THE FINANCIAL STATUS AND DECISION-MAKING OF THE AMERICAN MIDDLE CLASS

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For centuries the American middle class has served as the social backbone of the country. Among other contributions, its purposeful work has made it possible for the U.S. to become the dominant economy in the world today. This middle class also represents a majority of American voters.

Yet, as noted by numerous scholars and commentators, the American middle class has recently grown weaker as a result of several trends, particularly the stagnation of their incomes and increase in their job insecurity. Today, middle class households earn less than they did a decade ago, and little more than they earned two decades ago. The income of the typical American family, in 2010 dollars, was $49,445 in 2010 but $53,164 in 2000 and $48,423 in 1990. And the doubling of unemployment rates in the recent recession has generated economic insecurity among many more middle class workers than those who lost their jobs or saw them downsized.

This report focuses on the financial status and decision-making of the American middle class. It is based on two recent sources:

- An analysis of data found in the recently released Federal Reserve Board's 2010 Survey of Consumer Finances undertaken, for Primerica and the Consumer Federation of America, by Professor Catherine Montalto of The Ohio State University.
- A recent survey commissioned and designed by Primerica and the Consumer Federation of America that was carried out by Opinion Research Corp International (ORCI), which interviewed 2015 representative Americans from all income groups on the weekends of July 12 and 19, 2012.

The American middle class was considered, in analyzing the Fed data, to be those households with incomes between $35,600 and $94,600. Surprisingly, these households comprise only 40 percent of all households, with far more of them, 40 percent, having incomes below this level than those, 20 percent, having incomes above this level. In the ORC survey, the middle class was treated as the roughly 50 percent of all households with incomes between $30,000 and $100,000.

This report addresses questions such as the following: What are the financial assets, non-financial assets, indebtedness, and net assets of the American middle class? What are the key elements of these assets and debts, and how have they changed over time? How do middle class Americans rate their financial decision-making? What are the principal sources of information they use to make different types of financial decisions? Do these Americans think they have ever made bad financial decisions and, if so, how costly have these decisions been? Finally, if given $10,000, $100,000, or $1,000,000, how would they invest these funds for their retirement?

Financial Condition In 2010

According to the Fed data, in 2010 a typical middle class family held financial assets of $27,000. Nearly all of these 2010 families (98%) had a checking or savings account, and the typical (median) amount in these accounts was $3,900.

Only about three-fifths of these families (61%) had money in contributory retirement accounts, and these funds represented the bulk of financial assets for most families. The typical amount held by families in these accounts was $29,000.

Far fewer middle class families held other financial assets. In 2010, only 21 percent had a cash value life insurance policy, 15 percent stocks outside a retirement account, 14 percent certificates of deposit, and 13 percent U.S. Savings Bonds.

Not surprisingly, because of homeownership middle class families had far higher nonfinancial assets than financial assets. Over three-quarters (76%) owned a home whose typical value was $155,000. But because of mortgage debt, the actual value of these homes was lower. Nearly three-fifths (59%) of middle class families had mortgage debt whose typical value was $104,000.

The only other nonfinancial asset that was widely held was motor vehicles. A very large majority (94%) owned a vehicle or vehicles whose typical value was $17,000. Only a minority of these households had outstanding auto loans.

These auto loans and student loan debt represented nearly all of the installment debt held by over half (53%) of middle class families. The typical amount per family was $13,500. Nearly as many families (49%) carried credit card debt, yet the typical amount per family was much lower at $2,700.

Debt was not a significant burden for most middle class families. The typical debt to assets ratio was 27 percent. The typical debt payments to income ratio was 20 percent, and only 13 percent had a ratio above 40 percent. Only 9 percent had debt payments that were at least 60 days due.

Net assets represent the sum of financial and nonfinancial assets minus debts. In 2010, the typical middle class family held $94,700 in net assets.

Compared to 2007

The previous Fed Survey of Consumer Finances was conducted in 2007. Comparing data from this survey with those from the 2010 survey helps reveal why many middle class Americans are dissatisfied with their financial condition.

Between 2007 and 2010, the net worth of the typical middle class family declined 35 percent, from $145,600 to $94,700. In this period, the financial assets of the typical family fell 28 percent, from $37,800 to $27,300, primarily because the amount in typical retirement accounts declined from $38,800 to $29,000. Also in this period, chiefly because of the decline in home values, nonfinancial assets fell 18 percent, from $199,100 to $163,900.

Yet, debt remained pretty much the same. Consumer and mortgage debt of the typical middle class family was $85,400 in 2007 and $84,400 in 2010. And mortgage debt for the typical family with this debt declined only very slightly from $105,800 in 2007 to $104,000 in 2010.

Financial Decision-Making

The ORC International data on financial decision-making provides additional insight into the financial condition of middle class Americans.

Perceived Competence: Most middle class Americans rate their ability as "excellent" or "good" to make decisions on a wide variety of financial issues. But fewer rate their ability highly on relatively complex financial issues about which they make decisions infrequently. Over four-fifths said their ability to budget their income (81%), manage credit card debt (80%), and purchase auto insurance (83%) was good or excellent. But only about two-thirds rated highly their ability to save for retirement (63%), purchase a mortgage loan (67%), or purchase life insurance (66%).

Not surprisingly, many more older persons than younger persons rated their ability as excellent, for example, 56 percent of those 65 and older compared to 27 percent of those 18-34 for budgeting your income, and 48 percent of older persons compared to 33 percent of younger persons for saving enough for emergencies.

