Community Development Research Brief

Household Net Worth & Asset Ownership among the Economically Vulnerable

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INTRODUCTION

The Federal Reserve released its quarterly Flow of Funds report in March 2013, which showed continued improvements in household net worth and led to upbeat news headlines such as, "U.S. net worth back to pre-recession level" and "Household incomes, net worth rising." [1,2] Indeed, the net worth of households and nonprofits reached $66.1 trillion in the fourth quarter of 2012, the highest level since it bottomed out at $51.4 trillion in early 2009, as seen in Figure 1.[3] These data hint at recovery at the aggregate level, but much of the economic gain was driven by improvements in financial markets, while the housing market has been slower to recover. Financial assets, which include checking and savings accounts, money market funds, stocks and bonds, increased 31.0 percent from their trough of $41.5 trillion in Q1 2009 to the post-recession high of $54.4 trillion in Q4 2012. Within the category of financial assets, the aggregate value of stocks increased 45.7 percent, from their lowest point in Q1 2009 at $14.1 trillion to $20.6 trillion in Q4 2012. In contrast, the aggregate value of real estate bottomed out later, at $18.3 trillion in Q2 2011 and grew 8.9 percent to $19.9 trillion in Q4 2012. These trends are significant for low- and moderate-income (LMI) households, as housing tends to make up a larger share of their household net worth, in comparison to wealthier households that typically own a broader range of assets, including larger amounts of financial wealth.

Figure 1 - Assets and Net Worth of Households and Nonprofits, 2005-2012

Quarterly, Not Seasonally Adjusted

Source: Board of Governors of the Federal Reserve System
* Includes checking and savings accounts, money market funds, stocks and bonds
** Held in mutual funds, life insurance, and pensions

In order to further understand these trends, this Research Brief examines household net worth and asset ownership in 2005 and 2011 across different demographic groups, using data from the U.S. Census Bureau's Survey of Income and Program Participation. This Brief also provides an overview of some of the issues around household financial stability, why balance sheets mattered so much going into the recession, and how they are impacting the subsequent recovery.

WHY HOUSEHOLD BALANCE SHEETS MATTER

Income tends to be a key indicator for the community development field, driven in large part by programmatic and regulatory requirements to serve a specific population defined by relative income.[4] While income remains a vital economic indicator of financial well-being, there is a growing effort to understand household financial stability more broadly in the context of net worth and household balance sheets. This effort is rooted in the asset building movement that developed in the early 1990's with Michael Sherraden's seminal work, *Assets and the Poor.*[5] A wide body of research has since demonstrated that asset ownership can promote economic, social and psychological well-being for low-income individuals in ways that income alone cannot.[6] This is not to suggest that one indicator is "more important" than the other, but rather to reinforce the idea that low-income households need sufficient income *and* assets to achieve long term financial stability and access to opportunity.

But in order to develop a comprehensive understanding of total financial health, we must also consider the role of debt and net worth, particularly as they relate to economic mobility for lower-income households. Ray Boshara, Director of the Federal Reserve Bank of St. Louis Household Financial Stability Initiative,[7] explains the significance of household balance sheets:

> *And our strategy must heed the lessons arising from the Great Recession—namely, that we need to take downside risk as seriously as the upside of encouraging working families to save and build wealth… No one thought the balance sheets of lower-income and minority households—who disproportionately had too little savings, too much debt, and too few assets beyond housing—could bring the economy down, but they did. We learned the hard way that we must think comprehensively and proactively about household balance sheets—why they matter, and what we can do to improve them*[8]*.*

