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Five Simple Questions That Reveal Your Financial Health and Wealth

By William R. Emmons and Bryan J. Noeth

A few simple questions can reveal a great deal about a person's overall health and risk of illness or death. These questions might ask, for example, about smoking habits, seat belt usage when riding in a car, resting heart rate, blood pressure and consumption of alcoholic drinks each week.

Similarly, a few simple questions can reveal a lot about your financial health. If you save regularly, make all of your payments on time, pay off your entire credit card balance when due, maintain a healthy stock of safe and liquid assets, and never take on debts that put a heavy strain on your monthly income, you are very likely to be financially healthy and able to accumulate significant wealth. If you do none of those things, you are very likely to be financially unhealthy.

We created a "financial health scorecard" that consists of five questions that were asked of each of the 38,385 families who participated in the Federal Reserve's Survey of Consumer Finances (SCF) between 1992 and 2013:[1]
- Did you save any money last year?
- Did you miss any payments on any obligations in the past year?
- Did you have a balance on your credit card after the last payment was due?
- Including all of your assets, was more than 10 percent of the value in liquid assets?
- Is your total debt service (principal and interest) less than 40 percent of your income?

How we scored the responses to these questions and the average number of points all respondents received on each question are in Table 1. The average total score for 1992-2013 was 3.01 out of a possible 5.[2]

To investigate the predictive power of the scorecard for financial success, we split the SCF sample in each survey year into 48 unique group combinations, based on:
- Three age groups: less than 40, 40-61, and 62 and over
- Four education groups: less than high school diploma, high school or GED diploma, two- or four-year college degree only, and graduate or professional degree
- Four racial and ethnic groups: black or African-American, Hispanic of any race, Asian or other minority not elsewhere specified, and non-Hispanic white

We then calculated the simple correlation coefficient between each group's average financial health score for 1992-2013 and the natural logarithm of the group's inflation-adjusted median net worth averaged across the eight waves. The resulting correlation was 0.67, indicating a very strong relationship between our measure of financial health and actual wealth. A scatterplot of the 48 data points, together with a trend line showing the underlying statistical association, is shown in Figure 1.

To translate this statistical relationship into descriptions of real people, Figure 1 and Table 2 highlight six of the demographically defined groups that fall close to the trend line. The three groups with financial health scores below 3 (approximately the overall average of all groups) also had median net worth levels below

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FIGURE 1

Scatterplot of Net Worth vs. Score on Financial Health Scorecard
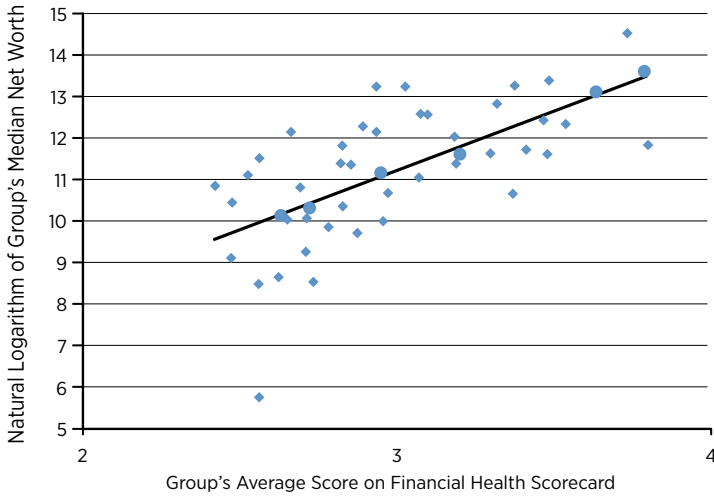
SOURCE: Federal Reserve Board's Survey of Consumer Finances and our calculations. The simple correlation coefficient is 0.67. Enlarged round markers in this chart represent groups highlighted in Table 2.

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the average of the overall median of the eight SCF surveys, which was about $100,000 (the natural logarithm of which is about 11.5). The three highlighted groups with financial health scores over 3 all had median net worth levels above the overall median.

Several patterns emerged. The highlighted groups below the medians on both financial health scores and net worth were younger than 40 and non-white.[3] The highlighted groups above the medians on both financial health scores and net worth were older than 62, and two of the three groups were non-Hispanic whites. The two groups with very high financial health scores and median wealth substantially above the overall median of $100,000 (groups 5 and 6) were non-Hispanic whites who were older than 62 with at least college degrees.

