

THE EFFECTS OF THE FINANCIAL CRISIS ON THE WELL-BEING OF OLDER AMERICANS: EVIDENCE FROM THE COGNITIVE ECONOMICS STUDY

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This paper uses the Cognitive Economics Study (CogEcon) to examine how the financial crisis affected the well-being of older Americans. The CogEcon study has several features that provide distinctive insights into this question. The initial wave of the CogEcon study (CogEcon 2008) was fielded shortly before the financial crisis that began in the fall of 2008. It provides baseline wealth measurements and very detailed information about the structure of households' portfolios for a representative sample of U.S. individuals aged 50 years and older. In addition to this detailed information on wealth and portfolios, the CogEcon study measures a wide range of characteristics that should influence households' portfolio choices. These include measures of risk preference, expectations, financial knowledge and attitudes, and cognitive status.

A second wave was fielded in early summer 2009. This wave (CogEcon 2009 post-crash) was designed to provide direct evidence on the effects of the financial crisis that began in September 2008. The post-crash study re-measures some of the CogEcon 2008 variables, but largely consists of questions to assess the change in circumstances, attitudes, and plans as a result of the financial crisis. The combination of the baseline measures of CogEcon 2008 and the change measures of CogEcon 2009 thus provide an important set of data for assessing how the financial crisis affected older Americans.

This paper links several key findings. Holding a high fraction of wealth in the form of stock is correlated with having high cognitive status and high levels of wealth. Households with low levels of wealth also reported being substantially affected by the financial crisis. These findings provide a nuanced picture of the effects of the financial crisis across older Americans. Those with disproportionate exposure to the financial crisis by virtue of having high shares of stock in their portfolios tend to have substantially higher cognitive capacity and greater wealth than average. This finding raises the possibility that those most directly affected by the stock market crash were well equipped to adjust to it.

By construction, low-wealth households were unaffected by the stock market decline because they had no financial wealth at stake. Nonetheless, they report similar downward adjustments in consumption and delays in the expected date of retirement as households that experienced substantial financial losses. This finding points to effects of the financial crisis on economic security that greatly exceeded the direct loss of value in the stock market. The paper will examine credit and labor market factors that help explain the overall effects of the financial crisis and how it affected different households differently.

The financial crisis led to a large decline in stock market value with potentially very serious implications for retiree finances. Stock holders, who tend to have relatively high wealth and relatively high cognitive capacity, might be better equipped than the average household to adjust to the financial crisis. On the other hand, the financial crisis was not just about a decline in the stock market. It involved a sharp decline in housing equity, a sharp increase in unemployment, and broad disruptions of credit markets. The CogEcon study, particularly its post-crash survey, was designed to capture the effects of all these developments.

Table 1 shows the loss in financial wealth as a consequence of the financial crisis—measured as the percent change from July 2008 to the date of the CogEcon 2009 in early summer 2009. The first two columns give the initial level of wealth. The next three columns give the 25th percentile, median, and 75th percentile of the percent change in wealth. Overall, the median decline in wealth was 15 percent. Those who lost more than 10 percent had much higher initial wealth because the high wealth group is more exposed to the stock market.

Table 1 also shows the powerful association of the level of wealth with the level of cognition. Likewise, notice the lower rate of loss for low cognition respondents owing to the fact that high cognition individuals hold a higher share of their financial

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wealth in stock. Finally, the last line of the table reminds us that about 20 percent of households in the 50+ age group have almost no exposure to financial wealth and therefore no direct exposure to the stock market crash.

The CogEcon 2009 post-crash survey contains measures designed to assess the effect of the financial crisis. Several of these are presented in Table 2. The measures include the percent change in non-durable consumption owing to the crisis, delays in purchasing vehicles, and delays in retirement. The striking feature of Table 2 is that those with no financial wealth behaved about the same as those who had substantial financial losses. Both groups report larger drops in consumption, greater deferral of vehicle purchases, and greater delays of retirement than those who had relatively small drops in wealth shown in the middle column of the table.

The CogEcon post-crash survey has a rich set of covariates that help explain why the effects of the financial crisis were so widespread. The paper presents multivariate analysis of the decline in planned consumption following the financial crisis.

- Within the population aged 50 years and older, homeownership is ubiquitous. About 90 percent of the CogEcon sample are homeowners. The average decline in house values they report is about the same as the average decline in wealth. Across households, the decline in house values accounts for roughly the same amount of the decline in consumption as the decline in financial wealth, though since there is not much variation across households, this estimate is not precise.

- A substantial minority of households report financial distress. Housing related financial distress is rare in this population. Being denied credit or making a late payment is more common. Financial distress is much more common among the non-wealth holders. They are five times more likely to report more than one indicator of financial distress than those with positive financial wealth.

- Controlling for a broad range of financial factors, there remains a role for the level of cognition in explaining the effects of the financial crisis.

Table 1. Financial Wealth and the Financial Crisis

	Financial wealth, July 2008		Percent change since July 2008				
	Mean	Median	Mean	25th ptile	Median	75th ptile	Obs.
≥\$10,000 wealth	\$516,123	\$270,001	-15.2%	-29.1%	-15.0%	-0.6%	655
Lost ≥10%	\$628,182	\$402,432	-28.7%	-35.5%	-26.8%	-19.1%	385
Lost <10%	\$356,336	\$122,404	4.0%	-4.7%	0.0%	3.3%	270
By fluid intelligence							
Bottom third	\$370,142	\$145,390	-12.1%	-24.2%	-8.4%	0.0%	162
Middle third	\$473,951	\$263,820	-14.4%	-28.0%	-14.3%	0.0%	256
Top third	\$661,461	\$386,551	-18.3%	-32.5%	-20.0%	-5.8%	237
<\$10,000 wealth	\$2,745	\$1,251	-3.4%	0.0%	0.0%	0.0%	157

Source: Wealth (retirement accounts plus cash and stock outside of retirement accounts) is from the CogEcon 2009 Post-crash survey. Fluid intelligence (number series score) is from the CogUSA survey.

Table 2. Consumption and Retirement Adjustments Owing to Financial Crisis

	Wealthholders		No financial wealth
	Lost ≥ 10%	Lost < 10%	
	Change		
Food at home	-1%	0%	-2%
Food away from home	-5%	-3%	-6%
Other nondurables	-5%	-3%	-6%
Total consumption	-4%	-2%	-5%
	Fraction of responses		
Delayed motor vehicle purchase	16%	12%	23%
Delay retirement (if working)	45%	30%	35%
	Years		
Mean delay retirement (includes zeros)	1.5	1.0	1.6

Source: CogEcon 2009 post-crash. Individual data. "No financial wealth" means financial wealth less than \$10,000. "Total consumption" is an unweighted average of the change of the three categories.

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