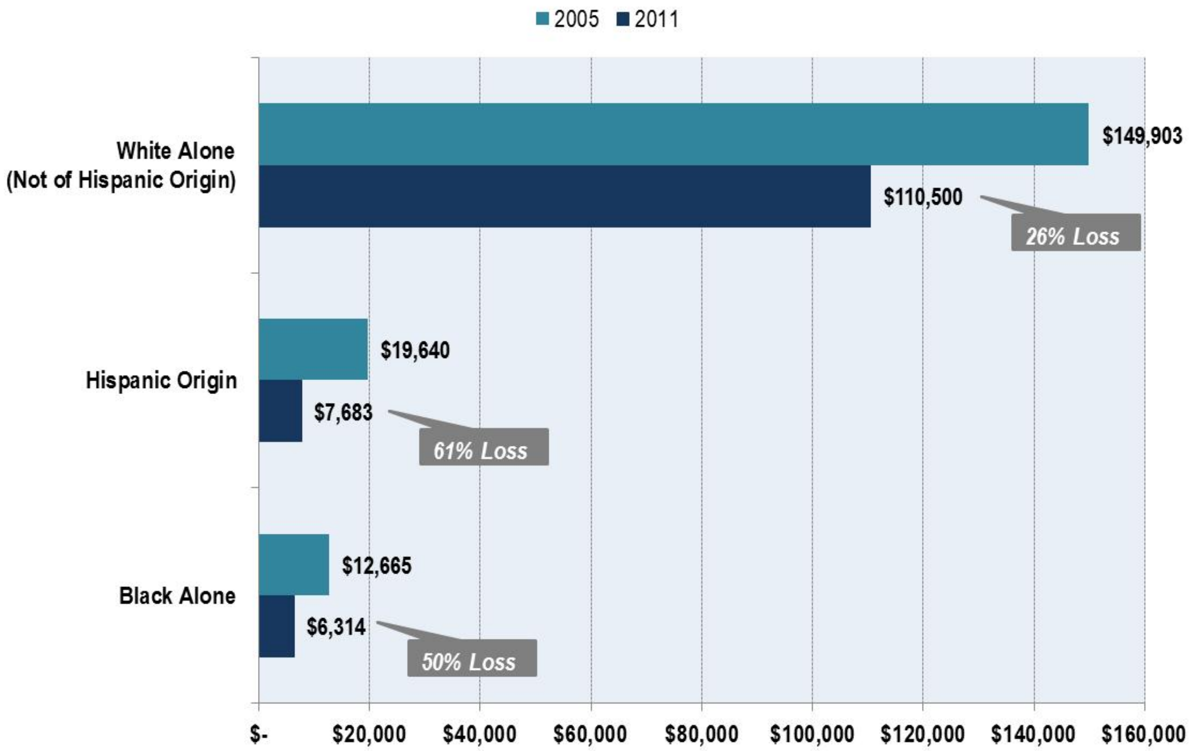
Taking a closer look at household balance sheets before and after the recession, Emmons and Noeth find that younger, minority and less-educated families suffered the largest wealth losses during the economic crisis.[9] They use data from the Federal Reserve's triennial Survey of Consumer Finances (SCF) and find that these households held a large amount of real estate relative to their incomes and total assets, mostly in the form of a primary residence, and had relatively little owners' equity in their homes. Declining house prices had a relatively large impact on the net worth of these households, many of which simultaneously experienced job and income losses during the recession. Similarly, using data from the SCF, Grinstein-Weiss and Key find that low-wealth homeowners owned relatively few non-housing assets and were thus deeply exposed to the broad downturn in housing prices during the recession.[10] In absolute terms, wealthier homeowners lost more home equity during the housing crisis, but homeowners with lower initial net worth lost more as a proportion of their total wealth.

These trends at the household level have important macroeconomic implications. Mian, Rao and Sufi find that poorer and more indebted households reduced their spending much more than their wealthier counterparts in response to declines in housing net worth during the Great Recession.[11] Similarly, Dynan and Edelberg find that after the recession, households that were more indebted were more likely to report cutting back consumption, even after controlling for wealth, income, and other factors that would be expected to influence consumption.[12] Case, Quigley and Shiller find that changes in housing values exert a larger and more important impact upon household consumption than do changes in stock market values.[13] These studies suggest that the status of household balance sheets, particularly the level and composition of household debt, have an influential impact on aggregate consumption, which has been a factor in the slow economic recovery.

NET WORTH OF HOUSEHOLDS 2005 VS. 2011

The Census Bureau's Survey of Income and Program Participation (SIPP) gathers information at the household level on income, labor force participation, program participation and eligibility, as well as information on assets and liabilities.[14] The SIPP calculates net worth as the market value of all assets owned by every member of the household minus the value of all liabilities owed by the household. The median net worth of all households was an estimated $107,180 in 2005 and $68,828 in 2011, a decrease of 35.8 percent (in constant 2011 dollars[15]). However, disaggregating the data by demographic characteristics reveals wide disparities in household net worth, as well as stark differences in how households fared after the Great Recession. Figure 2 shows median net worth by race and reveals a significant racial wealth gap. In 2011, non-Hispanic white households had a median net worth of $110,500, roughly 14.4 times that of Hispanic households and 17.5 times that of black households. White households also experienced smaller losses between 2005 and 2011 as their median net worth fell 26 percent, compared to 61 percent for Hispanic households and 50 percent for black households.

