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The Potential of Savings Accounts to Protect Young Adults from Unsecured Debt

INTRODUCTION

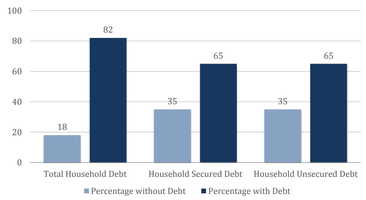
- Mounting debt can limit young people's chances for economic mobility. From this perspective, debt can be considered a "double-edged sword."[1] n some cases, debt can be used in productive ways that might promote economic mobility .[2] In other cases, debt can act unproductively as a drain on resources.[3]
- Secured debt's collateralized nature allows borrowers to leverage existing assets and bend credit markets to their advantage,[4] making it productive for economic mobility.
- Borrowers of unsecured, uncollateralized debt have not leveraged existing assets, and their use of credit markets is riskier;[5] as such, unsecured debt may be unproductive for economic mobility.
- One strategy for helping young adults decrease their reliance on unproductive debt may be ownership or acquisition of a savings account.[6] Just as a savings account serves as a gateway to building the asset side of young Americans' balance sheets, a savings account may also be related to the debt side of their balance sheets

AIMS

- Does ownership or acquisition of a savings account facilitate the acquisition and accumulation of young adult households' secured debt?
- Does ownership or acquisition of a savings account protect against the acquisition and accumulation of their unsecured debt?
- How do young adults' age, education level, and earned income interact with a savings account to produce these effects?

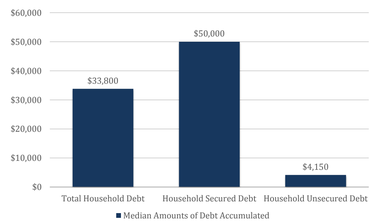
Tables 1 & 2: Young Adult Households' Debt

Table 1: Percentages of Young Adult Households with and without Types of Debt



Source: Data from the 1996 Survey of Income and Program Participation (SIPP), includes all households with young adult heads ages 18 to 40, *N* = 43,455.

Table 2: Median Amounts Accumulated among Young Adult Households with Debt



Source: Data from the 1996 Survey of Income and Program Participation (SIPP), includes median amounts only for young adult households with debt (Total household debt *n* = 35,654; Household secured debt *n* = 28,444; Household unsecured debt *n* = 28,243).

METHODS

- This study used a sample of 43,455 young adults ages 18 to 40 from the 1996 panel of the Survey of Income and Program Participation (SIPP).
- Young adults were asked about their debts, including mortgages, businesses, real estate, vehicles, credit cards, unsecured loans, and outstanding bills. Total, secured, and unsecured debt amounts were windsorized at their 99th percentiles and log transformed.
- To model the acquisition of a savings account, young adults' account ownership was tracked to determine whether or not, and when, they acquired or closed a savings account using retrospective, quarterly histories tracked over one previous calendar year.
- Given that home ownership was likely a driver of and endogenous to young adult households' debt accumulation, home ownership was also tracked quarterly to determine whether or not, and when, young adult households purchased or sold a home—capturing dynamic changes in home ownership.
- Eleven variables were included as controls in the analyses, including age, gender, race, marital status, college enrollment, education level, employment, quarterly earned income, family household type, new head of household, and geographic region.

Figure 1: Savings Account Acquisition by Age

About half of young adults owned a savings account (46%) and a smaller percentage (4%) acquired an account during the panel. In the analysis, young adults' account ownership, acquisition, and closure were compared to no savings account ownership.

Source: Data from the 1996 Survey of Income and Program Participation (SIPP), includes all households with young adult heads ages 18 to 40, *N* = 43,455.

- The data was analyzed using Cragg's double-hurdle models with and without interaction effects.[7] This analytic approach was ideal because it assumed that the extent to which households were leveraged varied among those that used debt and may have been unrelated to their preference to avoid or inability to access debt.
- Average partial effects (APEs) were estimated to provide assessments of the additional debt accumulated for each year of age, level of education, and $1,000 in quarterly earned income. Standard errors for APEs were produced by bootstrapping at 250 replications.[8]