Sources of Information: Few middle class Americans said their principal source of information or advice about several specific financial decisions would be "information on the Internet or in books, magazines, or TV." And a surprisingly high percentage said they "wouldn't seek any information or advice, and just make a decision."

- Two-fifths said they would not seek information or advice in managing credit card debt (40%). And about one-quarter said they would not do so in purchasing auto insurance (25%) and life insurance (24%). Lower percentages said they would do so for purchasing life insurance (17%) and saving and investing (17%).
- The proportions who said they would use mainly information on the Internet or in publications were lower for these five decisions – managing credit card debt (16%), purchasing auto insurance (25%), purchasing life insurance (17%), purchasing a mortgage loan (16%), and saving and investing (15%).
- The percentages who said they would use information and advice from a financial professional tended to be higher for the relatively complex decisions about saving and investing (45%) and purchasing a mortgage loan (35%) though lower for purchasing life insurance

(24%), managing credit card debt (18%), and purchasing auto insurance (13%).

Somewhat surprisingly, the least well-educated were the least likely to seek information or advice in making these financial decisions. For example, 28 percent of those with a high school degree or less, but only 17 percent of college grads, would not seek information about purchasing life insurance. Similarly, 23 percent of the least educated, but only 10 percent of the best educated, would not seek information about saving and investing.

Bad Decisions: Two-thirds of middle class Americans (67%) said that, in the past, they had made at least one "really bad financial decision," and nearly half of those questioned (47%) acknowledged that they had made more than one of these bad decisions. When questioned about estimating the dollars lost because of these decisions, there were big differences between the median response ($5,000) and the mean (average) response ($23,000). That is because some losses were substantial. Eleven percent said their losses had been at least $50,000, and two percent said these losses had been $200,000 or more.

Investing for Retirement: Those surveyed were asked, if they were given a certain amount to invest for retirement, "what would you do with most of this money?" The amounts to be invested were $10,000, $100,000, and $1,000,000. And there were nine "investment" options – gambling on lottery tickets or at a casino or track, purchasing a cash-value life insurance policy, keeping funds in a safe deposit box, purchasing gold or precious metals, purchasing an annuity, purchasing certificates of deposit or U.S. Savings Bonds, purchasing a house or land, putting funds in a savings account, or purchasing stocks, bonds, and/or mutual funds.

For all three amounts, over three-fifths said they would select one of just three options – savings account, stocks/bonds, or house/land. But the proportions varied depending on the amounts invested. About a third with $10,000 (30%) or $100,000 (33%) said they would invest mainly in stocks/bonds. But only about one-fifth of those with $1,000,000 (21%) said they would do so. On the other hand, the proportion who said they would invest in real estate grew from 9 percent for $10,000 to 25 percent for $1,000,000. The proportion who said they would keep most of the funds in a savings account varied little among amounts – 23 percent for $10,000, 19 percent for $100,000, and 19 percent for $1,000,000.

Between 20 and 30 percent said they would invest the funds in one of three other options – an annuity, CDs/Savings Bonds, or gold/precious metals. The "gold bugs" represented only 6 percent ($100,000, $1,000,000) or 7 percent ($10,000) of those surveyed.

Comparison to Higher-Income Americans: There were some significant differences between responses of middle-income and upper-income ($100,00 and above) Americans. More upper-income respondents than middle-income ones rated highly their decision-making about saving for retirement (76% vs. 63%) and about purchasing a mortgage loan (77% vs. 67%). And fewer upper-income respondents said they had made a least one bad financial decision (61% vs. 67%), but predictably, because they had more money to spend and invest, their losses tended to be higher -- $61,000 vs. $23,000 on average.

One striking difference between the financial decision-making of upper- and middle-income Americans is their confidence in stocks and bonds. Nearly half of the upper-income group (48%) said they would invest most of $1,000,000 in stocks or bonds while little more than one-fifth of the middle-income group (21%) said they would do so. While the differences for lesser amounts invested were not as great, they were still significant.

Summary and Conclusions

Most middle class Americans are not financially desperate. In 2010, after being battered by economic recession, they typically had:

- Sufficient funds in transactions accounts (checking and saving), $3,900, to cover most unexpected expenses.
- Total financial assets of $29,000.
- Manageable debts, with a debt to asset ratio of 27 percent, and only 9 percent with debt that is at least 60 days overdue.

However, in 2010 they were poorer than at the outset of the recession three years earlier. While their consumer and mortgage debt remained about the same, their financial assets were 28 percent lower and their nonfinancial assets 18 percent lower, and in consequence, their net assets were 35 percent lower.

Most middle class Americans rate their ability to make financial decisions highly. But more of them had confidence to make decisions on issues such as budgeting their income and managing their debt than on more complex issues such as saving and investing or purchasing a mortgage. Moreover, two-thirds acknowledged that, in the past, they had made at least one "really bad financial decision." This decision had typically cost them $5,000 but for a number of respondents, much larger sums.

Perhaps these mistakes help explain why, on a range of decisions from managing credit card debt to saving and investing, most middle class Americans said they would rely primarily on information or advice from financial professionals, friends or family, or the Internet or publications. Only a minority said they would not seek information or advice in making these decisions.

Their losses during the recession may also help account for their conservative investment preferences. Nearly as many (19%) would invest $1,000,000 in a savings account as in stocks and bonds (21%). And despite their loss of home equity during the recession, an even higher percentage (25%) would invest most of $1,000,000 in real estate. However, only a very small minority (6%) would invest this amount in gold or precious metals.

The Consumer Federation of America is an association of nearly 300 nonprofit consumer organizations that was established in 1968 to advance the consumer interest through research, advocacy, and education.

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