Figure 2 - Median Net Worth by Race, 2005 vs. 2011 (in $2011)

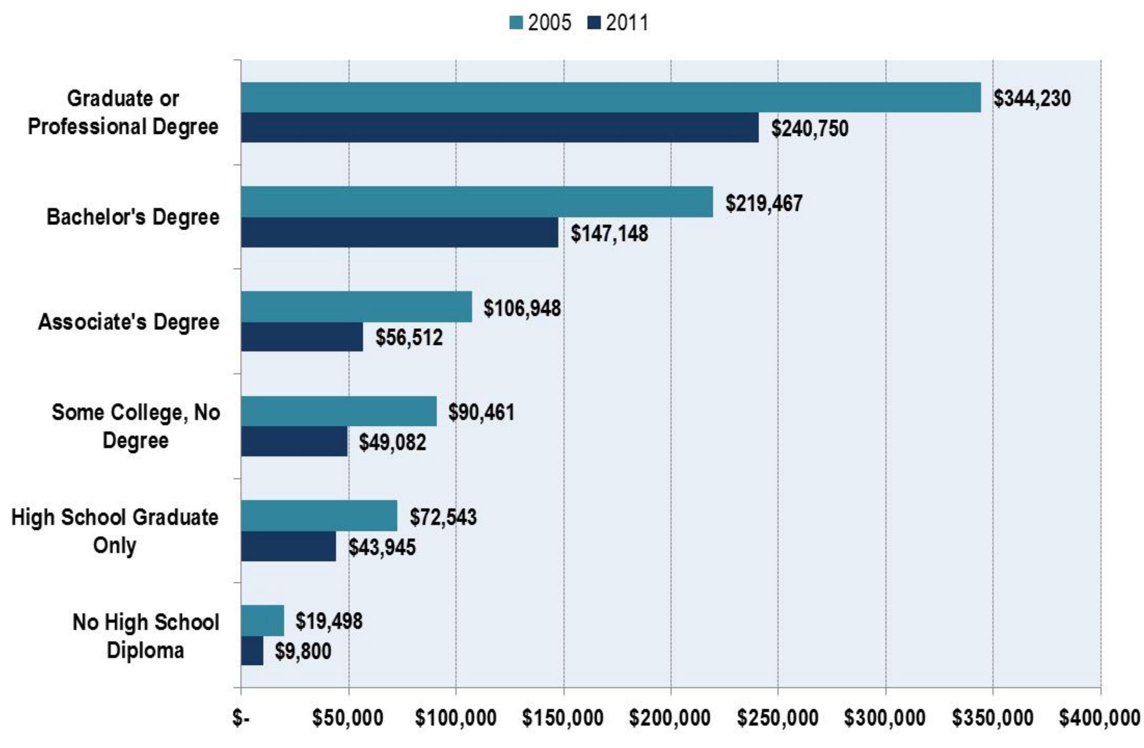


Source: U.S. Census Bureau, Survey of Income and Program Participation 2004 and 2008 Panels.

A recent study by the Institute on Assets and Social Policy at Brandeis University finds that the total wealth gap between white and African-American families nearly tripled between 1984 and 2009.[16] The authors attribute this gap to policies and institutional practices that create different opportunities, such as historic differences in access to credit and residential segregation patterns which have implications for school quality and educational achievement. Such conditions have created disparate opportunities where equal achievements, such as income gains, yield unequal wealth rewards for whites and African-Americans. The study reveals that every dollar increase in average income among households studied over the 25-year period added $5.19 of wealth for white households, while the same income gain added just 69 cents of wealth for African American households.

Another important factor in household net worth is educational attainment, as demonstrated in Figure 3. A household led by someone with a bachelor's degree had a median net worth of $147,148 in 2011, compared to someone without a high school diploma, who had a median net worth of $9,800. While all households experienced losses in net worth from 2005 to 2011, the median net worth of households led by someone without a high school diploma decreased by 49.7 percent, compared to 39.4 percent for high school graduates and 33.0 percent for those with a bachelor's degree. In 2005, those with a bachelor's degree had a median net worth that was three times larger than those with a high school diploma. In 2011, this had increased to a factor of 3.3, reflecting the growing importance of educational attainment, particularly the "premium" that accrues to those with a college degree. This premium is even greater when comparing college completion to those without a high school diploma. In 2005, households with a BA had a median net worth 11.2 times greater than households without a high school diploma; by 2011, households with a BA had 15 times the net worth of households without a high school diploma.

