

# EXECUTIVE SUMMARY

## **MONEY MANAGEMENT BY LOW-INCOME HOUSEHOLDS: EARNING, SPENDING, SAVING, AND ACCESSING FINANCIAL SERVICES**

LISE MCKEAN, PH.D., SARAH LESSEM, AND ELIZABETH BAX  
CENTER FOR IMPACT RESEARCH  
AUGUST 2005

## **PROJECT BACKGROUND**

---

Opening and maintaining a checking or savings account at a credit union or bank are crucial steps for establishing the kinds of relationships with financial institutions that lead to qualifying for credit and developing assets. An estimated 22.2 million households or 56 million adults in the U.S. did not have a bank account in 2002. The lack of a bank account is more pervasive among low-income families than higher income families: 83% of families without bank accounts earn less than \$25,000 per year. Furthermore, as many as 22% of low-income families—more than 8.4 million families earning less than \$25,000—do not have a checking or savings account. Families in the lowest income group are even less likely to have accounts. An estimated 29.1% of families with incomes in the lowest twentieth percentile (\$10,300 or less) are without accounts, which is more than three times the median of 9.1% for all families.

Classifying households as either banked or unbanked is conventional in the literature on the use of financial services by low-income households. However, a continuum that encompasses banked, formerly banked, underbanked, marginally banked, aspiring to bank, and unbanked better characterizes the way low-income persons access the broad array of financial services available to them. For example, approximately one-half of those currently without a bank account had one in the past; people may have a bank account and still use alternative financial institutions such as check cashing outlets (CCOs), known as currency exchanges in the Chicago area; and 30% of persons without an account report some kind of ongoing relationship with a bank. In fact, the terms mainstream and fringe or alternative themselves depend on one's perspective. That is, what may be regarded as fringe or alternative in one community might be ordinary and mainstream in another.

A bank account can be a vehicle for maintaining and accumulating savings. However, having an account does not ensure that account holders are able to save. For example, although an estimated 78% of families with an annual income less than \$25,000 had bank accounts in 2001, 53.4% of this income group reported having saved in the previous year. For households in the lowest income quintile (\$10,300 or less), the savings rate is 30.0%. Furthermore, the reasons for saving differ among income levels, with families at lower income levels saving for more immediate expenditures such as rent and holiday gifts, compared with the longer timeframe of savings by higher income groups for future expenditures such as children's education and retirement.

## **FIRST ACCOUNTS PROGRAM**

In May 2002 the First Accounts Program, an initiative of the U.S. Department of the Treasury, awarded 15 grants for projects in twenty-five states. The purpose of the program was to expand access to financial services for low- and moderate-income individuals who currently do not have an account with an insured bank or credit union. The First Accounts Program was designed to develop financial products and services that could provide models in other communities and to provide financial education to low- and moderate-income individuals who did not have bank accounts.

As a First Accounts grant recipient, the Center for Economic Progress (CEP) in Chicago worked with local banks to design the First Accounts Express Savings and First Accounts Express Checking accounts, which offer safe deposits at reduced fees. The First Accounts checking and savings accounts were designed as no-cost accounts that permitted account holders to have a \$0 balance without accruing any fees. In addition to giving participants in the First Accounts Program access to these specially designed accounts, CEP also provided financial education workshops covering issues related to banking, personal financial management, and asset development as well as a Savings Club and individual financial counseling. The project-planning phase of CEP's First Accounts project began in the second half of 2002; the direct service component began in June 2003 and lasted one year, during which period it served 1,760 people.

In response to a request by CEP for a study of participants in its First Accounts project, the Center for Impact Research (CIR) conducted face-to-face interviews with 77 First Accounts participants between August and October 2004. The sample included First Accounts program participants who opened bank accounts as well as participants who did not open bank accounts. The information obtained in these interviews provides in-depth information about the participants' experiences in regard to using banks and non-bank financial services, establishing and maintaining savings, and building assets. The survey data also covers attitudes about saving and managing household finances. The findings on these topics are useful for better understanding the needs and experiences of low-income households in relation to accessing financial services and opportunities for asset development, which in turn can be used to enhance the curriculum of financial education workshops. However, it must be kept in mind that all except one of the survey participants in this study were African American, and that there are likely to be significant differences related to issues and experiences regarding access and use of financial services for other groups of low-income households—particularly for immigrants and those with limited English.

## **FINDINGS**

---

### **EMPLOYMENT AND INCOME**

The difficult and often dire financial circumstances that characterize the households of many First Accounts participants need be the starting point for making financial education workshops relevant to their daily life experiences. The low incomes of respondents in this study (median total household income for all respondents of \$1,269 per month; median household employment income for respondents' with household employment income of \$1,651 per month) are related to low wages, insecure employment, and unemployment. At the time of the survey nearly one-half

of respondents were unemployed; one-third of respondents who were employed were at their current job for less than one year; and 28.2% were employed for less than three months. Unstable employment and unpredictable and irregular work schedules lead to fluctuating incomes and make it difficult for many of these low-wage workers to budget for normal household expenses—not to mention save for emergencies.

Insufficient income leads to ongoing domestic hardships. For example, at least once over the past 12 months, 32.5% of respondents had to borrow money to pay for food and bills; 23.4% had no food at the end of the month; and 13.0% had their gas or electricity service disconnected because of overdue bills.

