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## 20 Coping with risks during the Great Recession

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- ▶ The aggregate proportion of 50+ households in financial distress has been stable between 2011 and 2013 but individual circumstances have changed for many households
  - ▶ Financial assets have been used as a buffer, in particular by low income households hit by health shocks
  - ▶ Greater social inclusion, proxied by the size of the social network, reduces the probability of falling into financial distress
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### 20.1 The protective role of assets and social networks during the crisis

According to a recent report (OECD 2013), the current economic crisis has severely hit the OECD area, which has registered, as a whole, a decline by almost 2.5 per cent of the real GDP per capita per year. Even if between 2010 and 2011 the same aggregate measure has increased by one per cent, economic recovery is still feeble, especially in some countries.

Among OECD countries, in fact, the effects of the Great Recession have differed both in terms of timing and magnitude: overall, since 2008, the largest declines in real household disposable incomes have been registered in Southern European countries, such as Spain and Italy.

The persistence of adverse economic conditions has jeopardised the ability of many households to cope with negative shocks. In a majority of OECD countries, though, lower-income older people did relatively well thanks to the role played by the pension system (OECD 2014).

In this chapter we investigate the role played by assets to support the living standard of the (more affluent) older population. We analyse whether and how those households who were financially distressed in Wave 4 coped with their financial problems by liquidating their assets, real and financial, between Waves 4 and 5. We also focus on the role of social networks, as providers of informal support, in preventing or escaping financial distress. In our analysis we consider having a large social network an indicator of higher social inclusion.

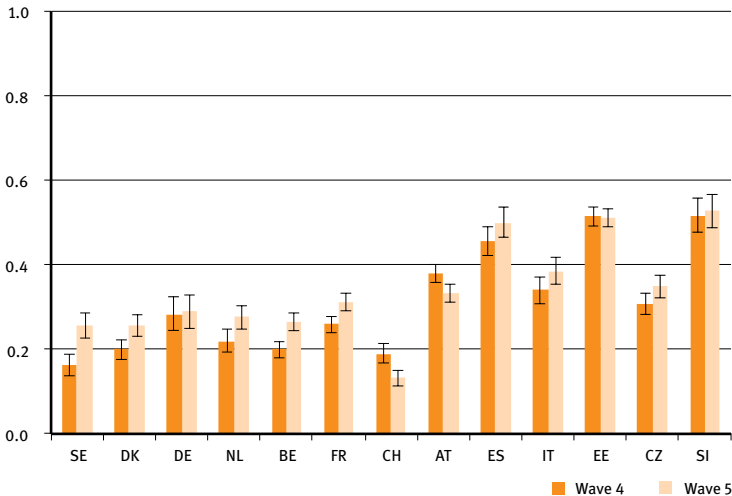
The chapter is organised as follows. We first analyse which characteristics trigger financial distress in Wave 5 – conditional on being not financially dis-

tressed in Wave 4 – or help escape it. We then focus on assets liquidation, and investigate whether financially distressed households in Wave 4 are more likely to sell their house, their financial or other real assets between Waves 4 and 5.

## 20.2 Transitions into and out of financial distress

In order to understand transitions into and out of financial distress, we select households belonging to the longitudinal sample, that we observe in Waves 4 and 5 with no missing information regarding household income and financial wealth. Financial distress is defined as in Cavasso and Weber (2013) where the household is considered financially distressed if two conditions are met: (1) financial wealth, net of non-mortgage debt, is less than three months' income and (2) household equivalent income is not in the top third of the country specific distribution.

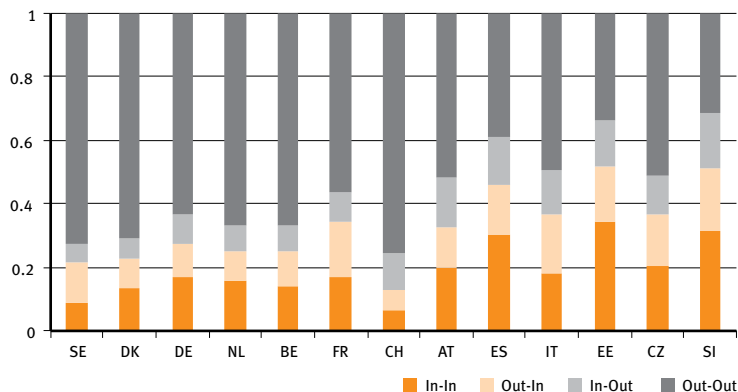
In Figure 20.1 we report the fraction of households in financial distress by country and wave: differently from what Cavasso and Weber (2013) find when looking at transitions between Waves 2 and 4 for 65+ individuals, we notice that the proportion of financially distressed households does not change dramatically between Waves 4 and 5. In fact, it is rather stable in all countries except Sweden, Denmark, the Netherlands, Belgium and France (where it increases), and Switzerland and Austria (where it decreases).