Figure 3 - Median Net Worth by Education, 2005 vs. 2011 (in $2011)

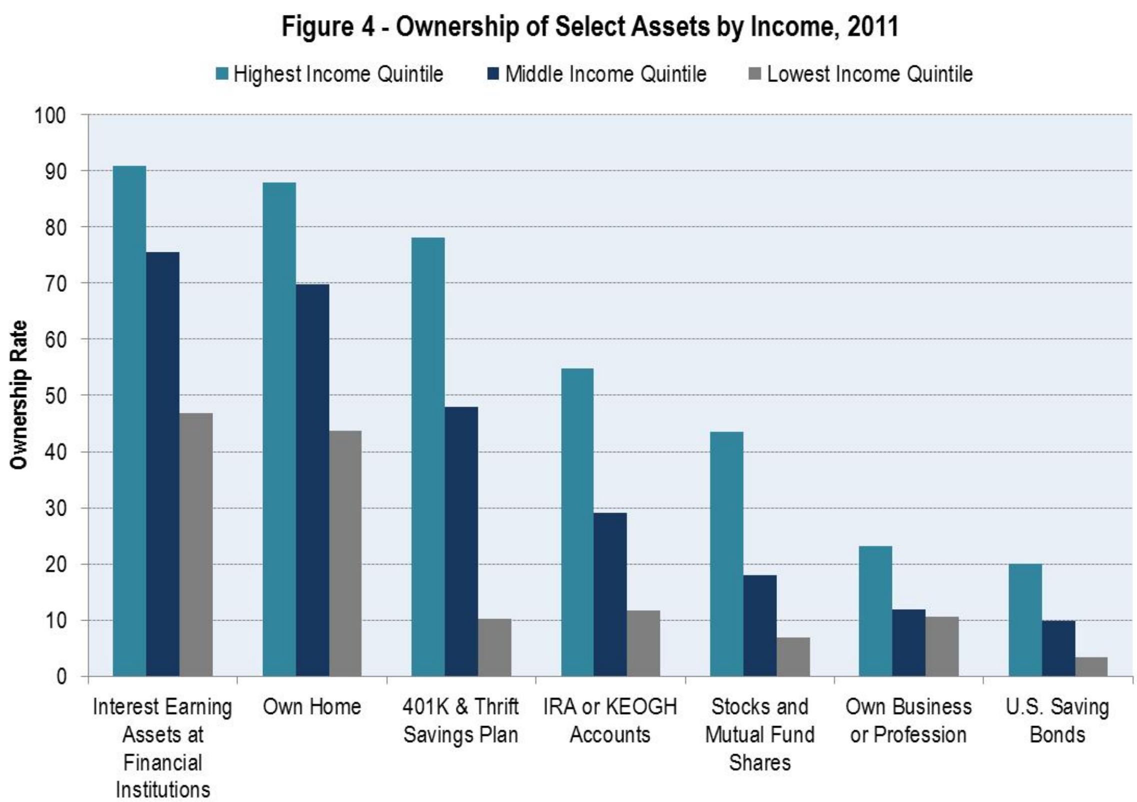


Source: U.S. Census Bureau, Survey of Income and Program Participation 2004 and 2008 Panels.

Many households rely on student loans to finance postsecondary education, which have important implications for household balance sheets. Student loan debt now exceeds credit card debt in the U.S., with aggregate balances exceeding $1 trillion in 2012,[17] and the average student debt per borrower is $23,300.[18] In a recent study, Nam finds evidence that educational loans above $10,000 reduce the probability of college graduation,[19] suggesting that high student debt can negatively impact long term financial health in multiple ways. The Pew Research Center surveyed individuals who took out college loans and are no longer in school; 48 percent said that paying back the loan has made it harder to make ends meet and 25 percent said it has made it harder to buy a home.[20] However, Gross, Rock and Hogarth argue that while student debt appears on the liability side of the household balance sheet, there is no compensating value on the asset side for the additional earning power the debt has enabled.[21] The Pew study estimates that the lifetime net payoff of getting a college degree is still quite substantial—for a typical student who graduated from an in-state, four-year public university, this net gain is about $550,000.[22]

