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Financial Fragility Following COVID-19 Income Shocks: Who is Most Vulnerable?

Ray Boshara , Lowell R. Ricketts

Note: *An extended version of this article was first published as an In the Balance research brief, Which Families Are Most Vulnerable to an Income Shock such as COVID-19?*

In early March, when it was clear that the COVID-19 pandemic was not just a health crisis, but also an economic one, we wondered: Which families should we be most concerned about?

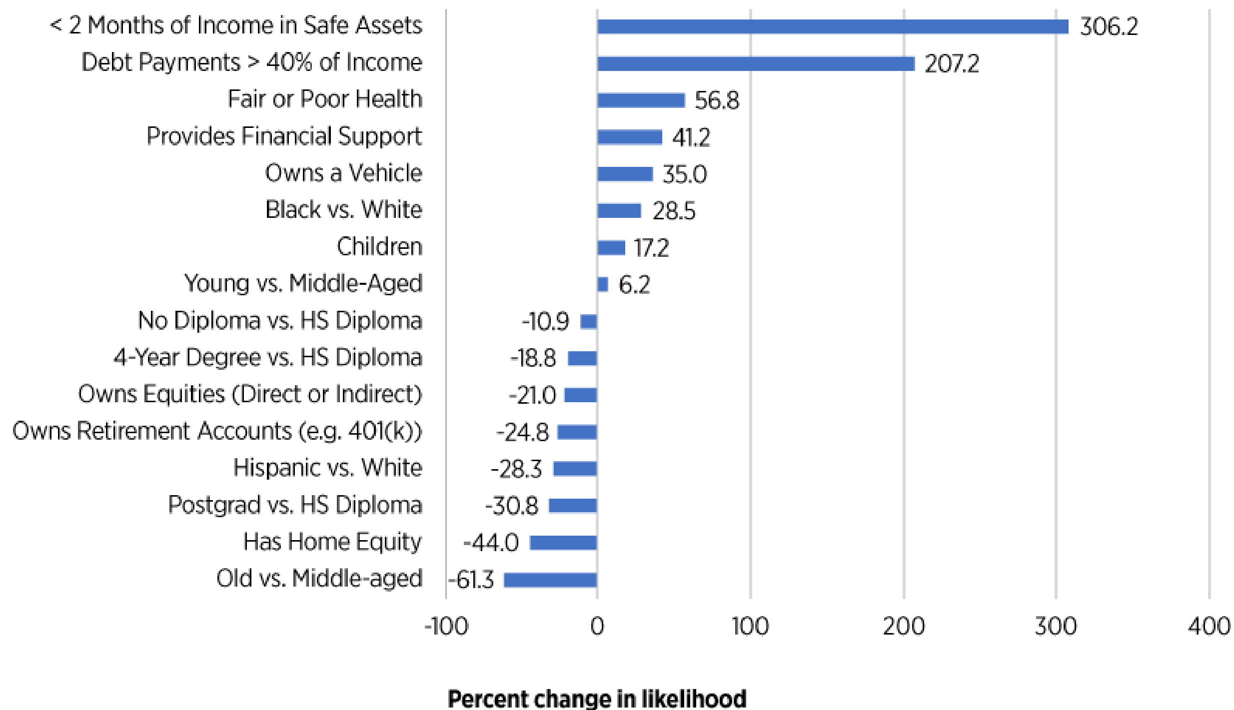
Millions of Americans were about to lose their jobs and incomes, an issue which policymakers were beginning to address, but we knew that families with weak balance sheets—too much debt and not enough savings, home equity or other assets to fall back on—would likely suffer even more.

But which families, exactly? To answer that question, we decided to look at a meaningful barometer of financial fragility: **serious delinquencies**, defined as being at least two months behind on a current loan obligation.

Based on the table below, the answers are grouped into two categories—those who are more and those who are less likely to fall behind on their debt payments.

Who Is More Likely To Fall Behind?

Liquid Assets and Debt Burden Have Biggest Effect on Likelihood of Serious Delinquency



SOURCES: Federal Reserve Board's Survey of Consumer Finances and Center for Household Financial Stability calculations.
NOTES: The bar chart shows the percent change in the likelihood of serious delinquency. Each bar compares two groups. For example, in the sixth bar from top, we see that, on average, Black families were 28.5% more likely to be seriously delinquent than white families, after controlling for the other variables shown here.

They don't have enough "safe" assets. By far, the most important predictor of serious delinquency is whether a family has at least two months' worth of income in the form of "safe" or liquid assets, such as cash and checking and savings accounts. If they don't, they are about 300% more likely to be seriously delinquent than those who have at least that buffer (or more).