**Figure 20.1:** Fraction of households in financial distress – longitudinal sample, Wave 4 and Wave 5

Notes: 15,645 observations

Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0



**Figure 20.2:** Transitions in and out financial distress between Wave 4 and Wave 5

Notes: 15,645 observations

Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

Even if the fraction has remained generally stable between waves, we can see from Figure 20.2 that there has been reshuffling of households between the financially distressed or non-distressed groups.

We estimate transition probabilities in and out of financial distress as a function of demographics, health, homeownership and household income. In addition we consider also participation in financial markets and the size of social network (standardized with respect to country means). The last variable should capture the role of informal support in preventing or escaping financial distress.

We report in Table 20.1, column (1), probit estimates when the outcome is the probability of falling into financial distress in Wave 5, given that the household was not in financial distress in Wave 4. We estimate a protective role of education, employment, income, and homeownership. We also find that greater social inclusion, proxied by the size of the social network in Wave 4, significantly reduces the probability of entering financial distress.

Participation in the financial market and better health conditions in Wave 4 are also associated to a lower probability of falling into financial distress in Wave 5. The same table reports, in column (2), estimates for the probability of leaving financial distress by Wave 5, given that the household was in financial distress in Wave 4. We find that income, homeownership and financial market participation help recover from financial distress. We do not find statistically significant effects for the size of social network.

**Table 20.1:** Probit estimates for transition probabilities in and out of financial distress, Wave 4 and Wave 5

Variables	(1) IN		(2) OUT	
	Marginal effects	Standard error	Marginal effects	Standard error
Female	0.034***	(0.008)	-0.016	(0.015)
Foreign	0.071***	(0.013)	-0.101***	(0.021)
Education (ISCED 0-2)	0.128***	(0.011)	-0.127***	(0.022)
Education (ISCED 3-4)	0.081***	(0.010)	-0.100***	(0.022)
Employed	-0.069***	(0.013)	0.191***	(0.023)
Retired	0.003	(0.013)	0.034	(0.021)
Age	-0.013*	(0.005)	0.006	(0.009)
Age squared	0.007	(0.004)	-0.001	(0.006)
Partner	-0.013	(0.009)	0.077***	(0.017)
Household size	0.004	(0.005)	-0.010	(0.008)
Poor health	0.079***	(0.014)	-0.066***	(0.020)
HH equiv. income (log)	-0.030***	(0.004)	0.017**	(0.006)
Homeowner	-0.067***	(0.009)	0.103***	(0.015)
Financial market part.	-0.079***	(0.009)	0.060***	(0.018)
Social network size	-0.013***	(0.004)	0.001	(0.007)
N. Obs.	10,627		4,718	
Pseudo R-squared	0.1090		0.0676	

Significance: \*\*\* = 1%; \*\* = 5%; \* = 10%

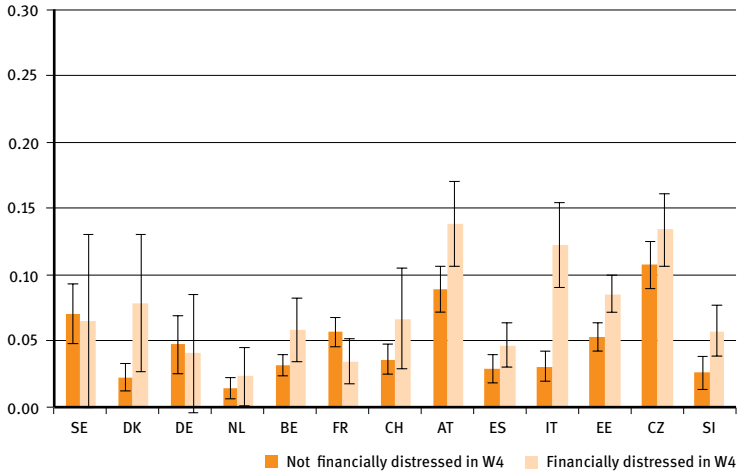
Notes: Controlled for country dummies. Employment status, age, having a partner, household size, poor health, income, homeownership, financial market participation and social network size are relative to Wave 4

Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

## 20.3 Assets liquidation: housing, real and financial assets

We now turn to assets liquidation as a strategy to cope with negative shocks.

We focus on financial assets (including bonds, stocks, mutual funds, individual retirement accounts, contractual saving and life insurance policies, but excluding cash and deposit accounts), home (the main residence), and other real assets (including secondary dwellings, investment homes, other real estate, cars and own business).



