Financial Crisis in American Households

The Basic Expenses That Bankrupt the Middle Class

Joseph Nathan Cohen

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CHAPTER TWO

A Snapshot of U.S. Household Finances

Talking about other people's money is generally considered impolite. Many people don't share financial information with friends and family. For this reason, we tend to have a vague sense of other people's financial situations. Maybe we know that a $50,000 income is considered mid-range nationwide and that a six-figure income is relatively good. We might know how much someone has to earn to move up in tax brackets or qualify for social assistance programs. Often, the only financial details that people grasp are their own, and much of society doesn't even understand much about their own personal circumstances.

Most people see their financial situation as normal, typical, or average. A 2012 Pew Research Center survey asked Americans to identify the economic class to which they belonged. About 91 percent of respondents self-identified with some part of the middle class (about 8 percent saw themselves as poor, and 1 percent as rich).[1] On this basis, we might infer that the U.S. middle class earns between the 8th and 99th percentiles of income or wealth. Data from the Federal Reserve Bank's *Survey of Consumer Finances*[2] suggests that, in 2013, these class dividing lines imply that the middle class has incomes between $12,000 and nearly $700,000 per year. Their net worth is implied to range between nearly $8 million and less than zero. In other words, a large number of people in very different financial circumstances think that their economic situations are typical.

This penchant to see our financial situation as typical is partly a result of our social environment's insularity. We tend to work and live among others whose financial situations are roughly comparable to our own. We mix

with people who live in the same community, share a workplace, or have children who go to the same school. In an economically segregated society, people are surrounded by others under similar circumstances. Although we may know people who are somewhat richer or poorer, the bulk of our social relations have economic circumstances comparable to our own, and we tend not to mix with people whose circumstances are dramatically different. When everyone around us is similar to us, it is natural to assume that we are typical.

All of this can skew our understanding of household finances in general. The issues that might press a wealthier household into financial problems (e.g., overpriced higher education, overspending on lattes and designer clothes, or not having enough retirement savings to retire comfortably) are very different from those faced by people closer to the bottom of the economic hierarchy (e.g., the cost of not having access to an affordable bank account or the strains of finding basic child care or transportation to work). Most of the country more closely resembles the bottom class than the upper-middle class (though the market for scholastic policy analysis skews wealthy).

To provide a more concrete anchor to this book's discussions, this chapter examines how much money Americans earn, own, and owe. It describes the basics of household finances, parses out how household finances differ across major U.S. demographics, and attempts to flesh out a more detailed picture of the U.S. economic hierarchy.

Understanding Households' Financial Circumstances

What does it take to be rich in the United States? A 2011 Gallup poll asked this question to a random sample of Americans, and more than half settled on an annual income of $150,000 a year *or less*. These estimates often draw laughs of incredulity. The audiences for academic presentations about household finances skew more educated and wealthy, so many of them live in, or come from, households that would fit this definition of "rich." Most of them flatly reject the idea that they are rich. However, a look at the broader distribution of wealth makes it clear that a family with two $75,000-a-year jobs is very well off in comparison to the rest of the country. They may not be among the top 1 percent, but they have more money coming in than 9 out of 10 U.S. families. It is hard to see a household that out-earns 90 percent of those living in one of the world's richest societies as being in hard-luck circumstances.

Most people focus on income because the numbers are easy to comprehend. Our annual incomes are printed on our pay stubs, we have some ability to map income estimates to people's job titles, and we see income

differences laid out on tax forms and job posting sites. However, income is only part of a household's financial picture. What constitutes a "high" or even "sufficient" income depends on people's living costs, which can vary widely depending on geography, household composition, household members' health, and a range of other circumstances. Moreover, people with similar incomes can be in very different overall circumstances that are determined by wealth and debt. There are lower-income Americans with considerable wealth, and there are high-income Americans getting crushed by debt.

These considerations illustrate some of the complex issues involved in judging the state of household finances and the utility of starting our discussion about U.S. household finances with an exposition of the basic balance sheet and income statement concepts that determine a family's financial situation. We start our discussion with a brief exposition of basic personal finance concepts.

Incomes

Incomes are money flows into a household's accounts. Households can receive income from a variety of sources. In 2013, about 72 percent of households received money from wages (payment from an employer for doing a job). About 42 percent received government checks. Just under one-quarter (22 percent) received financial (e.g., investment portfolio) income. About 8 percent received income from a personal business. Less than 5 percent received alimony or child support.

Gross income refers to pretax income. The distribution of U.S. households' gross income is depicted in Figure 2.1.[3]

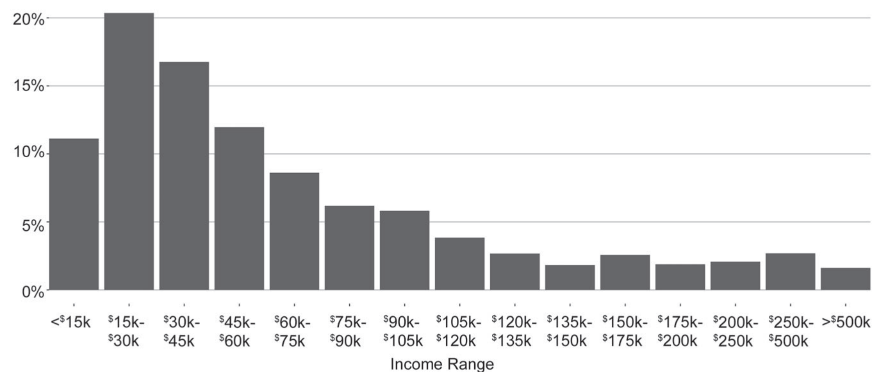

Figure 2.1 The Distribution of U.S. Household Income, 2013.
Source: Federal Reserve Bank (2014), *Survey of Consumer Finances.*

The data suggest that the median household received roughly $47,000 of income in 2013. This is household income, which in many cases represents the combined earnings of multiple earners. The middle 50 percent—those between the 25th and 75th percentiles—received between $24,000 and $90,000. The data estimate that 13.5 percent earn less than a poverty-line income, and about one-tenth earn six-figure incomes or more. The top 1 percent took in an income of $696,000 in 2013.

The bulk of household income comes from two sources: wages and government payments. Among all households that earned wage income, the median took in $48,000 from this source. The median take from government payments was $15,000, with the middle 50 percent (the 25th and 75th percentiles) taking in between $8,400 and $24,700. Among the 22 percent of households receiving financial income, the median proceeds from these investments was $958, and one-quarter of this group took in less than $10 a month from this source. Personal businesses also often yielded small incomes; of the 8 percent of households receiving business income, only about 1.8 percent received the equivalent of a median household income from that source.[4]

About 18 percent of households received no wages, financial income, or business income. The median household in this group earned about $19,000 in income in 2013, and the middle 50 percent took in between $12,000 and $33,000. Much of this money came from government payments (with a median take of $12,000, primarily through Social Security), supplemented with private pensions, familial transfers (e.g., alimony and child care), or other atypical sources. Social Security is by far the biggest type of government payment received, with several times more beneficiaries receiving several times larger checks than from other government payment programs (e.g., unemployment insurance or workers' compensation programs, or Supplemental Nutritional Assistance Program [SNAP], Temporary Assistance for Needy Families [TANF], or Supplemental Security Income [SSI] welfare programs for the poor).[5]

Taxes on Income

Taxes on income shape the amount of income that is ultimately available for households to spend. There are two major types of taxes on income. What we typically call *income taxes* are federal, state, and sometimes local governments' tax levies on household incomes. These are the federal and state income tax lines on people's pay stubs, which are mainly involved when people file their 1040s and their state/local equivalents in April. These income taxes are generally progressive (some states have flat taxes), which

means that wealthier people pay more than poorer people. For example, in 2013, a household earning less than $8,925 owed 10 percent in federal income taxes, whereas one earning $100,000 owed 28 percent, and one earning more than $400,000 owed almost 40 percent. Higher income families are often able to pay less in taxes than the rates listed in federal tax return bracket tables because households have a range of deductions and credits that ultimately reduce their obligations. Although tax rates seem highly progressive, the larger tax structure is designed to enable people to move down in tax bracket by structuring their financial reports in ways that make their incomes nontaxable or taxable at lower rates.

