# Discussion: Sergeyev, Lian and Gorodnichenko (2024) – The Economics of Financial Stress

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# Key take-aways

- financial stress has important effects on individuals' economic decisions
  - labor supply
  - consumption/savings
- financial stress has very different effects on sophisticated vs. naive people
  - "sophisticates" save extra to stay away from financial constraint
  - "naifs" fall into a poverty trap (= still dissaving close to constraint)
- more people are naive than sophisticated $\rightarrow$ macroeconomically important
- a great paper on a highly relevant topic – and food for thought!

# Measuring financial constraints

- Question: "If your household experienced an unexpected emergency, would you need to borrow money in order to pay for a \$2,000 expense?"
- Answers:
  - "no need to borrow": 46.2%
  - "need to borrow": 44%
  - "cannot pay": 9.8%

$\rightarrow$ $\sim$ 54% at least somewhat constrained

| | median | % $<$ 2000 USD |
|---|---|---|
| liquid assets (2022 SCF) | 7850 | 28.7 |
| financial assets (2022 SCF) | 36810 | 20.4 |
| net financial assets (2022 SCF) | 16850 | 38.8 |
| net financial assets (SLG) | 5000 | ? |

# Measuring financial constraints

- households might perceive themselves as more constrained than they are (perhaps due to mental accounting / narrow bracketing?)
- model: financial stress function $\Theta(a)$ directly depends on assets $a$
- Could there be a systematic perception bias? Households who worry more about their finances might also be more inclined to say they cannot cover an emergency expense.
- survey conducted in April-May 2022: peak of US inflation, Ukraine war recently broke out – potentially lower "baseline level" of financial stress at other times?

$\rightarrow$ might be interesting to study other countries and points in time

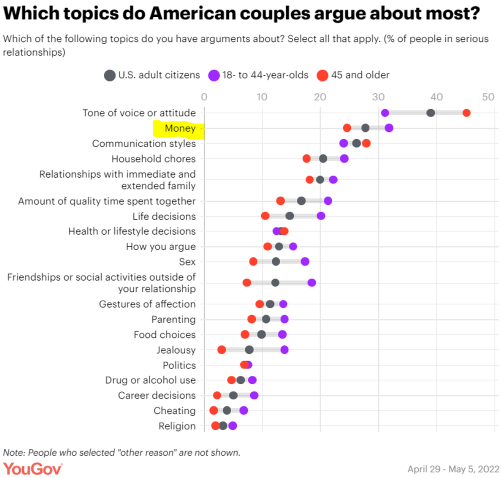
$\rightarrow$ could link survey to admin data to get more comprehensive (and not self-reported) picture of relationship between worries and actual financial situation

# Life cycle

- data suggest inverse U-shape of financial worries, with peak at around 50 years
  - What drives this? College entry of children?
  - Is this pattern similar in other countries?
- both financial worries and actual financial constraints vary across the life cycle (e.g., Schlafmann et al. 2024) $\rightarrow$ could model life cycle dimension to see how these factors interact and shape individuals' behavior at different points in their lives
- model focuses on "prime-age", employed workers $\rightarrow$ How does financial stress affect the elderly and unemployed?

# Households and risk

- model assumes unitary households
- finances are among top reasons for arguments in relationships



# Households and risk

- How does financial stress affect household formation and stability?
- Can within-household insurance mitigate financial stress?
- Do labor market supply effects of financial stress differ between men and women?
- model features only risk-free assets $\rightarrow$ How does financial stress affect portfolio choice (and vice versa)?

# Policy

- model suggests substantial welfare losses, especially for naive individuals
- naivety is common: estimate of around 2/3
- Can we educate people to become more sophisticated? $\rightarrow$ RCT with information treatment?
- Which policies might help people to avoid falling into a poverty trap due to naivety about financial stress?
- paper shows importance of financial stress for fiscal policy transmission: lump-sum fiscal transfers can relieve financial stress, increasing labor supply and output
  - Might targeted transfers be even more efficient?
  - How does it affect monetary policy transmission?

Thank you!

# Literature

Schlafmann, K., O. Setty, and R. Vestman (2024): "Designing Pension Plans According to Consumption-Savings Theory," *Review of Financial Studies (forthcoming)*.