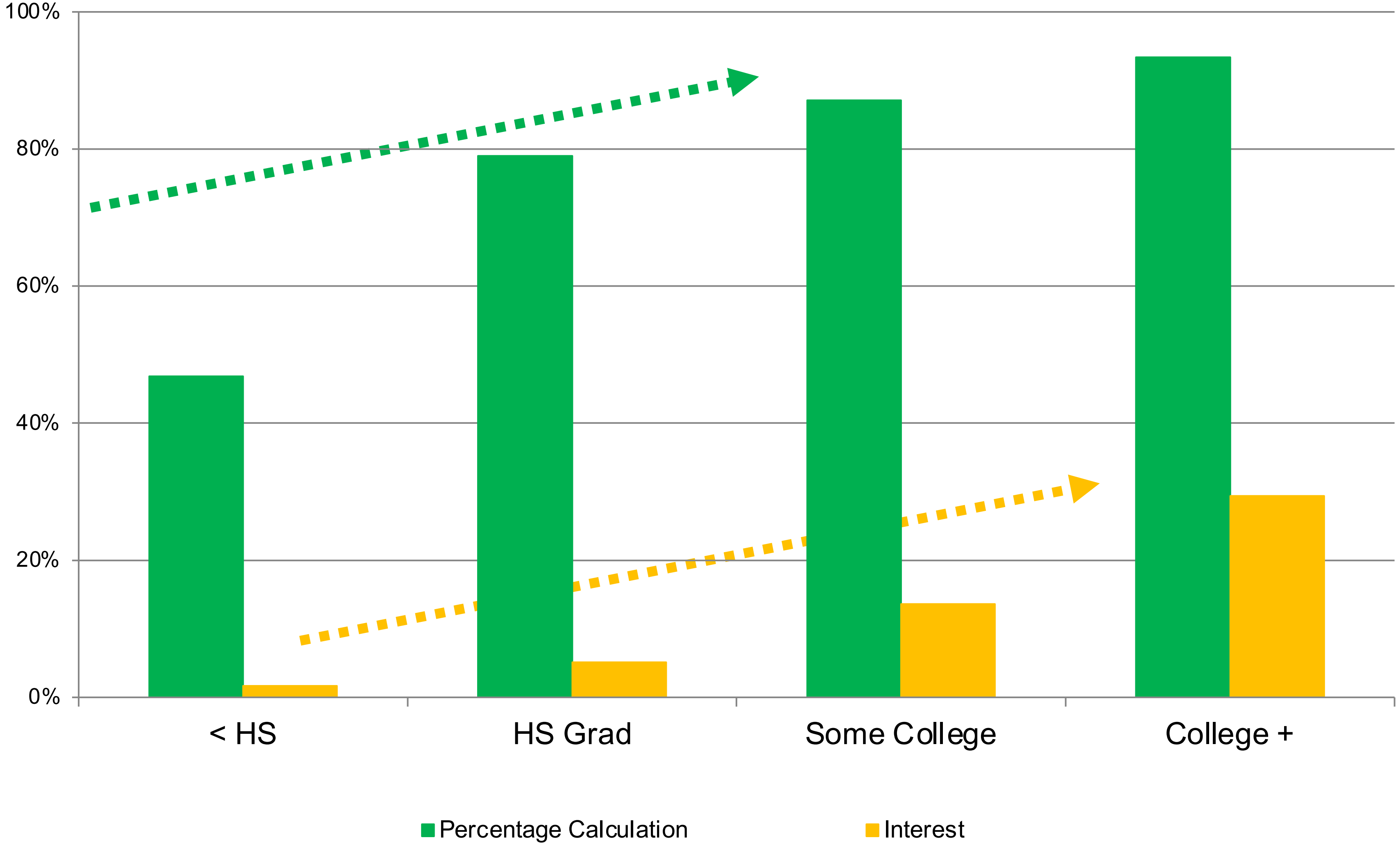
	Responses			
	Correct	*Incorrect*	*DK*	*Refuse*
Interest rate	67.1	22.2	9.4	1.3
Inflation	75.2	13.4	9.9	1.5
Risk diversif.	52.3	13.2	33.7	0.9

NB: Only **ONE THIRD (34%)** answer all 3 questions correctly; only around **HALF (56%)** answer the interest rate and inflation questions correctly.