A second type of income tax is *payroll taxes*, which are levied on employment (including much self-employment) income. Payroll taxes have increasingly replaced personal (and corporate) income taxes as an income source for the federal government.[6] These are the Social Security and Medicare tax lines on your pay stubs. Payroll taxes are often construed as a form of non-taxes, both in political debate and in major household finance data sources. The tax status of payroll taxes is complicated by the fact that they are nominally tied to some (vague) future promise of receiving health insurance and cash payments in old age. As such, it resembles a pension investment. However, it also resembles a regular tax and associated welfare program, in the sense that Social Security is a pay-as-you-go system where today's workers pay for the benefits of today's elderly. Presumably, today's young workers will receive similar benefits when they are old. To the extent that they do not, then payroll taxes are simple taxes that pay for the working-age population's elderly contemporaries, much like tax-financed welfare programs pay for their poor contemporaries.

Federal payroll taxes are flat taxes levied against employment income that, in 2013 (the survey year), amounted to a rate of 7.65 percent on the first $113,700. This income cap helps drive down the rate paid by higher income households. The data suggest that the median households earning less than $50,000 paid 7.61 percent of their income in payroll taxes, and the middle 50 percent paid between 5 percent and 7.65 percent. In contrast, households that were earning at least $250,000 paid 5.3 percent of their income in payroll taxes, with the middle 50 percent of that group paying between 4.4 percent and 5.7 percent. Higher income households pay proportionally less in payroll taxes due to these caps. The net result is that this is partly a regressive tax, as poorer people pay proportionally more of their income. The program is also regressive in the sense that people who earned more money in their working years receive bigger cash payments. Richer people actually receive the biggest Social Security payouts.

Financial Obligations, Discretionary Spending, and Savings

In addition to taxes, often families are tied into several contractual *financial obligations*, which are legally binding payment obligations. For example, households have to repay debts, such as a vehicle lease or rent. Some households are required to pay child support or alimony. Federal Reserve estimates maintain that the average U.S. household owes about 15 percent of its posttax income in mortgages or rents, property tax payments, home insurance, and service payments on consumer debts.[7] Note that this is an average. As discussed later, much of the country carries little debt, and many households have already paid off their mortgages. These averages are pulled up by a narrower set of households that carries larger obligations.

The amount of income left after a household pays its taxes and meets its financial obligations is available for *discretionary spending*. These are spending choices that the household has the ability to make or forgo. Money that is left unspent is *saved*, which can be used to build a households' wealth.

Wealth

We tend to understand people's economic situation with reference to their incomes. People are classified as poor when their incomes fall below the poverty line. Many of us assume that people are "rich" if their incomes are high. Wealth is an equally critical—some might argue more critical—determinant of households' financial security. *Wealth* (or "net worth") is the value of a household's assets, less the value of its outstanding debt. Figure 2.2 describes the distribution of household wealth.

Data from the *Survey of Consumer Finances*[8] suggest that the median household had a net worth of about $81,000. The distribution of wealth varies more widely than income. The middle 50 percent—those between the 25th and 75th percentiles—registered between $9,000 and $315,000 in net worth. About 13 percent of households have a negative net worth (i.e., they owe more money than the value of their possessions). In contrast, about 18 percent are worth at least $500,000, 9 percent at least $1 million, and 0.6 percent at least $10 million.

Households hold their wealth across a range of *assets*, that is, property that can be converted into money. The most common forms of assets held by households are cash accounts (held by 93 percent of households), vehicles (86 percent), homes (65 percent), retirement accounts (49 percent), nonretirement financial investments (42 percent), or owned businesses (10 percent). Generally, these holdings are modest. For example, the median

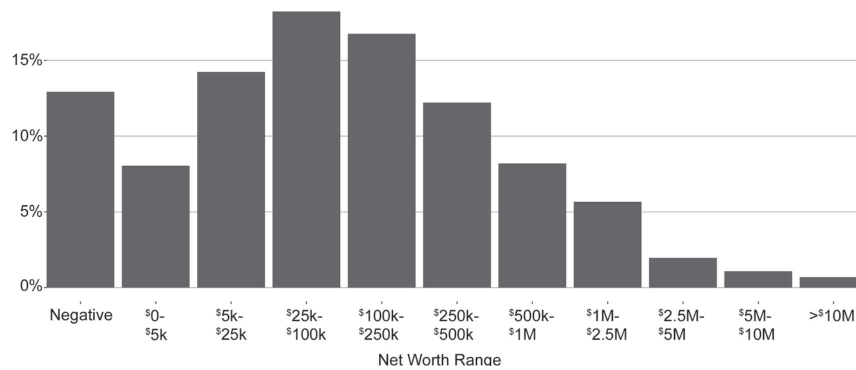

Figure 2.2 Distribution of U.S. Household Net Worth, 2013.
Source: Federal Reserve Bank (2014), *Survey of Consumer Finances.*

cash account held about $4,520, and 25 percent of households' cash accounts hold less than $900. The median owned home was worth $170,000. Few households have retirement savings that could cover more than a few years at the poverty line.

The value of assets is offset by *debts*, that is, borrowed money that a household is contractually obligated to repay. Debt is an important part of asset acquisition. The acquisition of major assets, such as a home, vehicle, or, in the United States, a postsecondary education, can require more money than families typically have saved. They must borrow money to ultimately accumulate money.

About 74 percent of households carry debt. The most common forms of debt are home-related, such as mortgages, home equity loans, or lines of credit. About 42 percent of households (66 percent of homeowners) carry these types of loans, and these debtors owe a median of $60,000 (or 15 percent of household assets) on these kinds of debt. Home-related debt is by far the biggest debt on household balance sheets. Education debt is a second important form of debt. Roughly one-quarter of households carried education debt, with a median debt of $16,720 (18 percent of household assets). Credit card debt is often discussed, but it is a minor item on household balance sheets. About 42 percent of U.S. households carried credit card balances, and the median balance carried by this minority was about $2,300 (or 1.5 percent of household assets—credit cards are generally extended to people with incomes and assets).

These are the basic parts of households' financial picture. A household must manage inflows and outflows of money, save money, and accumulate money while managing debt. Some households successfully juggle these

moving parts, while others find this balancing act more difficult. Who tends to succeed, and who is more prone to difficulty? We turn to this question next.

Demographic Differences in Financial Fortunes

Demographic comparisons are useful in helping us understand what is going on with household finances. Knowing who is faring better or worse in terms of earning income may help shed light on what is happening with U.S. household finances. In this section, we concentrate on seven types of demographic categories that demarcate meaningful differences in financial situations: sex, race, age, education, marital status, labor force status, and parental status.

Table 2.1 spells out some of these differences in terms of what people earn and own. In reading these statistics, remember that these categories overlap and cut across each other. Households are more likely to be headed by someone who is married, in the working-age population, white, employed, male, and with less than a college degree's worth of educational attainment. These characteristics describe general tendencies rather than provide a profile of the majority. Only about 11 percent of U.S. households are headed by a working-age, married, employed white man with a high school degree or less.

Income

Household incomes tended to be higher in households headed by men, non-Hispanic whites, the college-educated, the employed, and those who were paired (married or cohabiting). Households headed by a female, nonwhite, Hispanic, young, undereducated, unemployed, or unpaired person were more likely to be poor.

Some of these differences make sense. For example, younger people are often studying or just starting out in their careers, and they have been hit hard by unemployment in recent years. Older people are less likely to be working or are working less than they did during their peak earning years. Paired adults earn more because there are more potential earners, or a division of labor enables one member to commit more fully to earning than he or she would as a single person. The college-educated are presumably better trained for better jobs. Traditionally, women and nonwhites have been subject to discrimination in job markets, and nonwhites' difficulty in accumulating wealth has been compounded by housing discrimination.