They have too much debt relative to their income. The next most important factor associated with serious delinquency is whether a family's debt obligations exceed 40% of their income. If the family's debts are over that threshold, they are about 200% more likely than those who aren't as leveraged to be seriously delinquent.

They lack good health. Families reporting "fair" or "poor" health were nearly 60% more likely than those reporting "good" or "excellent" health to report a serious delinquency. This highlights how health problems, such as COVID-19, can lead to financial instability.

They are supporting family or friends. Families providing financial support to relatives or friends were 41% more likely to fall at least two months behind. In addition, each child in the family increased the likelihood of a serious delinquency by 17%.

They own vehicles. Those who own vehicles are 35% more likely than those who don't to report serious delinquency. It's possible that a vehicle loan itself is a source of delinquency.

Who Is Less Likely To Fall Behind?

Now let's look at some factors associated with families being less likely than others to report a serious delinquency, again holding all other factors constant.

They have other sources of wealth. Notably, families that have home equity, retirement accounts and equities (such as stocks) are 44%, 25% and 21% less likely, respectively, to report a serious delinquency than families without those assets. We speculate that these generally appreciating assets serve as buffers. They can be converted to more liquid assets, if necessary.

They have attained higher levels of education. In general, the more education families have attained, the less likely they are to experience serious delinquency. Compared to those with high school diplomas, those with a post-graduate degree were 31% less likely to report a serious delinquency, and those with a four-year college degree were nearly 19% less likely to report having one.

They are older. Older Americans (those aged 62 and above) are 61% less likely than middle-aged Americans (those aged 40 to 61) to experience serious delinquency. Younger Americans (aged 39 or younger) had roughly the same rates of serious delinquency as those who are middle-aged; this is consistent with findings from the second essay of the 2018 Demographics of Wealth series that suggests middle-aged and younger Americans typically have more financial obligations and less wealth than older Americans.

Race and Ethnicity Matter, too, though It's More Complicated

Findings regarding race and ethnicity were complex:

Hispanics are less at risk of serious delinquency. Compared to whites, Hispanics are 28% less likely to experience a serious delinquency once we account for the factors above (e.g., safe assets, debt-to-income ratios, education, etc.) that otherwise place families at a greater or lesser risk of falling at least two months behind on a debt payment.

Black families remain at a greater risk of serious delinquency. Black families are still 29% more likely to report a serious delinquency than whites—even after accounting for the characteristics above that otherwise make families more or less likely to fall behind. While it is hard to fully explain this, we believe that this remaining disparity—unique to Black families—partly reflects cumulative and systemic factors, such as the legacy of slavery and decades of housing discrimination, as identified in previous research by the Center for Financial Stability.

How Can Economic Resilience Be Promoted?

We encourage policymakers and others to promote economic resilience not only through cash payments and other liquidity measures, but also by helping families build or rebuild their wealth.

Efforts should be especially targeted among less-educated, younger and Black and Hispanic Americans who consistently have lower levels of wealth (as noted in a recent *On the Economy* blog). Doing so would not only help build wealth buffers, but also expand opportunity and upward economic mobility.

ABOUT THE AUTHORS

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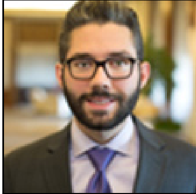

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Lowell R. Ricketts is the data scientist for the Institute for Economic Equity at the Federal Reserve Bank of St. Louis. His research has covered topics including the racial wealth divide, growth in consumer debt, and the uneven financial returns on college educations. Read more about Lowell's research.

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CRA: An Examiner's Perspective — Assessing Community Credit Needs

Douglas Yarwood

This article is part of a series on Community Reinvestment Act (CRA) best practices from an examiner's perspective. Although this column focuses on CRA best practices for financial institutions, the content may provide insights for community development organizations working with financial institutions in meeting credit and community development needs. As a disclaimer, this series is meant only to represent best practices; financial institutions should consider the information presented in context of the requirements or guidance of their primary regulators and the business needs of their financial institutions.

Assessing community credit needs is an ongoing process that is essential to fine-tuning lending strategies, as well as business and community development goals. Avenues for meeting the credit needs of communities constantly change due to various factors, including a financial institution's financial and human resource capacity, economic conditions, varying initiatives (e.g., federal, state, county and local) and natural disasters.

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Due to ongoing change, it is important for financial institutions to actively network with a wide variety of organizations to ensure members of the community seek out their institution for credit (commercial and personal) and finance needs.