Table 3: Predicting Household Secured Debt with Cragg's Double-Hurdle Models

	Probability of Acquiring Secured Household Debt (*n* = 43,455)	Value of Accumulated Secured Household Debt (*n* = 28,444)
Age	–.008*** (.002)	–.007*** (.002)
Female	–.008 (.020)	–.010 (.017)
New head of household	–.003 (.029)	–.009 (.030)
Education level (Reference: Less than high school degree)		
College degree or more	.319*** (.035)	.506*** (.039)
Some college	.401*** (.032)	.309*** (.038)
High school degree	.265*** (.032)	.152*** (.039)
Household quarterly earned income / 1000	.098*** (.008)	.087*** (.010)
Home ownership (Reference: No home ownership)		
Owned a home	1.291*** (.021)	1.988*** (.021)
Purchased a home	1.331*** (.043)	2.099*** (.029)
Sold a home	.105** (.034)	.194*** (.042)
Savings account (Reference: No savings account ownership)		
Savings account ownership	.236*** (.021)	.150*** (.018)
Savings account acquisition	.160*** (.037)	.037 (.035)
Savings account closure	.216*** (.036)	.106** (.034)

Source: Data from the 1996 SIPP, accounting for individual-level clustering.
Notes. There were 15,011 young adult households that did not accumulate any secured debt and 28,444 that accumulated secured greater than $0. Only selected variables are presented here in order to conserve space. Full results are presented in the paper, which is available upon request.
β = regression coefficient; SE = Robust standard error. ***$p < 0.001$, **$p < 0.01$, *$p < 0.05$

RESULTS

- While a savings account was related to more accumulated debt overall, the type of debt accumulated was less risky and potentially more productive.
- Owning a savings account was associated with a 15% increase, or $7,500, in the value of secured debt.
- Owning a savings account was associated with a 14% decrease, or $581, in the value of unsecured debt.
- Age was negatively related to debt acquisition; for the most part, older young adults were less likely to acquire and accumulate debt. Young adults accumulated almost 2% less total debt and almost 3% less unsecured debt for each additional year of age.
- Young adults acquired and accumulated more debt as they achieved higher levels of education. Young adults accumulated about 56% more total household debt, 34% more secured debt, and 53% more unsecured debt with each additional level of education.
- Young adults accumulated about 25% more total household debt, 30% more secured debt, and 11% more unsecured debt with each additional $1,000 in earned income.
- Large gains in accumulated secured debt were observed as households earned more income, while accumulated unsecured debt remained mostly flat. In other words, there was a bifurcation in the borrowing system that steered higher-income young adults toward secured, productive debt and lower-income young adults toward unsecured, unproductive debt.

Table 4: Predicting Household Unsecured Debt, with Cragg's Double-Hurdle Models

	Probability of Acquiring Unsecured Household Debt (*n* = 43,455)	Value of Accumulated Unsecured Household Debt (*n* = 28,243)
Age	–.009*** (.002)	–.003 (.002)
Female	.055** (.002)	–.035 (.002)
New head of household	–.074** (.029)	–.054 (.036)
Education level (Reference: Less than high school degree)		
College degree or more	.445*** (.032)	.828*** (.045)
Some college	.567*** (.028)	.530*** (.042)
High school degree	.362*** (.027)	.358*** (.042)
Household quarterly earned income / 1000	.028*** (.006)	.049*** (.010)
Home ownership (Reference: No home ownership)		
Owned a home	.083*** (.020)	–.077** (.025)
Purchased a home	.146*** (.034)	.059 (.043)
Sold a home	.030 (.033)	–.018 (.047)
Savings account (Reference: No savings account ownership)		
Savings account ownership	.211*** (.018)	–.136*** (.024)
Savings account acquisition	.295*** (.034)	–.028 (.044)
Savings account closure	.240*** (.033)	–.015 (.041)

Source: Data from the 1996 SIPP, accounting for individual-level clustering.
Notes. There were 15,212 young adult households that did not accumulate any unsecured debt and 28,243 that accumulated unsecured greater than $0. Only selected variables are presented here in order to conserve space. Full results are presented in the paper, which is available upon request.
β = regression coefficient; SE = Robust standard error. ***$p < 0.001$, **$p < 0.01$, *$p < 0.05$

CONCLUDING IMPLICATIONS

- In the midst of public discussions about young adults' indebtedness and the problems it can create for building healthy balance sheets, our findings demonstrate that a savings account—a simple financial tool—can be a potentially powerful solution. Thus, a savings account may help young adults "invest in their debt," serving as a gateway to better, healthier credit markets and protecting them from riskier ones.
- Minimizing unsecured, unproductive debt is an obvious policy intervention which would benefit young adults' balance sheets and allow them to begin building toward a strong financial future. Like the historic wealth transfers made available by the Homestead Act of 1862, perhaps the equivalent policy intervention for the 21st century is one that invests in young adults' debt to stabilize their financial health and catalyze them toward economic mobility.

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