Table 2.1 Demographic Profile of U.S. Household Heads and Their Finances, 2013

	# HHs (Millions)	% HHs	Income			Net Worth			
			Median	% Poor	>$100k	Median	<$20k	>$200k	>$1M
Total	**123**	**100%**	**$46,668**	**14%**	**21%**	**$81,456**	**33%**	**34%**	**9%**
Sex									
Male	88	72%	$59,857	10%	27%	$113,440	28%	39%	12%
Female	35	28%	$27,265	23%	5%	$29,660	46%	21%	3%
Race									
White, Non-Hispanic	82	67%	$55,799	9%	26%	$142,122	24%	43%	13%
Nonwhite or Hispanic	40	33%	$33,480	23%	11%	$18,184	51%	16%	3%
Age									
<35	25	21%	$35,103	24%	10%	$10,433	62%	8%	1%
35–44	21	17%	$60,872	13%	28%	$46,978	37%	26%	6%
45–54	24	20%	$60,872	11%	28%	$104,970	29%	37%	10%
55–64	23	19%	$55,191	10%	26%	$165,068	24%	46%	15%
65–74	16	13%	$45,897	9%	21%	$232,282	14%	54%	19%
75+	13	11%	$28,204	13%	7%	$195,574	16%	49%	9%
Education									
<HS	13	11%	$22,522	34%	2%	$17,278	52%	15%	1%
HS	38	31%	$36,726	16%	8%	$52,287	38%	24%	3%
Some College	23	19%	$40,987	14%	14%	$47,080	39%	27%	6%
College	48	39%	$79,539	6%	39%	$218,904	21%	52%	19%

(continued)

Table 2.1 *(continued)*

	# HHs (Millions)	% HHs	Income			Net Worth			
			Median	% Poor	>$100k	Median	<$20k	>$200k	>$1M
Total	**123**	**100%**	**$46,668**	**14%**	**21%**	**$81,456**	**33%**	**34%**	**9%**
Marital Status									
Paired	70	57%	$70,408	7%	32%	$148,328	24%	43%	14%
Unpaired	53	43%	$28,001	22%	5%	$31,880	45%	22%	4%
Labor Force									
Working	87	71%	$56,002	11%	25%	$118,060	28%	39%	9%
Not Working	35	29%	$29,421	19%	9%	$69,112	35%	32%	10%
Life Cycle									
Under 55, Unpaired, and Childless	17	14%	$31,694	23%	6%	$14,195	55%	13%	2%
Under 55, Paired, and Childless	11	9%	$63,611	4%	26%	$59,370	36%	28%	4%
Under 55, Paired, and with Children	31	25%	$75,278	10%	35%	$75,996	32%	33%	9%
Under 55, Unpaired, and with Children	11	9%	$28,204	32%	4%	$8,396	65%	7%	1%
Over 55 and Working	22	18%	$69,191	4%	33%	$260,490	15%	56%	22%
Over 55 and Not Working	30	24%	$31,450	15%	10%	$157,148	22%	44%	10%

Source: U.S. Federal Reserve (2014).
Note: Households counts may not add up to 123M due to rounding.

These individual demographic factors are related. For example, female households are more likely to be single (as paired households tend to identify the male as the "head"). Single adult households are disproportionately younger or older. Younger or older people are more likely to be unemployed, as are those without a college education. Whites have higher rates of college attainment relative to nonwhites/Hispanics as a whole. We could go on and on with these chains of relationships. The main point is that the individual effects of these demographic factors need to be parsed by using an analytical method called regression analysis,[9] which separates out the independent explanatory factors on a particular outcome. The procedure helps us discern the degree to which sex, race, education, age, marital status, or parenting status coincide with higher earnings, net of each other. The results are presented in Table 2.2.

The results suggest the typical female-headed household can be expected to earn about 7 percent less than a household headed by a man of the same race, age, education, and marital, labor force, and parental status. A household headed by a nonwhite or Hispanic person earns almost one-quarter less than an otherwise similar household headed by a white person. Households headed by older people tend to earn double that of a younger household with similar labor force status, educational attainment, and so on. The typical college graduate is estimated to earn 2.5 times the income of an otherwise similar household headed by a college dropout. Parents earn slightly more than nonparents. Income-earning advantages are accruing to men, whites, older people, the more highly educated, people who are paired, people who are working, and people with children.

Wealth

The differences in wealth are far starker than differences in income. Table 2.3 describes the results of a similar regression analysis predicting household wealth.

Some of these results are more straightforward to explain. For example, older people have much more wealth than younger people, in part as a result of the young not having had enough time to accumulate wealth of their own. Moreover, older people are more likely to have inherited any family wealth that might exist. More educated households have more wealth, in part because their higher incomes have allowed them to save more money and accumulate more wealth. Lower incomes and potentially higher living costs might also explain why single people are estimated to have one-quarter the accumulated wealth of their paired counterparts. Wealth differentials for those who are working might also exist for the same reason.

Table 2.2 Demographic Predictors of Household Income, 2013

	Estimate	Coeff.	SE
Baseline Income	**$17,891**	**9.792**	**0.043**
Sex (Baseline: Male)			
Female	–7%	–0.072	0.035
Race (Baseline: White Non-Hispanic)			
Nonwhite/Hispanic	–23%	–0.268	0.022
Age (Baseline: <35 years)			
35–44	+50%	0.403	0.032
45–54	+51%	0.412	0.036
55–64	+70%	0.533	0.033
65–74	+98%	0.685	0.036
75+	+85%	0.614	0.038
Education (Baseline: <HS)			
HS	+41%	0.342	0.030
Some College	+66%	0.505	0.038
College	+162%	0.962	0.029
Marital Status (Baseline: Paired)			
Unpaired	–54%	–0.774	0.036
Labor Force (Baseline: Not Working)			
Working	+64%	0.497	0.026
Parental Status (Baseline: No Children)			
Has Children	+13%	0.123	0.027

Model predicts logged household income.
Coeff. = Coefficient (predicted effect of category on logged income).
SE = Standard error of estimated effect.

Source: U.S. Federal Reserve (2014).

The Economic Classes

As noted at the outset of this chapter, most Americans have a vague grasp of other people's financial situations, and they often understand society-level financial issues through the prism of their personal situation and the situations of those around them. Our understanding of how household finances differ often involves a vague three-category typology. The widespread sense is that we have a prosperous and privileged upper

Table 2.3 Demographic Predictors of Household Net Worth, 2013

	Estimate	Coeff.	SE
Baseline Net Worth	**–$30,954**	**12.30**	**0.03**
Sex (Baseline: Male)			
Female	–11%	–0.11	0.02
Race (Baseline: White Non-Hispanic)			
Nonwhite/Hispanic	–19%	–0.21	0.01
Age (Baseline: <35 years)			
35–44	+25%	0.22	0.02
45–54	+54%	0.44	0.02
55–64	+92%	0.65	0.02
65–74	+142%	0.89	0.03
75+	+143%	0.89	0.03
Education (Baseline: <HS)			
HS	+8%	0.21	0.02
Some College	+24%	0.59	0.02
College	+79%	0.59	0.02
Marital Status (Baseline: Paired)			
Unpaired	–29%	–0.25	0.02
Labor Force (Baseline: Not Working)			
Working	+22%	0.20	0.02
Parental Status (Baseline: No Children)			
Has Children	+1%	0.01	0.02

Model predicts logged household net worth (Shifted + 250000).
Coeff. = Coefficient (predicted effect of category on net worth).
SE = Standard error of estimated effect.

Source: U.S. Federal Reserve (2014).

class, as well as an underclass that struggles. In between these two groups, we understand there to be a middle group of regular people, whose economic fortunes are the topic of debate. In the abstract, the scheme is easy to grasp.