Perhaps surprisingly, educational attainment was not as strongly associated with financial health and wealth in this small sample as either age or race and ethnicity. Older families generally had greater financial health and wealth than younger and middle-aged families for any given race, ethnicity or level of educational attainment. This may be due to learning better financial habits over time, getting beyond the financial challenges of early and middle adulthood and the benefit of time in building a nest egg.

Meanwhile, non-Hispanic white and Asian families typically had greater financial health and wealth than Hispanic and African-American families for any given age or level of educational attainment. This may be due to differences in the economic and financial challenges each group faces and to systemic and historical differences in access to wealth-building institutions and policies, like mainstream financial institutions, employer-provided retirement plans and various types of saving incentives.

In summary, good financial health—as measured by our simple five-question scorecard—is highly correlated with the accumula-

TABLE 1

Questions Used in the Financial Health Scorecard

	Scoring	Mean Score in Eight SCF Waves, 1992-2013
1. After adjusting for any purchases of durable goods or investments you made, did you spend more, the same or less than your income in the past year?	Less = 1 Same or more = 0	0.56
2. How did the respondent answer the following question: Now thinking of all the various loan or mortgage payments you made during the last year, were all the payments made the way they were scheduled, or were payments on any of the loans sometimes made later or missed?	We sometimes got behind or missed payments = 0 Else = 1	0.84
3. Do any of these statements apply to you? *"We carried over a credit-card balance after we made our last payment."* *"We have been turned down in the past five years by a particular lender or creditor when I (or my husband/wife/partner) made a request for credit."* *"There was a time in the past five years that we thought of applying for credit at a particular place, but changed our minds because we thought we might be turned down."*	No, none apply or no credit cards by choice = 1 Yes, one or more apply = 0	0.44
4. Including all of your assets, was more than 10 percent of the value in safe and liquid assets, defined as liquid accounts (checking, saving or money-market accounts), certificates of deposits, bonds or savings bonds?	Yes = 1 No = 0	0.27
5. Is your total debt service, including both scheduled repayment of principal and interest owed, less than 40 percent of your income?	Yes = 1 No = 0	0.91
TOTAL SCORE	0 to 5 possible	3.01

A family's score on the financial health scorecard is the sum of the individual scores, with a range of 0 to 5. A score of 5 indicates the strongest financial health, with a score of 0 indicating the weakest financial health. Scores may not add to total due to rounding.

SOURCE: Federal Reserve Board's Survey of Consumer Finances and our calculations.

TABLE 2

Group	Average Financial Health Score	Description of Group	Natural Logarithm of Median Net Worth (2013 Dollars)	Median Net Worth (2013 Dollars)
1	2.63	African-Americans under 40 with a two- or four-year college degree	10.13	$25,199
2	2.72	Asian-Americans under 40 with less than a high school or GED diploma	10.32	$30,242
3	2.95	Hispanics under 40 with a graduate or professional degree	11.14	$68,940
4	3.20	Hispanics 62 or older with a high school or GED diploma	11.61	$110,179
5	3.64	Non-Hispanic whites 62 or older with a two- or four-year college degree	13.11	$494,789
6	3.79	Non-Hispanic whites 62 or older with a graduate or professional degree	13.62	$824,348

SOURCE: Federal Reserve Board's Survey of Consumer Finances and our calculations.

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tion of wealth. To be sure, we cannot say which way causation runs: from financial health to wealth or vice versa. Perhaps other factors are primarily responsible for the correlation, such as:

- The influence of the life cycle in shaping both financial behavior and financial outcomes
- Unique challenges related to race or ethnicity
- Disparate access to wealth-building financial institutions and policies

Whatever the causal mechanisms, our simple financial health scorecard provides a surprisingly accurate prediction of the median wealth of groups of families defined by their age, educational attainment, and race or ethnicity. ■

William R. Emmons is senior economic adviser at the Center for Household Financial Stability at Federal Reserve Bank of St. Louis. Bryan J. Noeth is a policy analyst at the Center.

ENDNOTES

1. The Survey of Consumer Finances is a detailed triennial survey of a representative cross-section of American families. See www.federal reserve.gov/econresdata/scf/scfindex.htm. The questions in the text are paraphrases. The precise wording of the questions is in Table 1.
2. The average score in individual years of the survey ranged from 2.91 in 2007 to 3.13 in 1992.
3. The average age among all family heads in all years was 49.3 years. The shares of family heads who were white, black or African American, Hispanic of any race, and Asian or other minority were 74, 13, 9 and 4 percent, respectively.

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