ASSET OWNERSHIP

While net worth is a good indicator of overall financial health, the composition of a household's asset portfolio also has important implications for household financial stability. As discussed previously, much of the recent gain in household net worth has been driven by strong performance in the stock market. For example, the S&P 500 gained 13.4 percent in 2012, marking the index's largest annual return since 2009 and fourth-largest return in the last decade.[23] Similarly, the Nasdaq Composite Index was up nearly 16 percent in 2012, an improvement over the previous year when the index fell 1.8 percent.[24] As seen below in Figure 4, stock price appreciations are more likely to benefit higher income households, who own stocks, mutual funds, and retirement accounts at much larger rates than lower-income households. In 2011, among households in the highest income quintile, 43.6 percent owned stocks and mutual fund shares, compared to 6.9 percent of households in the bottom income quintile (a factor of 6.3 times). Ownership of 401K and thrift savings plans was 78.1 percent among the highest income quintile and 10.3 percent among the lowest income quintile (a factor of 7.6 times).



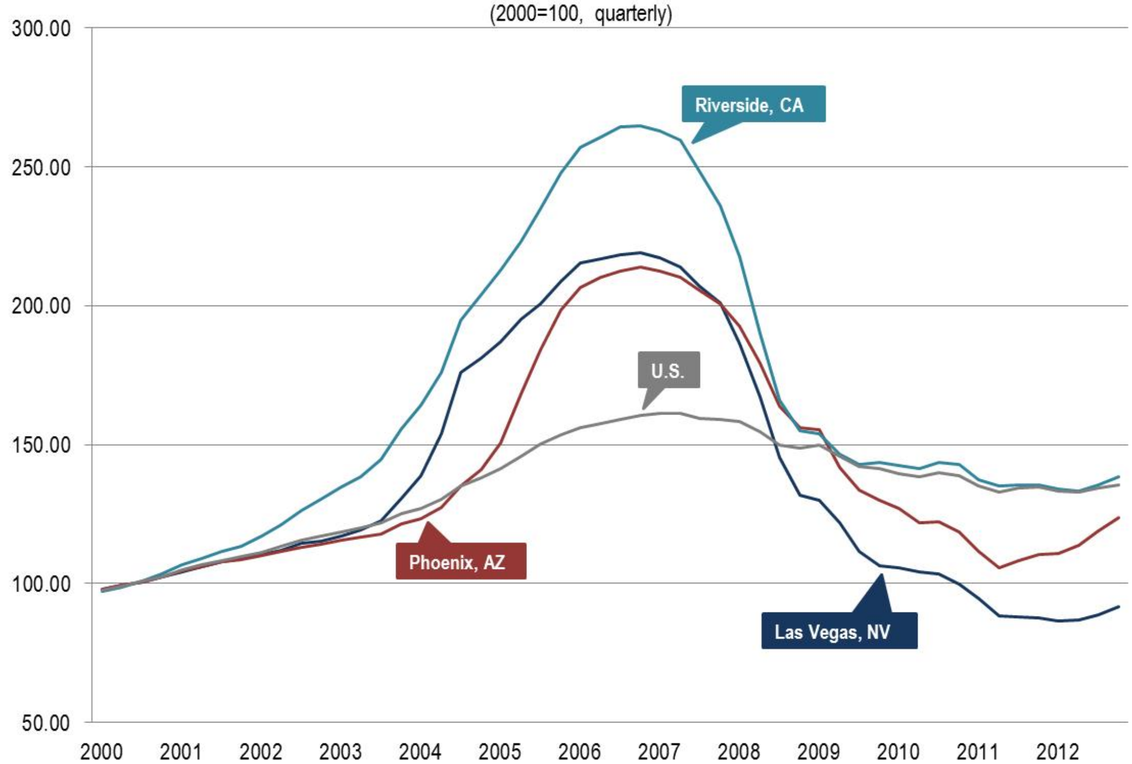
Source: U.S. Census Bureau, Survey of Income and Program Participation 2004 and 2008 Panels.

Across all income groups, the greatest share of households own interest earning assets at financial institutions, which includes funds in passbook savings accounts, money market deposit accounts, certificates of deposit, and interest earning checking accounts. Almost 91 percent of households in the top income quintile own this type of asset, compared to 75.6 percent of the middle income quintile and 46.9 percent of the bottom income quintile. Despite greater ownership rates across income groups, relative to other types of financial assets, the values of these holdings vary dramatically. The median value of interest earning assets at financial institutions for households in the top income quintile was an estimated $10,000 in 2011, compared to $360 for the lowest income quintile. This stark difference in liquid assets means that higher-income households are much more likely to be resilient in times of financial distress. In contrast, a $360 cash cushion is simply not enough to provide meaningful financial support for lower-income households, who are more likely to face job losses and decreases in household income.