When we move beyond these broad generalities, it becomes quite clear that people's grasp of household finances differs. Very poor people think that they are middle class, as do many multimillionaires. As discussed at

the outset of this chapter, this is probably related to the fact that most people are surrounded by others who are in roughly the same financial position. We tend not to mix with people who are markedly richer or poorer than us, which leaves us with a very weak sense of the financial situation faced by people who aren't like us. Table 2.4 presents a better-specified view of how household finances differ across the U.S. economic hierarchy.

At the top of the economic pyramid, there are the wealthy and near-wealthy. These two groups are distinguished by their considerable accumulated wealth, which seems roughly sufficient to guarantee that a person never has to work again (as long as they keep their lifestyle expectations in check). At the bottom of the economic pyramid, there are those conventionally considered society's poor. They tend to earn and own little. Between these two extremes, there are three groups termed the "middle class." They may earn a living wage and only sometimes accumulate much in the way of wealth, most of which is invested in a house. The middle class comprises about 86 percent of society.

The Wealthy

When most people think about the wealthy's possessions, they imagine the accoutrements of the rich—fancy homes, fine art, expensive cars, designer clothing, vacation homes, and so on. However, these are not the possessions that define wealth. Income-generating assets make wealthy people wealthy. The bulk of the wealthy's accumulated wealth is held in income-generating property, such as businesses, financial investments, and nonresidential real estate. Over the past several decades, these types of assets have been spectacularly profitable, both in comparison to how profitable they were in the mid-20th century and in comparison to labor today.[10]

Questions about the wealthy must always deal with the nagging question of where to draw the line between the rich and nonrich. Just how much money does it take to be considered "wealthy"? Different people harbor different definitions. As noted earlier, more than half of the country believes that it takes a yearly income of $150,000 to be "rich." At the other end of the spectrum, there are people like Louisiana Congressperson John Fleming, who argued that his household could not bear paying more taxes despite his $6 million annual income because after "you pay 500 employees, you pay rent, you pay equipment, and food," you are left with "a mere fraction of that"—"by the time I feed my family, I have maybe $400,000 left over."[11] People harbor different ideas about who should be considered rich.

Table 2.4 A Typology of U.S. Economic Classes

	Overall	**Poor** Income Below PL	**Lower-Middle** Income Below 200% PL	**Middle-Class** Income 2x–4x PL	**Upper-Middle** Income Above 400% PL	**Near Wealthy** Net Worth Above $1.4M	**Wealthy** Net Worth Above $5.3M
% U.S. Households	**100%**	**13%**	**23%**	**28%**	**29%**	**5%**	**2%**
Median Income	**$47k**	**$11k**	**$25k**	**$46k**	**$101k**	**$192k**	**$520k**
[25th, 75th Percentile Values]	[$24k, $90k]	[$9k, $16k]	[$18k, $32k]	[$37k, $61k]	[$75k, $142k]	[$110k, $311k]	[$259k, $1M]
% Receive [Median Received]:							
Wages	72% [$46k]	52% [$10k]	59% [$25k]	76% [$44k]	87% [$91k]	68% [$157k]	70% [$222k]
Government Payments	44% [$12k]	66% [$8k]	58% [$16k]	42% [$17k]	27% [$17k]	41% [$27k]	39% [$27k]
Business Profits	16% [$15k]	6% [$4k]	9% [$12k]	14% [$12k]	19% [$17k]	48% [$41k]	72% [$123k]
Financial Income	23% [$958]	4% [$602]	8% [$244]	18% [$300]	35% [$588]	72% [$16k]	87% [$78k]
Median Net Worth	**$81k**	**$5k**	**$16k**	**$77k**	**$225k**	**$2.3M**	**$8.5M**
[25th, 75th Percentile Values]	[$9k, $316k]	[$0, $34k]	[$1k, $86k]	[$14k, $218k]	[$89k, $585k]	[$1.8M, $3.2M]	[$7M, $14M]

(*continued*)

Table 2.4 *(continued)*

	Overall	Poor	Lower-Middle	Middle-Class	Upper-Middle	Near Wealthy	Wealthy
		Income Below PL	Income Below 200% PL	Income 2x–4x PL	Income Above 400% PL	Net Worth Above $1.4M	Net Worth Above $5.3M
% Possess [Median Value]:							
Home	60% [$180k]	23% [$92k]	42% [$120k]	61% [$150k]	81% [$225k]	95% [$539k]	92% [$1M]
Vehicles	86% [$19k]	62% [$7k]	80% [$10k]	92% [$15k]	95% [$24k]	93% [$33k]	96% [$47k]
Cash Accounts	92% [$7k]	72% [$556]	86% [$1k]	97% [$4k]	99% [$13k]	99% [$71k]	100% [$193k]
Retirement Accounts	47% [$53k]	5% [$4k]	21% [$9k]	49% [$24k]	77% [$80k]	88% [$443k]	89% [$780k]
Financial Investments	24% [$25k]	7% [$5k]	11% [$7k]	24% [$10k]	41% [$20k]	73% [$551k]	85% [$2.4M]
Business Equity	10% [$100k]	3% [$22k]	4% [$23k]	8% [$29k]	12% [$60k]	36% [$784k]	72% [$3.2M]
Demographics (% Headed by):							
White	70%	48%	58%	74%	81%	91%	94%
Under 35 Years	21%	37%	24%	21%	15%	1%	2%
Over 65 Years	24%	18%	28%	26%	17%	38%	38%
Married/ Cohabiting	57%	30%	44%	59%	72%	84%	88%
College Degree or More	39%	16%	20%	34%	60%	82%	84%
Employed	71%	60%	61%	72%	83%	72%	77%

PL = poverty line, k = thousands, M = millions.
Source: U.S. Federal Reserve (2014).

Drawing a practical dividing line between the wealthy and nonwealthy is difficult, unless you set it at some patently uncontroversial level, such as a net worth in the hundreds of millions or billions of dollars. Many single-digit millionaires reject the idea that they are wealthy. Many nonmillionaires have difficulty envisioning how someone with that much net worth could be worried about money.

Where to draw the line? At some point, an analysis needs to set provisional definitions in order to move past measurement debates and start interpreting data. The analysis for this book is based on two thresholds. The higher threshold, which is designated the "wealthy," includes households with a net worth of $5.1 million or more. The lower threshold, designated the "near-wealthy," has a net worth of $1.4 million or more. The former group comprises about 2 percent of society, and the latter comprises about 5 percent. Moving forward, references to wealthy Americans, refers to both groups.

Explaining the Thresholds

Why these thresholds? Here, "wealthy" is defined as having enough wealth to finance a typical or comparatively privileged income into perpetuity. A wealthy person has enough wealth to be reasonably assured of maintaining a regular person's lifestyle without ever having to work again. They are in a position of supreme security, and the money worries faced by this group are probably more fairly characterized as concerns with maintaining a privileged lifestyle and transmitting that advantage to future generations than with genuine fears of absolute deprivation. We use these two criteria to demarcate two groups: the *wealthy*, who are in a position of supreme security, and the *near-wealthy*, who are in a reasonably secure position.

These are the standards used to distinguish the wealthy and near-wealthy from the rest of society. We want a level of wealth that can generate sufficient living income indefinitely, where people can survive "on the interest" without spending away their principal (original) investment.[12] We presume that the near-wealthy can survive on a median income and that the Wealthy can survive on a 75th percentile income (accounting for cost-of-living increases).[13] Regarding the amount of risk assumed for our lower, near-wealthy standard, we will assume an asset portfolio that is wholly invested in financial assets (no proprietary businesses or real estate) with 25 percent of its funds invested in T-bills, 50 percent in Treasury bonds, and 25 percent in an S&P 500 index fund.[14] This type of allocation is roughly similar to what the investment analysis firm Morningstar would describe as a conservative investment portfolio.[15] For our higher standard, we consider a 25 percent T-bill/75 percent T-bond allocation, which mirrors

Morningstar's recommended allocations for an "Ultra Short-Range" income-oriented portfolio for retirees. Most financial planners would agree that these allocations are very conservative.