## **BANKING AND SAVING**

Over two-thirds of respondents (68.8%) currently had bank accounts; nearly one-fourth (23.4%) did not currently have a bank account but had an account in the past; and 7.8% never had an account. Respondents who currently had a bank account had significantly higher monthly household incomes (median of \$1,539; mean of \$1,680) than those without accounts (median of \$1,111; mean of \$1,147). Respondents with bank accounts were also marginally more likely to own a car, with 38% of those with accounts owning a car compared to 17.4% of those without bank accounts owning a car. In terms of household size, marital status, educational attainment, or employment status, there were no significant differences between respondents with and without a bank account.

Data about past bank accounts indicate that cycling through accounts is common. That is, persons open an account and use it until the balance runs down or fees accrue and the account is then closed. For example, 75% of respondents without a current account had one in past and 83% with a current account had a different account in past that had been closed. In addition to having overdrawn the account, the reasons respondents gave for closing their accounts were similar to the reasons of those who did not have a current account: insufficient resources to maintain the account and confusion about fees and policies.

With few exceptions, respondents reported being satisfied with their treatment at banks. Those with current and past accounts said the accounts helped them better manage their money, particularly noting that they used their accounts for cashing checks, paying bills, and direct deposit of paychecks. Respondents commonly said that savings accounts helped them focus on savings and that direct deposit to checking and savings accounts means having less cash at hand, which in turn helps reduce unnecessary spending. Several respondents also commented on the emotional benefits of having an account, particularly the security and sense of accomplishment of having money in the bank.

However, some respondents stated that they were not confident about their money management skills and were uncomfortable having a checking account because of danger of incurring high overdraft fees. These respondents were concerned that their low balances allow no cushion for miscalculations of how long a deposited check will take to clear or for mistakes in balancing the account. Other respondents who typically have low balances in their accounts said that they prefer to cash checks at check cashing outlets because they do not want to wait for the bank to clear the check. These respondents said that they cash checks at check cashing outlets because

they can then deposit cash into their accounts so it is immediately available for writing checks to pay bills.

Like their views on having bank accounts, respondents generally expressed positive views about saving money, stating that there is a financial and personal or emotional benefit to saving. However, nearly two-thirds (62.2%) of respondents currently were not saving in a bank account; and the level of those who were saving was low, with a median balance of \$225, and 44.8% with less than \$250 in their savings account. Lack of money after paying for basic necessities and having to pay debts were the reasons given by respondents for not saving or not saving more. Savings were often for short-term or more immediate expenditures, for example, 58.6% of those currently saving said they were saving for rent and 66.7% of those who were not saving said they would save for rent.

## RECOMMENDATIONS

---

Low-income households access banking and non-banking institutions for a range of financial services—checking and savings accounts, ATMs, credit cards, cashing checks, paying bills, and borrowing money. Programs to promote financial literacy and access to bank accounts are useful and needed. Such programs offer a pathway to other financial services, including credit and mortgages. The recommendations presented here are based on the data obtained by surveying participants in the First Accounts Program. They pertain to program and workshop design and curriculum development for programs with objectives similar to First Accounts—increasing skills in personal financial management and expanding knowledge of and access to financial and banking services. These recommendations are applicable to programs designed for participants with low incomes, unstable employment, and limited experience with banking services.

### FINANCIAL WORKSHOPS

These are topics about which respondents expressed concern, uncertainty, and a need for more information and guidance.

#### Public Benefits

- Provide information about programs, eligibility requirements, and application procedures for public benefits.
- Conduct screenings to identify households and individuals who may not know that they may be eligible for benefits.

#### Consumer Education

- Identify key issues of concern to participants. Issues pertinent to survey respondents include: banking and overdraft fees; car ownership, loans, and repairs; budgeting for utility, telephone, cable, and Internet bills; homeownership; student loans; life insurance; charitable donations; credit cards; and borrowing and lending money among family and friends.
- Incorporate into the curriculum information that explains the advantages and disadvantages for low income families of key issues related to personal financial management.

- Introduce a family workshop session that encourages participants to bring their adolescent children and adult household members. This family session would allow other members of the participant's household to learn about basic principles of personal financial management and better understand their role in family finances and how they can contribute to the participant's efforts to budget, manage expenses, and save.

## **FINANCIAL SERVICES**

- Continue to advocate for banking products and services appropriate to low-income account holders and more competitive fees for money orders to reduce reliance on check cashing outlets.
- Advocate to limit the amount of overdraft fees and to provide better information for account holders about the terms, conditions, and imposition of these fees.
- Advocate for banks to provide understandable information about the bank's confidentiality and security policies and ways that account holders can safeguard their personal banking information.
- Advocate for availability of direct deposit among both large and small employers.
- Advocate for integration of financial education and access to banking initiatives into workforce development programs.
- Continue to research and promote a better understanding of the continuum along which low-income persons access financial services—from the fully banked with checking and savings accounts to the underbanked to those without bank accounts who rely on check cashing outlets and other non-bank services to manage their finances.

Survey respondents report positive attitudes about the benefits of having bank accounts and their positive impact on money management. They also talk about the importance of saving and their efforts to save, with the belief that it is empowering to do so regardless of the amount. It must be kept in mind that given the high levels of economic hardship and low levels of savings, financial education and bank accounts in of themselves have limited scope for substantially improving the long-term financial prospects of the majority of these households. However, financial education and access to banking initiatives should be an integral component of workforce development programs.

Asset building initiatives need to take into account the many positions along the spectrum of financial services, from no bank accounts and no savings to fully banked with regular additions to savings. Building on an understanding of this spectrum, initiatives can explore opportunities to develop products and services that leverage the reach and accessibility of non-bank financial services. Furthermore, the actual financial situations of households need to be a key factor for program development. With this starting point, the messages and expectations of financial education programs will be respectful of participants' resourcefulness and informed about the underlying causes of their stressful financial circumstances and their formidable barriers to asset building.