The second most commonly owned asset across all income groups is a home. Compared to a homeownership rate in 2011 of 87.9 percent among households in the highest income quintile, 43.6 percent of households in the lowest income quintile and 69.9 percent of the middle income quintile own their own home (a factor of 2.0 and 1.3, respectively). As mentioned previously, housing dominated the balance sheets of LMI households going into the Great Recession, which meant these households were deeply exposed to the downside risk that eventually materialized during the housing downturn.

The 12th District is home to some of the hardest-hit areas in the nation, such as Phoenix, Arizona, Riverside, California, and Las Vegas, Nevada. As shown in Figure 5, these areas saw tremendous price increases during the boom and subsequent losses that destroyed wealth for many households. House prices showed signs of recovery in late 2012, but are still well below their pre-recession levels. By the end of 2012, home prices in Riverside were still 47.8 percent below their peak in the fourth quarter of 2006, compared to the U.S. as a whole, which was down 16.0 percent from its peak in the first quarter of 2007. Las Vegas home prices are still below their level from 2000, meaning that even households that purchased their homes well before the bubble formed lost significant equity. Many households in these depressed markets remain “underwater” and are unable to refinance and take advantage of historically low interest rates. In contrast, the *Wall Street Journal* recently reported an increase in cash-out refinancing among wealthy households, who are using the proceeds to purchase investments, such as stocks or other real estate,[25] further widening the wealth gap.

Figure 5 - FHFA (formerly OFHEO) House Price Index
(2000=100, quarterly)

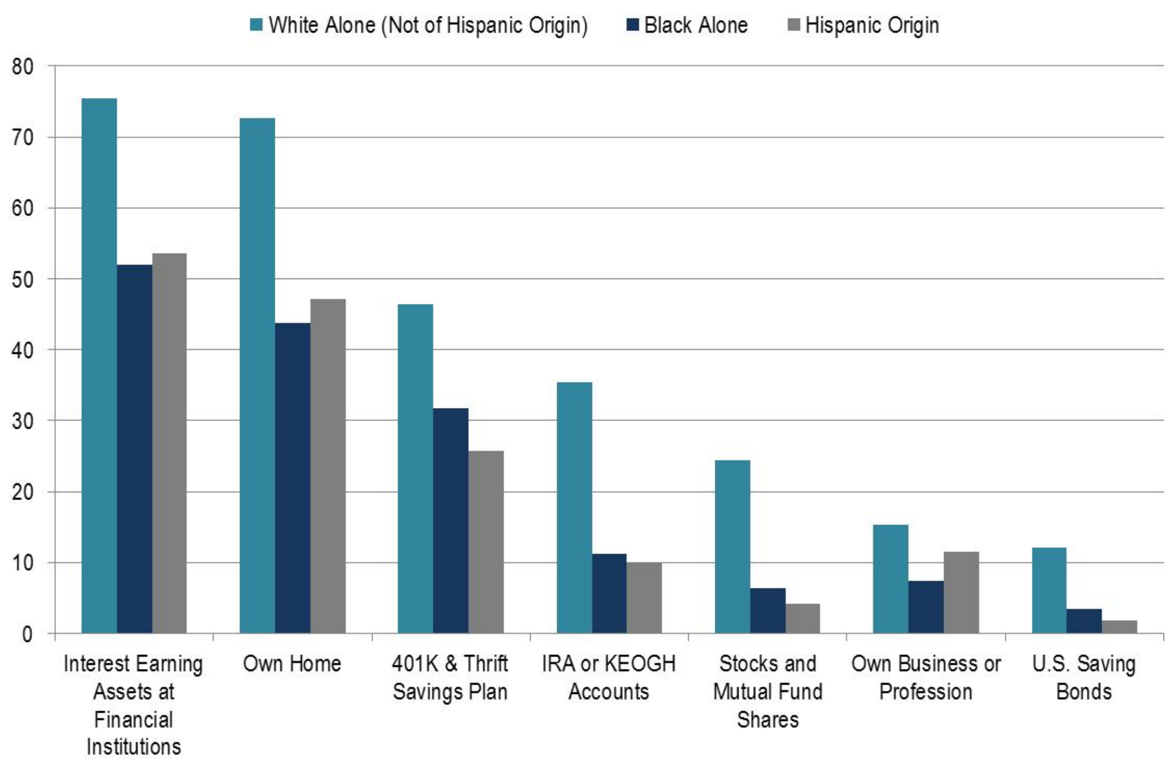


Source: Federal Housing Finance Agency (formerly OFHEO)