Between 1928 and 2010, blue chip stocks (as measured by the S&P 500) appreciated by an average annual rate of 11.3 percent, or 8.2 percentage points above inflation.[16] Blue chip long-term debt (as measured by the 10-year Treasury bond) averaged a real (inflation-adjusted) appreciation rate of 2.1 percent annually. Short-term debt (measured by the 3-month T-bill) averaged 0.5 points over inflation. This renders an expected real annual rate of return of 3.2 percent for our lower standard and 1.7 percent for our higher standard of risk aversion.[17]

If we want to receive $90,000 (inflation-adjusted) into perpetuity, at a real return rate of 1.7 percent, the formula suggests that we would need about $5.3 million. A person with $5.3 million in accumulated wealth is extremely secure in the expectation that they can live among society's top 25 percent forever, or at least the rest of their lives, without having to work or assume much in the way of financial risk. To receive $45,000 at a real return rate of 3.2 percent per year, we would need about $1.4 million. A person could secure a median income with a quite conservative investment portfolio. We use these thresholds to divide the wealthy and near-wealthy from the rest of society.

Highly Diversified, and More Invested in Businesses and Finance

In addition to having more money, these wealthy are also distinguished by the diversification of their income and assets. Whereas most households tend to earn the bulk of their money from one or two sources and have most of their assets stored in one or two assets, wealthy households are diversified.

First, wages play less of a role in sustaining wealthier households. The median middle-class households and upper-middle-class households receive 88 percent and 95 percent of their income from wages, respectively. Wages contribute 45 percent of the median near-wealthy household's income, and just under one-quarter of the median wealthy households. Wealthier households earn money from a wider variety of sources. Just under one-third of wealthy households received income from at least four sources (among wages, proprietary businesses, financial proceeds, retirement pensions, government payments, rents, or royalties), while only 2 percent received income from only one source. Income streams tended to be less diversified among the near-wealthy, but their income still tended to be much more diversified than those in the middle class.

In comparison with the rest of the population, wealthier households receive much more money from proprietary businesses and financial investments, and they have much higher financial and business holdings. Strong business earnings suggest that much of the wealthier classes are composed of successful businesspeople. This does not imply that starting a business is a likely way to get rich. First, some selection effects are at work here. Proprietary business incomes have stagnated alongside wages over most of the income scale during the past 30 years,[18] but unsuccessful businesspeople quickly cease being business owners and get reabsorbed by the labor force. Second, some of these businesses are minority shares in a business in which they take a passive role; that is, they had money and then invested in the business, rather than starting a business and getting rich.

The wealthy have substantial financial holdings from which they receive considerable income. These holdings are certainly part of the reason that the wealthy have become wealthier. Financial markets have boomed over the past several decades, both relative to other asset classes and in comparison to financial investments in earlier eras. The wealthy have the resources to take part in these profits.

About 33 percent of households in this group receive government payments. This unexpectedly high incidence is due to the fact that wealthy people tend to be older, and this group collects Social Security payments. The median take from this source was $25,200, which is high compared to the amount received by poorer households. Social Security gives higher payments to those who earned more in their working years.

A Demographic Portrait of the Wealthy in the United States

The wealthy are disproportionately older, whiter, more educated, and more often married compared to other groups. Although most wealthy and near-wealthy households are headed by someone in their sixties or older, only minorities of people in their sixties or seventies are part of this group (the data suggest at most 3 percent for the former, and less than 7 percent for the latter). The wealthier classes may skew older for at least two reasons: they have had time to earn and accrue wealth, or they have reached an age in which family wealth is likely to have been passed on to them.

Many millionaires are likely late-career professionals or executive-level workers who earned enough to accrue into the low single-digit millions in net worth with their high incomes and accompanying latitude to save and invest money. Their ranks probably include many retired doctors, lawyers, dentists, engineers, small businesspeople, mid-level executives, and others who got educated, got and stayed married, saved regularly, and managed

their money reasonably well over a lifetime. The dominance of earned wealth among the ranks of the wealthy is probably truer of those with net worth in the single to tens of millions. As one moves higher up the ranks of the wealthy, inherited wealth becomes more prevalent.[19]

Thomas Piketty[20] suggests that the wealthy were more likely to maintain their position through inheritance before the 1950s. By 1950, the degree to which societal wealth was transferred across generations was falling in proportion to the total amount of household wealth accumulation, and it remained quite low during the 1960s and 1970s. In more recent decades, the concentration of wealth and the high returns to accrued assets relative to wages have likely bolstered intergenerational wealth transfers among the wealthy and pushed us back toward where we were before the 1950s.

Money is not the only resource transferred across generations. Noncash intergenerational transfers helped place today's and future wealthy people into a position to maintain their status. For example, this group enjoys high education levels, which may have been a function of their parent's ability to cover the costs of higher education or attain a foothold in better school districts. The wealthy are more likely to be homeowners and business owners, and much of this "earned" wealth may have been financed initially with parental aid. These forms of early-life help put young people in a position to begin accruing wealth early, which is important if someone of more modest means hopes to become a millionaire.

The Poor

Conceptually, the poor are distinguished by economic deprivation. They do not have enough money to secure the things they need. Deprivation is often described as being one of two types. In *relative deprivation*, people believe that, given their personal status or station in society, they ought to have access to particular goods and services. For example, it is relative deprivation if a person does not own a car but feels he ought to have a car by virtue of his age, background, or occupation. Relative deprivation exists where someone is not afforded access to a good, service, or right that is expected to be afforded to people of a particular status, ability, or ethic to which the deprived person self-identifies. In contrast, *absolute deprivation* occurs when someone lacks access to a good, service, or right that is necessary to meet some uncontroversial basic standard of living that transcends people's status or personal characteristics. This involves things presumed to be necessary to ensure survival, basic social integration, or minimal levels of well-being. Starvation is a form of absolute deprivation—all people undoubtedly need food, and, on the whole, society accepts the notion that no person should be hungry. Not having a car might be considered a form

of absolute deprivation for the 45 percent of Americans who have no access to public transit,[21] if we presume that all people should have some reliable conveyance to work, school, shopping, or healthcare. The key difference is that these types of needs associated with absolute deprivation are not seen as contingent on a person's status. These two different conceptions of deprivation play an important role in shaping public debates over how society should respond to people's money problems. Voters are more inclined to support fights against poverty in the form of absolute deprivation, but they are less inclined for poverty as relative deprivation.

Officially "Poor"

Conventionally, households are designated as "poor" if their gross income falls below the Census Bureau's or Department of Health and Human Services' poverty thresholds.[22] The official poverty line is society's most conventionalized method for differentiating society's poor from the nonpoor. These thresholds are used when discussing the poverty rate, a metric used to determine the prevalence of poverty in society. This measure is widely used by government programs to determine eligibility for public assistance. This line is also widely used by scholars in poverty research. The specific income level that one needs to earn to be considered "officially poor" changes from year to year, and it varies by the number of adults and children in a household.[23] In 2013, it ranged as follows: $11,534 for an elderly single-person household; $24,008 for a two-adult, two-child family; and $52,430 for the rare nine-adult household.

Despite its widespread use, the traditional poverty line is a crude measure. This line is calculated as three times the inflation-adjusted cost of what the U.S. Department of Agriculture estimated to be the cost of a minimum food diet in 1963.[24] The original poverty line in the United States was drawn roughly 50 years ago. At its drawing, it was presumed that one could sustain a minimally acceptable lifestyle on a pretax income that was three times the estimated market cost of what USDA officials deemed to be a modest food diet. After that threshold was set, the Bureau adjusted the figure annually according to the Consumer Price Index (CPI).

Are the "Poor" Really Poor?

