Income and Financial Well-being: Fragility, Knowledge and Help-seeking

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Objective

Income level is positively related to financial satisfaction and other well-being measures, for obvious reasons. This research seeks to determine if other measures have influence on financial well-being and if these influences vary by income level.

Significance

Early and subsequent studies of financial satisfaction noted that income is a main determinant (Joo and Grable, 2004; Woodyard and Robb, 2016). However, little work has been done to determine how consumers with differing income levels financial well-being is impacted by various factors. The author(s) hypothesized that financial attitudes and behaviors are more significant than financial knowledge in all income groups. This research hopes to assist financial counselors, planner, and therapists in working with different income groups and to develop educational curricula and treatments that are appropriate and effective for consumers in specific income categories.

Method

Using the 2015 FINRA National Financial Capability Survey, a series of ordinary least squares regressions were conducted to determine factors with the most impact on financial satisfaction. This study focuses particularly on the association between financial strain the financial satisfaction of the respondents after controlling for a number of socio-economic and demographic factors found to be associated with financial well-being of respondents in previous studies (Woodyard and Robb, 2016; Xiao, Chen, & Chen, 2014; Mottola, 2013). A further exploration examined those factors for various reported income levels and analyzed differences between income level groups. Our empirical model is explained below:

<u>Dependent Variable</u>
Financial Satisfaction is measured using a 10-point scale in response to the following question: "*Overall, thinking of your assets, debts and savings, how satisfied are you with your current personal financial condition?*"
In this scale, 1=Not atall satisfied; 10=Extremely Satisfied

<u>Independent Variables</u>
The key independent variables for this study are measures of financial knowledge, financial constraint, and seeking financial help from a professional.

Financial Knowledge related Variables:

Objective Financial Knowledge is measured based on the participants' responses to the five financial literacy questions that were included in the survey. These questions measured the participants'' knowledge of the concepts of compounding of interests, inflation, interest rates, association between bond prices and interest rates, and the concept of portfolio diversification.

Subjective Financial Knowledge is measured using a question where participants report how knowledgeable they feel about their finances on a 7-point scale (where 1=very low perceived knowledge; 7=very high perceived knowledge).

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Financial Constraint related variables:

Precautionary savings: A binary variable was constructed and coded as 1= if the participants in the survey reported that they could come up with $2,000 if needed for an emergency within the next month; and as 0= if otherwise.

Financial shock: A binary variable was created for financial shock as follows: 1=if the participant experienced a sudden unexpected drop in income in the past year; 0=if otherwise

Perceived financial strain: A binary variable was constructed perceived debt as follows: 1=if the participants perceived they currently had too much debt; 0=otherwise.

Other control variables:

Other control variables included in this study were age, gender, race/ethnicity, income, employment status, and risk tolerance.

The empirical model for this study is summarized below:
$Y= f(L, S, A)$
Where,
Y= Perceived financial satisfaction
L=Vector of the financial knowledge variables
S=Vector of the financial Strain and constraint related factors A=other control variables.
We have used an ordinary least squares regression specification for the empirical model of this study.

Results

Financial behaviors were found to have the most significant impact on financial well-being across all income level groups, although financial satisfaction was more difficult to model and explain with lower income groups.

Conclusion/Relevance

Lower level income consumers' financial satisfaction has the same determinants as those with higher income levels, but these factors do not go as far in explaining financial satisfaction.
Taking into account other factors such as income shocks and financial fragility helps to explain more of the lower income level consumers' financial well-being.

References

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