% Correct by sex *(HRS)*

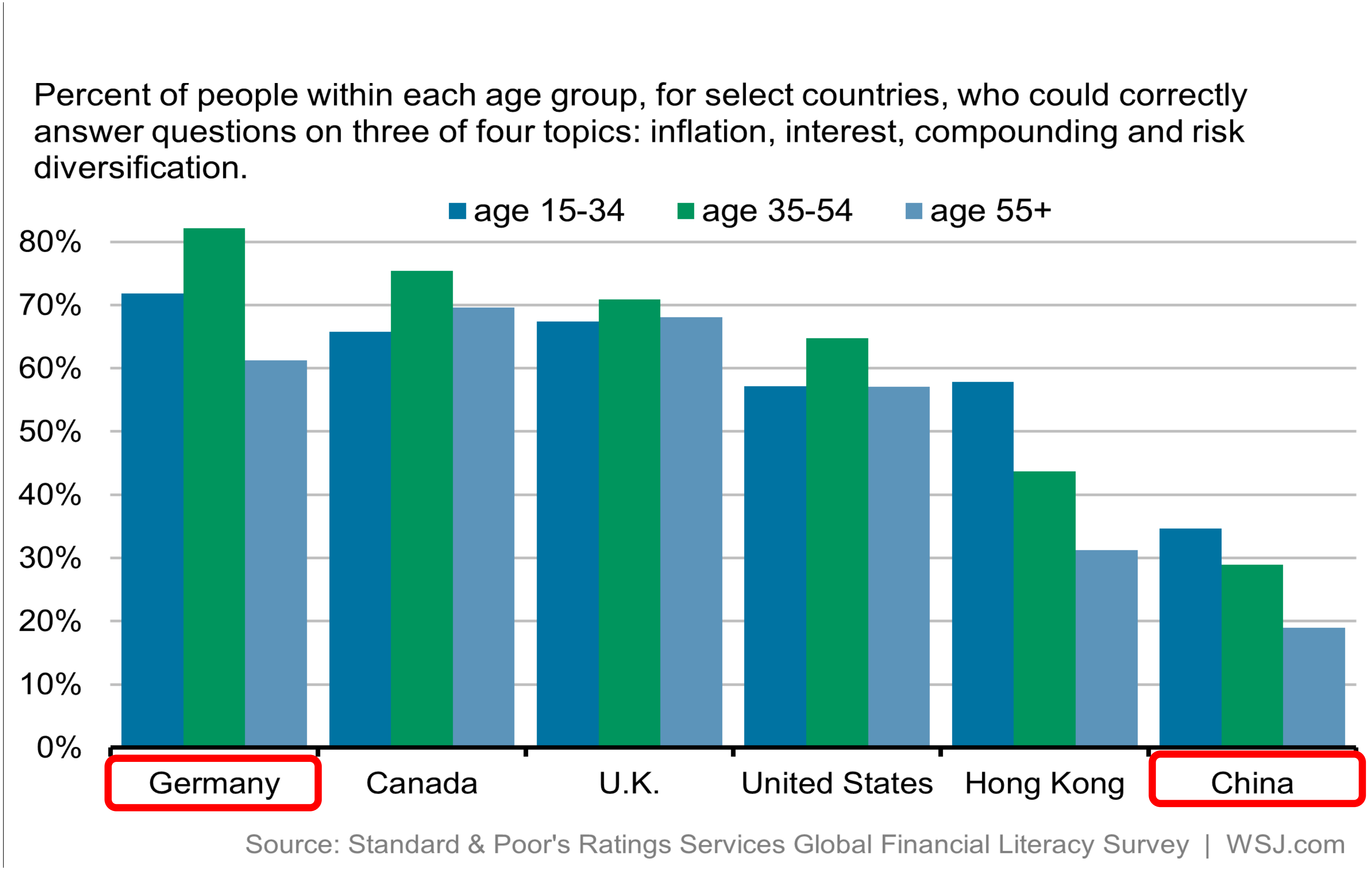


% Correct by education *(HRS)*



Lusardi/Mitchell 06

Financial Literacy around the World



Next…we measure who is debt-constrained?

“Debt and debt payments prevent me (and my spouse/partner) from adequately addressing other financial priorities.”

1 = “Strongly agree”
2 = “Somewhat agree”

Debt-constrained

3 = “Neither agree nor disagree”
4 = “Somewhat disagree”
5 = “Strongly disagree”

“Don’t know” and “Refuse to answer.”

And who is retirement ready?

"Have you (and your spouse/partner) ever tried to figure out how much you need to save for retirement?"

1 = "Yes" → Retirement ready

2 = "No"

"Don't know" and "Refuse to answer."

"Do you (and/or your spouse/partner) save for retirement on a regular basis?"

1 = "Yes" → Retirement ready

2 = "No"

"Don't know" and "Refuse to answer."