The crudeness of the official poverty line has led some analysts to ask whether the "officially poor" are absolutely poor. Whether poverty is relative or absolute is important to debates about the state of household finances. If poverty is overwhelmingly relative and not absolute, then discussions about poverty primarily involve matters of distributional equality.

Distributional inequality does not imply that people are desperate. If a billionaire joins a community of 100 middle-class families, the community becomes very unequal even though no one has become poorer in an absolute sense. Some observers, such as the Heritage Foundation's Richard Rector, advance this type of assertion in noting that many of those who are officially poor enjoy a range of material comforts that were considered luxuries in previous generations, such as air conditioners, dishwashers, flat screen TVs, or video game consoles.[25] Obesity, not starvation, is the principle nutritional problem facing the poor. Many "poor" own their own home, and the average poor person has a home with more living space than the typical resident of Amsterdam or Paris.[26] Although situations of absolute deprivation do occur (e.g., homelessness or hunger), these situations tend to be temporary or transitional situations, rather than a permanent state of affairs.[27] Moreover, these estimates may ignore the effect that expansive social programs in the United States have on the incidence of genuine poverty.[28]

These observations evoke questions about whether people's money problems are indeed serious, as opposed to a matter of people simply wanting to enjoy a better lifestyle than their incomes permit. Opponents of progressive redistribution often ground their policy views on the belief that absolute poverty is a rarity in the United States, that U.S. living standards are in fact rising rapidly and across the board, and that most people's complaints about money involve poor personal financial management, "class envy," and a desire to raise their own living standards at the expense of society's "makers" (as opposed to "takers"). In many corners of public debate, concerns expressed about the economic problems faced by the poor and middle class are construed as being more a matter of frustrated lifestyle aspirations and less about the threat of real, serious economic deprivation.

In the next chapter, we probe household finance and cost-of-living data to explore questions about absolute deprivation's genuine extent, particularly given the existence of the U.S. social safety net. In the following section, we take this conventional poverty line as given, in part because this threshold is a useful dividing line that is used to discern who merits public assistance from those who do not. Next, we explore the details of this group's finances.

Poor People's Money

The median poor household earned $11,000 in 2013, and its "middle 50 percent" (those between 25th and 75th percentile incomes) earned between $8,000 and $15,000. This amounts to a monthly income of $666

to $1,250 per month. Despite any disagreements about whether the poverty line represents a precise dividing line between the economically desperate and not desperate, it seems likely that most readers would find it challenging to sustain what they would personally consider a basic livelihood on this income.

About two-thirds of these households received income from government payments. Just under half of this group received money from welfare programs (e.g., TANF or SNAP), about 30 percent from Social Security, and 15 percent from both welfare and Social Security. A smaller proportion received income from other programs, such as workers' compensation or unemployment insurance. Among those who received any payments, median receipts from government assistance were $8,360–$3,600 for welfare recipients and $8,520 for Social Security recipients. This suggests that about one-third of poor households receive no assistance.

The second most common source of income comes from employment wages. About 50 percent of poor households earned income from this source. Among all poor households that earned any wages, median earnings from this source was $9,600. This is equal to 1,280 hours of work at the federal minimum wage, or 32 weeks of full-time, 40 hour-per-week employment. These are the "working poor." Many of them are low-wage workers who experienced some employment or income disruption during the survey year. Others are elderly workers who work to bridge shortfalls in their public or private pensions. The data suggest that the poor are sometimes partly sustained by retirement pensions, financial income, or business income.

The poor generally have few assets, and the assets they do possess tend to be stored in one of three asset types: automobiles, cash accounts, and owned homes. About 70 percent of households in this group owned a cash account, 61 percent owned a vehicle, and 22 percent owned a home. Cars depreciate in value fairly quickly, and most retail cash accounts lose real purchasing power over time. Prevailing deposit rates have been lower than inflation for several years. The median vehicle owner's cars were valued at $7,200, and the median bank account holder had about $510 stored in cash or near-cash instruments. Both assets depreciate in value over time—vehicles lose value under any circumstances, and cash accounts do so when interest rates are lower than inflation. Combined with the fact that low-value homes are least likely to appreciate, this means that the poor's asset base stagnates (if it does not erode) over time, rather than appreciates.

Theoretically, the poor could help themselves by investing in higher-performing assets, such as stocks. This idea has motivated some policymakers to propose schemes that encourage financial investment among the

poor. For example, in 2015, the federal government launched the myRA program, a tax-sheltered, low-fee, small-denomination retirement program that was designed to encourage the poor to make more financial investments. In general, it is hard for the poor to "play the market" with banking and financial fees heavy on low-asset households. Many market schemes designed to help the poor invest are larded up with high fees, and, of course, this group does not have much money to invest in the first place. This last piece was a more critical flaw in this program, and similar ideas that investment promotion will help the poor. If a poor family were to put aside an extra $50 a month (a considerable part of their disposable income) for 30 years, the program's own estimates suggest that he or she would be left with a nest egg of just under $27,000—two years of poverty line income replacement. These schemes do not do much if social programs are not generous.

Note that the poor are less likely to be indebted, relative to the middle class. This low indebtedness is probably a matter of this group's poor access to credit. Lenders typically won't extend credit to this group, so this group tends not to borrow. Often, the credit that is available to the poor is extended on onerous terms. For example, credit markets make loans available to anyone who receives a regular paycheck through payday loans, whose interest costs can run into the hundreds or even thousands of percentage points on an annual basis. A 2012 analysis by the Pew Research Center suggests that about 8 percent of Americans earning below $15,000 per year use such loans, a rate that seems commensurate with the lower-middle class and middle-middle class (see the next section).[29] For the most part, the poor are comparatively less disposed to incur debts and are not particularly inclined to use the debt arrangements most available to them.

Profiling the Poor

Overall, the poor are more likely to be younger or older (not middle aged), single, less educated, nonwhite, and nonemployed. These are general demographic tendencies. The poor are more demographically diverse than these broad characterizations suggest.

About 20 percent of poor households are headed by someone who is disabled, and another 17 percent are headed by retirees. This group may face considerable obstacles to earning money through markets, generally receives few to no wages, and most of this group (well over 90 percent) receives government assistance. In addition to the fact that both groups almost universally receive government payments, public assistance through

the Social Security program is comparatively generous for these two groups. On average, members of these two groups receive around $9,300 in government assistance, which is about two to four times more than other poor groups. Of the various poor demographics profiled here, only retirees have a substantial proportion of group members with some accumulated wealth. The data suggest that 25 percent of poor retirees have $128,500 or more in net worth, often invested in homes. Overall, though, this group's access to accumulated wealth is limited.

Another 21 percent of this group is headed by single parents or guardians. This category includes households with nonmarried/cohabiting heads of household and at least one resident child. A large majority of this group (~86 percent) has low education levels (high school or less). Most of this group is young (median age is 37), but about 10 percent are headed by someone aged 57 or older. Over half of this group earned wages in 2013. Employment rates were higher in black and Hispanic single-parent households (61 percent and 65 percent, respectively) than in white households (53 percent). Despite higher employment rates, the median single-parent black household earned just over half the wages received by whites or Hispanics ($5,000 versus $9,000 and $9,700, respectively).

Another 12 percent of poor households are headed by the young, aged 25 or less. Employment is very high in this group (87 percent), but incomes tend to be low because their ability is adversely affected by weak job market conditions in the survey year, their lack of experience, and the more time demands of schooling. Forty-one percent of this group self-describes as students. About 23 percent of these youth-headed households have resident children.

These four groups—those headed by the disabled, retirees, single parents, and the young—represent about 70 percent of the country's poor households. The distinguishing characteristics of this group include low educational attainment (82 percent less than college), disproportionate joblessness (30 percent self-reported as unemployed), and disproportionate Hispanic representation (28 percent Hispanic vs. 48 percent white). About half of these households have resident children.