Coordination is a key factor in assessing and meeting credit needs under the Community Reinvestment Act (CRA). Many financial institutions designate one or more individuals to seek out federal, regional, state and local entities to provide programs or services within their assessment area. Institutions should hone in on CRA-eligible programs or services for:

- low- and moderate-income (LMI) residents;
- those within distressed or underserved nonmetropolitan middle-income geographies; or
- small businesses/farms with revenues of $1 million or less.

In assessing community credit needs, financial institutions identify direct and indirect channels. Common direct affordable housing opportunities often include guaranteed lending programs, such as the Federal Housing Administration (FHA) and the Department of Agriculture (USDA), and down payment assistance programs like the Federal Home Loan Bank, Department of Housing and Urban Development or respective state agencies.

Similarly, economic development and small-business needs may also include guaranteed lending products, such as those from the Small Business Administration (SBA) and the USDA. While these products are designed to meet the needs of LMI individuals and small businesses/farms, they are not always the best fit for the institution, considering its resources and the communities it serves. For example, some USDA products are designed for communities under certain population sizes, and USDA, FHA and SBA products require additional expertise and resources of the financial institution to administer.

Fostering strong relationships with community development organizations focused on meeting CRA community development needs enables financial institutions to keep abreast of how to best offer products and services to LMI populations and small businesses/farms that do not yet qualify for a financial institution's lending programs.

Additionally, strong relationships with community development organizations keep financial institutions informed of investment and loan opportunities for larger-scale projects that affect their assessment areas, as well as larger regional areas that may also include their assessment area.

Individuals charged with building CRA community group relationships actively follow local news to learn about government plans for revitalization and stabilization and economic and workforce development programs that will impact LMI or nonmetropolitan distressed or underserved middle-income geographies. These individuals also follow economic development plans created with the help of local and regional economic development councils, NeighborWorks data and research through local university and college extension offices. This information may help identify opportunities to collaborate with organizations, such as small-business or homeownership counseling services and schools which primarily serve LMI populations.

Additionally, by supporting organizations that provide financial literacy and counseling, the financial institution is indirectly preparing the organization's clients for future credit opportunities.

When determining how to meet community credit needs, financial institutions not only assess their resources for direct lending opportunities, but also continually assess the resources of the communities they serve to identify CRA community development organizations with which they can foster collaborative working relationships.

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Community Development COVID-19 Resources

Our community development team collaborated to highlight these tools and publications from the St. Louis Fed and other organizations with the intention of providing assistance in the midst of the current pandemic.

HOUSING

National Housing Conference — A listing of over 600 articles cultivated to assist homeless service providers, homeowners, the multifamily finance industry, nonprofits, property management, renters, the single-family mortgage industry and more regarding housing assistance.

National Low-Income Housing Coalition — Review recommendations regarding housing and homelessness during the pandemic, analysis of the CARES and HEROES Acts and a tool that provides an overview of housing needs for each state.

FINANCE

Community Reinvestment Act (CRA) Consideration for Activities — The Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency united to provide a joint statement on CRA considerations for activities in response to COVID-19.

Federal Reserve Main Street Lending Program — This program was created to support lending to small and medium-sized businesses that were in sound financial condition prior to the COVID-19 pandemic.

SMALL BUSINESS

Small Business Administration (SBA) Loan Guidance — Business owners affected by the pandemic can discover funding options, recovery information, guidance, products and additional resources.

National Council of Nonprofits - PDF — Nonprofit owners can learn about the SBA loans available to them, as noted in the CARES Act.

WORKFORCE DEVELOPMENT

U.S. Department of Labor — Workers and employers can find guidance on the best ways to prepare for the impact of COVID-19.

CareerOneStop Unemployment Benefits Finder — The Department of Labor compiled data on the process for filing for unemployment benefits in each state.

FUNDING

St. Louis Community Foundation Regional Response Fund — St. Louis-area nonprofits that were affected by COVID-19 can apply to receive funding to sustain their organizations.

Community Foundation of Louisville Response Fund — Louisville-area nonprofits and individuals impacted by the pandemic can apply to receive financial support.

HOUSEHOLD FINANCIAL STABILITY

"Parasite," COVID-19 and U.S. Wealth Inequality — The Center for Household Financial Stability uses the South Korean film to provide insight on the spectrum of family wealth during the pandemic.

Which Families Are Most Vulnerable to an Income Shock such as COVID-19? — Families without enough "safe" assets and too much debt are at risk – who else should policymakers and others target for economic assistance?