What we learn:

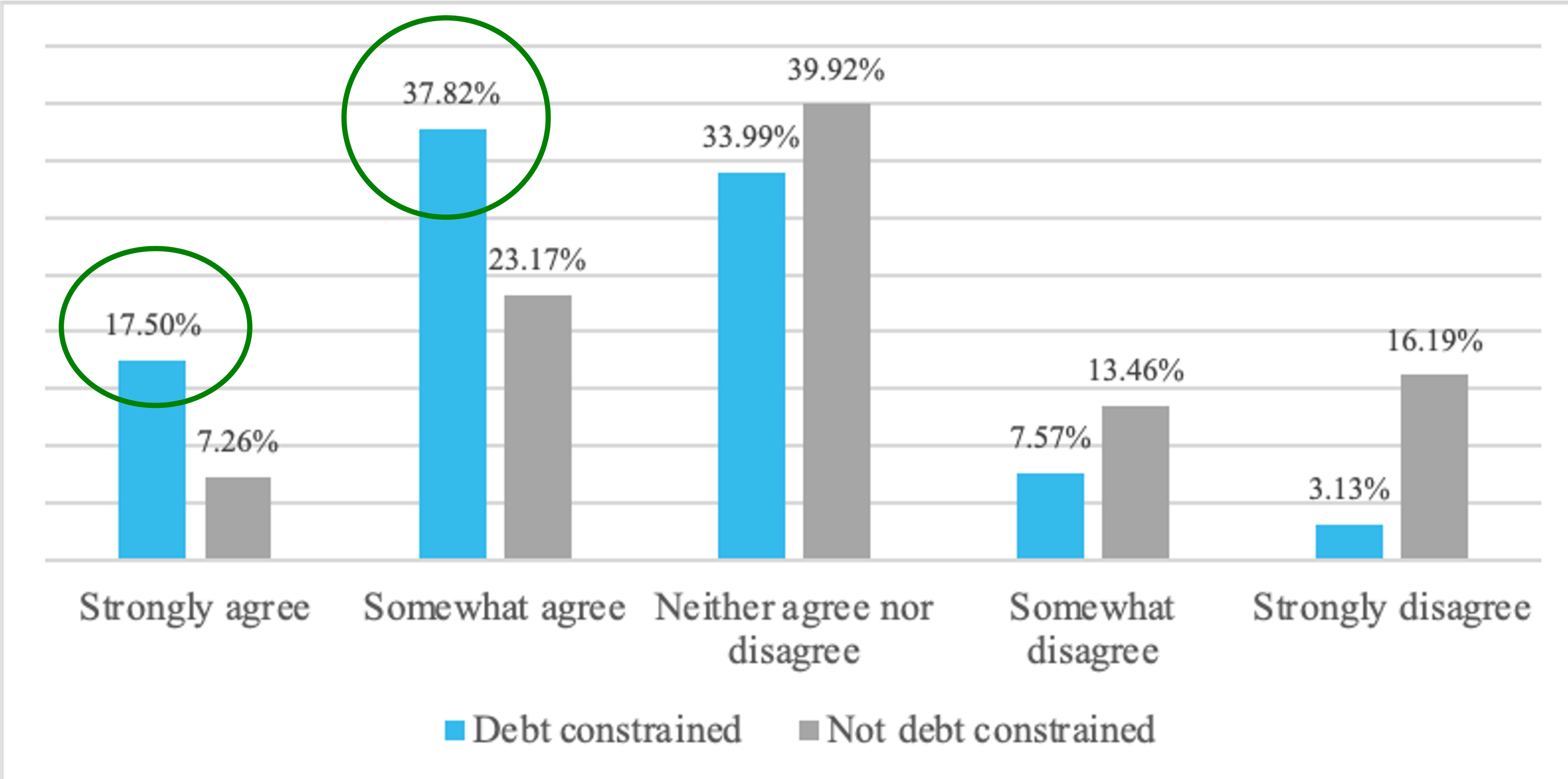
- Almost a third (31%) debt-constrained (in 2020 & 2021).
- Prime-age (30-44) most debt-constrained due to mortgages, student loans, childcare costs.
- Blacks and Hispanics more debt-constrained (35-45%) than Whites (26-27%).
- The least-educated most debt-constrained (<HS 48% vs Coll+ 25%).
- Most financially literate less debt-constrained than the financially illiterate (70% vs 43%).

And retirement readiness?

- Across both years: Fewer (26-31%) debt-constrained respondents planned for retirement vs non-debt-constrained (47-49%).

- And among nonretirees: Fewer (41-43%) of debt-constrained saved for retirement, vs not-debt-constrained (74-76%).

Post-pandemic, more seeking financial literacy!



Source: Authors' calculations using the 2020 and 2021 TIAA Institute-GFLEC P-Fin Index.

People more motivated to boost financial knowledge, especially the debt-constrained respondents.

Conclusions:

- Vulnerable groups struggled most with debt burden during the COVID-19 pandemic.
- The pandemic did not increase peoples’ debt burdens, due to federal relief efforts.
- Financial knowledge essential for managing debt and building retirement security.
- The pandemic did motivate people to boost financial literacy, especially if they were debt-constrained.

➔Financial literacy an essential skill for the 21st century!

Thank you!

- *For more information:*

Wharton's Pension Research Council:

- http://www.pensionresearchcouncil.org/

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