The Middle Class

When we remove the poor, the near-wealthy, and the wealthy, we are left with 82 percent of U.S. households representing the middle class. The defining feature of the middle class is that they are too wealthy to receive extensive help from the government, but they are not wealthy enough to be guaranteed a middle-class livelihood without the ability and opportunity

to maintain gainful work. This group can be understood as comprising three groups.

The Lower-Middle Class

Lower-middle-class households have incomes that lie between 100 percent and 200 percent of the poverty line. The median household in this group earns $23,000, and the middle 50 percent earns between $18,000 and $30,000. These incomes are generally sustained by a blend of wages, government assistance, and, to a lesser extent, pensions. Roughly 24 percent of U.S. households fall into this category.

As a group, they are not altogether different from the poor. Some analysts treat this group as the "near poor," and the fact that their incomes qualify them for a range of government payments and programs suggest that they are institutionally recognized as being in a financially precarious situation. Many of them could fall into official poverty were it not for their continuous employment, the continuity of their cohabitation arrangements, and, for retirees, their private pensions or Social Security payments (Social Security is not a means-tested program, which means rich and poor people get checks). Like the poor, many of those in the lower-middle class are heavily invested in their automobiles, although a larger proportion of this group owns their home than the poor.

About 28 percent of the lower-middle class is headed by someone older than 65. Although these households often do earn wage income, they more often are sustained by the Social Security program, which provides a median income of $13,200 to all senior-headed households in this class. For many elderly households, this public assistance program is sufficient to keep their household out of official poverty. Without the Social Security program, an estimated 59 percent of elderly lower-middle-class households would fall below the poverty line (see Chapter Three). Sometimes, this group supplements its income with modest private pension payments.

About 71 percent of the working-age lower-middle class (roughly half of the entire lower-middle class) earns enough money through wages to stay above the poverty line. This group includes many single-income families either because the household has only one adult head or one of its heads experienced unemployment. They tend to be less educated and thus earn less money when employed. This group also includes many single-income and highly educated households whose income was completely disrupted for some period during the year. This group can be considered the "working near-poor" and they effectively become the "working poor" in years where their income is interrupted by things such as a job loss or illness.

In general, this group has little accumulated wealth. Median net worth in this group is less than one year's poverty line income. The average household has more than one-third of its wealth stored in vehicles, which are nonperforming assets. Only about 23 percent own a home, and the median value of owned homes in this group was $120,000. Other assets are less widely held: 16 percent of them have any sheltered retirement savings, and 10 percent have any nonsheltered financial investments. The median household in this group has $600 in its bank accounts.

The Middle Class Proper

The middle-middle class includes the 30 percent of U.S. households earning between two and four times the poverty line. Median income is $45,000, and the middle 50 percent earns between $36,000 and $60,000. Median accumulated wealth is about $60,000, which is generally invested in a home. Aside from their cars and homes, this group tends not to accumulate much in the way of assets. About 43 percent have retirement accounts, and the median middle class retirement account has about $20,000 in holdings.

This group's demographic differs from that of the lower-middle class in several respects, particularly race, marriage/cohabitation, and full employment. As a whole, this group is not strikingly more educated than the lower-middle class (e.g., college attainment rates are roughly similar). This group's members are whiter, more likely to live as couples, and are more likely to have enjoyed uninterrupted employment. A household headed by the average, fully employed head is likely to fall here.

The Upper-Middle Class

In this book, households who earn more than 400 percent of poverty line income are designated as upper-middle income earners, but they lack sufficient wealth to be counted as wealthy or near wealthy. Younger members of this group seem well positioned to be wealthy with effective financial planning and the prevention of some major economic calamity. However, many members of this group are older and are struggling to establish a base of retirement assets that can work in conjunction with government payments programs such as Medicare and Social Security to render a reasonably comfortable retirement. Roughly 30 percent of U.S. households fall into this upper-middle class.

The members of the upper-middle class earn several times more than poor households and often accumulate some wealth over their lifetimes. This

group is disproportionately white, middle aged, educated, married, and employed. It might include couples who are college-educated and reasonably well employed or later-career workers whose pay has risen over time. The median household in this group earns $100,000, and the middle 50 percent earn between $74,000 and $142,000. This income generally comes from wages.

Like the rest of the middle class, the upper-middle class is largely invested in their homes. Home ownership is high in this group (82 percent), and the median value of an owned home is $230,000. Members of this group are more likely to have other kinds of assets, and the value of these assets tend to be larger than that of other members of the middle class, but the degree to which these households are well diversified and wealthy should not be exaggerated. The median household in this group has no nonsheltered financial investments and about $28,000 in retirement accounts. Only about 68 percent of households in this category have any retirement savings, and the median account has about $75,000 in it, which is roughly six years of poverty-line income. The median household has about $12,000 in liquid holdings.

This group pays more taxes than other members of the middle class and tends to receive less direct government aid over their working years. However, this group does enjoy high public retirement benefits, and they benefit from several government programs that are designed to help them accumulate net worth.

Conclusion

This chapter presents an overview of U.S. household finances. We tend to interpret personal finance issues by using our personal situation as a baseline comparison. The problem is that we have limited exposure to people in substantially different economic circumstances from our own. By sharpening our understanding of the variety of economic situations in which other Americans operate, we have a better cognizance of our own economic situation and how household finances differ on the rungs above and below us.

The data suggest that somewhere somewhat less than one-tenth of society has considerable accrued wealth, such that they would be able to live a livelihood similar to that enjoyed (or endured) by a plurality of Americans without ever having to work again. In many respects, their financial problems seem more likely to be a product of lifestyle expectations or, as we will see later, attempts to secure a position for their children in the upper ranks of society during a period in which economic mobility is low and inequality

is rising. This top 10 percent is more likely to be headed by older, college-educated, married whites, although other demographics are represented in this group.

At the other end of the economic hierarchy, there are society's poor, a group primarily composed of the very young, very poor, uneducated, nonwhites, Hispanics, and single parents. The economic situation of these groups is far inferior to the upper class and even middle class, although there is some debate about whether the deprivation experienced by this group is relative or absolute (a theme we will pursue later). This group roughly comprises one-seventh of society, and their situation is not altogether different from another 23 percent or so of society that is part of the lower-middle class. In many respects, having the good fortune of not losing work, experiencing a health condition, or running into some other economic misfortune separates the poor and lower-middle class. In any case, together these two groups comprise about 40 percent of U.S. society.

The remaining 50 percent of society is the middle class. They can be divided into two groups. The upper-middle class tends to be whiter, middle-aged, better educated, and married/cohabiting, all of which translates into better employment opportunities, higher income, and ultimately more opportunity to accumulate wealth. The middle-middle class is highly employed, like the upper-middle class, but they tend to have less education, more nonwhites or Hispanics, and more single people.

These are the various perches through which we can view the issue of household finances. Knowing where we sit on the economic pyramid provides a sense of whether the mental baseline presented by our own financial circumstances is more typical or outlying relative to the rest of the country.

The audience for an academic book on household finances likely skews educated and, as a group, is probably wealthier and earns more money than the general population. Readers can easily cross-reference their personal circumstances with the population at large. While most of us consider our situation to by typical or middling, it is probably "typical" for our social milieu in a society that is highly segregated economically. Much of the country feels like it is struggling financially, and it can be instructive to see how others do so with fewer resources at their disposal.

As noted in the preceding discussion about the poor, there are many observers who question whether or not those who sit at lower stations in the economic hierarchy are really struggling with serious economic adversity. Are the middle and lower classes struggling with serious money problems? We turn to this issue next.

34. Pew Research Center. (2010, May 4). "Socialism" not so negative, "capitalism" not so positive. Retrieved from http://www.people-press.org/files/legacy-pdf/610.pdf

35. Jacove, D. (2013). One in three Americans prepare a detailed households budget. Retrieved from http://www.gallup.com/poll/162872/one-three-americans-prepare-detailed-household-budget.aspx

36. Hastings, J., Madrian, B. C., & Skimmyhorn, W. L. (2013). Financial literacy, financial education, and economic outcomes. *Annual Review of Economics*, 5, 347–373; Lusardi, A., & Mitchell, O. S. (2014). The economic importance of financial literacy: Theory and evidence. *Journal of Economic Literature, 52*(1), 5–44.