In addition to equity losses from house price declines, many households lost their homes to foreclosure.[26] Of particular concern is the role that predatory mortgage products played in the foreclosure crisis and the fact that African American and Latino households were more likely to receive high-cost risky mortgages, regardless of their credit scores. The Center for Responsible finds that African Americans and Latinos with good credit (a 660+ FICO score) received a high-cost loan more than three times as often as white borrowers.[27] Additionally, the foreclosure rate for LMI African Americans is about 80 percent higher than that for comparable white households and foreclosure rates for higher-income Latinos is more than three times that of higher-income whites.[28] These figures are significant as homeownership accounts for a larger share of household wealth for black families, amounting to 53 percent of wealth for blacks and 39 percent for whites.[29]

As shown in Figure 6 below, minority households tend to have lower rates of non-housing asset ownership relative to non-Hispanic white households. White households owned stocks and mutual fund shares at a rate of 24.5 percent in 2011, compared to 6.4 percent and 4.3 percent for black and Hispanic households, respectively. Similarly, a larger share of white households owned financial assets through retirement accounts, such as 401Ks and IRAs. These households have not only higher ownership rates, but higher median asset values as well. The median value of a white household's stock and mutual fund shares was $24,000 in 2011, while black households had a median stock value of $4,750 and Hispanic households had a median value of $8,000. Similarly, in 2011, the median value of a white household's 401K or thrift plan was $35,000, compared to $12,000 and $15,000 for blacks and Hispanics, respectively. In addition, 75.4 percent of white households owned interest earning assets at financial institutions, compared to 51.9 percent and 53.6 percent for black and Hispanic households, respectively. However, the median value of these accounts also varies—$3,250 for white households, $500 for black households and $700 for Hispanic households.

Figure 6 - Ownership of Select Assets by Race, 2011



Source: U.S. Census Bureau, Survey of Income and Program Participation 2004 and 2008 Panels.

CFED estimates that in 2010, 62.6 percent of households of color were in “liquid asset poverty,” meaning they lacked sufficient liquid assets to subsist at the poverty level for three months in the absence of income, compared to 34.8 percent of white households.[30] Liquid assets play a particularly important role in helping economically vulnerable households cope with adverse events,[31] which can have important implications for long-term household financial stability.

CONCLUSION

While aggregate household net worth may be approaching pre-recession levels, it’s clear that the economic recovery is unfolding at an uneven pace. Households whose balance sheets were dominated by housing, particularly those in depressed markets and those exposed to high-cost predatory mortgages, were deeply exposed to the downside risk that became reality during the Great Recession. These households tended to be lower-income, minority, and have lower educational attainment, meaning they were already struggling with low net worth prior to the recession.

These trends reinforce the value of looking at household financial stability through the balance sheet framework. In order to promote greater financial stability for struggling families, we must pursue solutions that address both asset development and debt management:

- While not a silver bullet for wealth creation, homeownership is still an important factor in long-term and intergenerational wealth building for lower-income and minority households (particularly its role as a mechanism for forced savings), but we must find ways to promote sustainable homeownership and fair access to responsible mortgages for these populations.
- Similarly, we must identify viable options for paying for postsecondary educational attainment, which includes promoting college affordability and savings, such as federal Pell Grants or children’s savings accounts for education, as well as efforts to manage student debt. Even more foundational is the need to ensure that young people are college-ready and able to successfully graduate so they aren’t leaving school saddled with debt and no degree.
- Finally, we need to promote emergency savings in order to ensure that households have ready access to liquid assets during times of sudden financial need, such as the massive job losses that occurred during the recession.

As we’ve seen over the past few years, the financial health of all households has significant macroeconomic implications, particularly as it relates to consumption and economic growth. Promoting long-term financial stability at the household level is thus a critical factor in economic recovery. We must continue to pursue “what works” in Community Development in order ensure that such recovery is truly inclusive.[32]

ENDNOTES

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