37. For reviews, see Harvey, D. (2007). *A brief history of neoliberalism*. New York, NY: Oxford University Press; Centeno, M., & Cohen, J. N. (2010). *Global capitalism: A sociological perspective*. Cambridge, UK: Polity; Centeno, M., & Cohen, J. N. (2012). The arc of neoliberalism. *Annual Review of Sociology*, 38, 317–340; Peck, J. (2013). *Constructions of neoliberal reason* (New York, NY: Oxford University Press).

Chapter 2

1. Morin, R. & Motel, S. (2012, September 10). A third of Americans now say they are in the lower classes. Retrieved from http://www.pewsocialtrends.org/2012/09/10/a-third-of-americans-now-say-they-are-in-the-lower-classes/

2. U.S. Federal Reserve. (2014). *Survey of consumer finances*. Retrieved from http://www.federalreserve.gov/econresdata/scf/scfindex.htm

3. This figure and those that follow are derived from data from the Federal Reserve Bank's *Survey of Consumer Finances*. It is a different source than that used by the Census Bureau in its income calculations from Chapter One. Measurement and estimation mean that our analyses are dealing with gross, rather than fine, differences. Readers should assign less importance to distinctions amounting to a few hundred or even thousands of dollars. More meaning can be drawn from distinctions involving greater sums, for example in the tens of thousands of dollars.

4. Cohen, J. N. (2016, September 14). Family businesses: In decline? [Blog post]. Retrieved from http://fragilefinances.org/2016/09/14/family-business-decline

5. Cohen, J. N. (2016, August 31). Household income sources: Who gets welfare? [Blog post]. Retrieved from http://fragilefinances.org/2016/08/31/household-income-sources

6. Cohen, J. N. (2016, September 14). Who pays the federal government's bills? [Blog post]. Retrieved from http://fragilefinances.org/2016/09/14/who-pays-the-federal-governments-bills

7. Federal Reserve Board. (2015, December 28). Household debt service and financial obligations ratios [Data table]. Retrieved from http://www.federalreserve.gov/releases/housedebt

8. U.S. Federal Reserve. (2014). *Survey of consumer finances*. Retrieved from http://www.federalreserve.gov/econresdata/scf/scfindex.htm

9. A regression analysis is a statistical method for building predictive or explanatory models. It delivers formula used to predict variable values using other metrics ("predictors").

10. Piketty, T. (2014). *Capital in the twenty-first century*. Princeton, NJ: Belknap.

11. Seitz-Wald, A. (2011, September 19). Multi-millionaire rep. says he can't afford a tax hike because he only has $400k a year after feeding family [Blog post]. Retrieved from http://thinkprogress.org/economy/2011/09/19/322405/gop-rep-whines-400k

12. In financial parlance, we are pricing out a *perpetuity*, that is, a bond or security that is supposed to pay out forever. Such securities exist, although they are very rare. For example, the United Kingdom issued such bonds during World War I. Such bonds were retired by acts of British Parliament only recently. See Kollewe, J., & Farrell, S. (2014, October 31). UK bonds that financed First World War to be redeemed 100 years later. *Guardian*. Retrieved from http://www.theguardian.com/business/2014/oct/31/uk-first-world-war-bonds-redeemed

These types of securities are priced as

$$PV = \frac{A}{r}$$

where PV is the present-day value of the security, A is the periodic payout of the security, and r is the interest rate associated with the security.

13. In this exercise, we presume a perpetual income of $45,000 in 2013 dollars for the near-wealthy and $90,000 for the wealthy.

14. Our assumptions are to treat T-bills as cash equivalents, for example, if they were laddered. We treat Treasury bonds as an ultraconservative allocation of debt investments, and we consider the S&P 500 index as a reasonably conservative allocation of equity investments (the index is mostly composed of large, blue-chip firms).

15. Morningstar Investor Services. (2010). *Mutual fund portfolio allocation*. Retrieved from https://corporate.morningstar.com/us/documents/MarketingOneSheets/ADV_MPF_MutualFundPortfolioMap.pdf

16. Mean returns reported in this section were calculated using data inflation from Reinhardt, C., & Rogoff, K. (2011). From financial crisis to debt crisis. *American Economic Review, 101*(5), 1676–1706; and Damodara, A. (2015). Annual returns on stock, T.bonds and T.bills: 1928–current [Data table]. Retrieved from http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/histretSP.html

17. Of course, averages don't mean that someone will get these returns every year. There will be good years and bad years. For example, income investments did better in the 1990s and early 2000s than today. The good years are expected to be ones in which people save in anticipation of the bad ones.

18. Cohen, J. N. (2016, February 18). Family businesses: In decline? [Blog post]. Retrieved from http://fragilefinances.org/2016/02/18/family-business-decline

19. A rather colorful report by United for a Fair Economy suggests that about 21 percent of those in the 2012 *Forbes 500* richest Americans earned enough

wealth to rank in this group. An estimated 35 percent came from solidly middle-class or lower-class backgrounds, while the remainder enjoyed capital and opportunities from varying degrees of family affluence.

20. Piketty, T. (2014). *Capital in the twenty-first century*. Princeton, NJ: Belknap.

21. American Society of Civil Engineers. (2013). *2013 report card for America's infrastructure*. Retrieved from http://www.infrastructurereportcard.org/transit

22. The latter is a simplified version of the former. See Census Bureau. (2014). Poverty thresholds. Available for download at http://www.census.gov/data/tables/time-series/demo/income-poverty/historical-poverty-thresholds.html; Department of Health and Human Services. (2013). 2013 poverty guidelines. Retrieved from http://aspe.hhs.gov/poverty/13poverty.cfm

23. Along with consideration of the household head's age in single and two-person households, and special provisions for a higher poverty line in Hawaii and Alaska.

24. Short, K. (2014, October). *The supplemental poverty measure: 2013*. Current Population Reports. Retrieved from http://www.census.gov/content/dam/Census/library/publications/2014/demo/p60-251.pdf

25. Rector, R., & Sheffield, R. (2011). Understanding poverty in the United States: Surprising facts about America's poor. *Heritage Foundation Backgrounder #2607*. Retrieved from http://www.heritage.org/research/reports/2011/09/understanding-poverty-in-the-united-states-surprising-facts-about-americas-poor

26. Rector, R., & Sheffield, R. (2011). Understanding poverty in the United States: Surprising facts about America's poor. *Heritage Foundation Backgrounder #2607*. Retrieved from http://www.heritage.org/research/reports/2011/09/understanding-poverty-in-the-united-states-surprising-facts-about-americas-poor

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28. Short, K. (2014, October). *The supplemental poverty measure: 2013*. Current Population Reports. Retrieved from http://www.census.gov/content/dam/Census/library/publications/2014/demo/p60-251.pdf

29. Pew Charitable Trusts. (2012). *Payday lending in America: Who borrows, where they borrow, and why*. Retrieved from http://www.pewtrusts.org/en/research-and-analysis/collections/2014/12/payday-lending-in-america

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1. Salkin, A. (2009, February 6). You try to live on 500k in this town. *New York Times*. Retrieved from http://www.nytimes.com/2009/02/08/fashion/08halfmill.htm

2. For example, see Jones, R. P., Cox, D., & Navarro-Rivera, J. (2014). *Economic insecurity, rising inequality, and doubts about the future: Findings from the 2014 American values survey*. Washington, D.C.: Public Religion Research Institute. Retrieved from http://publicreligion.org/site/wp-content/uploads/2014/09/AVS-web.pdf; Financial Investor Education Foundation. (2013). Financial capability in the