**Figure 20.3:** Liquidation of the main residence, by financial distress in Wave 4

Notes: 18,869 observations

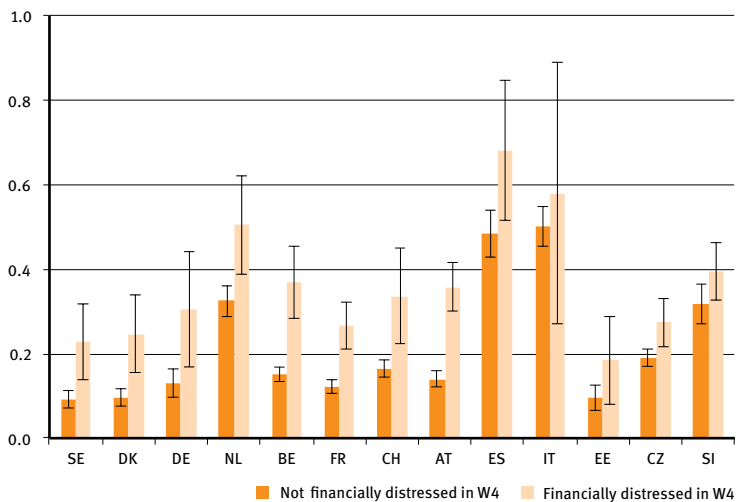
Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

We investigate whether households, who were financially distressed in Wave 4, liquidated their assets, real or financial, between Waves 4 and 5. We analyse separately cases in which a household owned a particular asset in Wave 4 and sold it between waves. Our outcomes therefore will be the liquidation of each group of assets separately, conditional on possessing them in Wave 4. By liquidation we mean the complete sale of a certain asset category, so that the outcome is a binary variable denoting the change in ownership. This definition ruled out changes in asset value due to its partial sale or to price variations. Our analysis provides descriptive evidence about important decisions, such as leaving the financial market, selling the main residence or other real assets, that can be adopted in the face of a reduction in available resources and lack of support.

In Figure 20.3 we show the fraction of individuals who owned their home in Wave 4 and sold it between waves by country and financial distress in Wave 4. We can see generally low percentages of households who sold between waves. Statistically significant differences between financially distressed households and those who are not in financial distress can be noticed only in Austria, Italy, Estonia and Slovenia.

Figure 20.4 instead shows the fraction of households who owned financial assets in Wave 4 and sold them entirely between waves. Compared to the previous figure, we can see that much higher proportions of households liquidated this type of asset. Also, the figure suggests that financially distressed households

were more likely to liquidate all financial assets between waves compared to not financially distressed households, except in few countries (where confidence intervals overlap).



**Figure 20.4:** Liquidation of financial assets, by financial distress in Wave 4

Notes: 12,985 observations

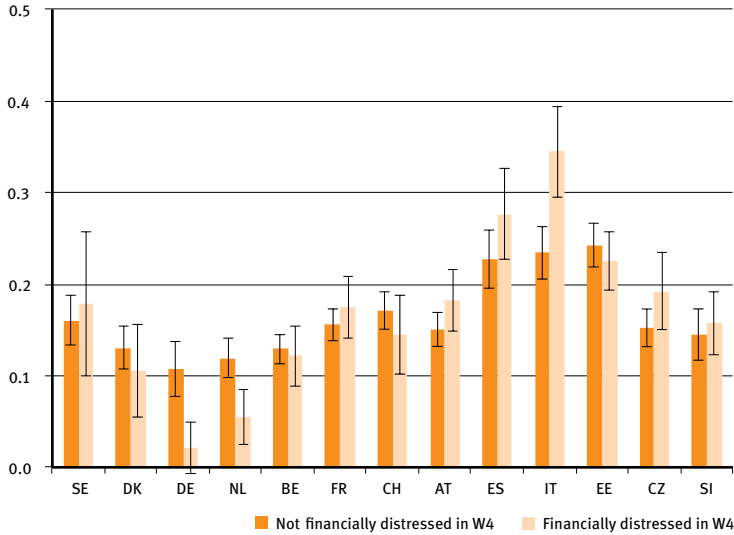
Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

Finally Figure 20.5 shows the fraction of households who owned other real assets, such as secondary or investment homes, other real estate, cars and own business, in Wave 4 and sold them entirely or partly between Waves 4 and 5. The fraction of households who sold this type of assets between waves is in general somewhere in between the previous two cases.

In Table 20.2 we report probit estimates for the probability of liquidating all assets (column 1), financial assets (column 2) or other real assets (column 3).

Estimates show that being in financial distress in Wave 4 is associated to a higher probability of liquidating assets, especially financial assets. The size of the social network plays a (significantly) protective role, particularly when we consider the probability of financial assets liquidation. The newly retired, as expected, are more likely to liquidate assets; bad shocks, such as health worsening or drops in the household size, are also predictive of asset liquidation. Being female or having low education is associated to a higher probability of liquidating assets, especially financial assets. The sale of the main residence, not shown in the table for the sake of brevity, is associated mainly to changes in the family size. This may reflect the reluctance to sell the main residence but may also signal

high transaction costs associated to the downsizing of housing equity (Angelini et al. 2014). The liquidation of other real assets, that increases with age and is positively correlated to household size drops, seems to be linked more to a rebalancing of household portfolios or to the desire to transfer wealth to the offspring, rather than to a situation of financial difficulty.



**Figure 20.5:** Liquidation of other real assets, by financial distress in Wave 4

Notes: 19,035 observations

Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

**Table 20.2:** Probit estimates of assets liquidation between W4 and W5

Variables	(1) All assets		(2) Financial assets		(3) Other real assets	
	Marginal effects	Standard error	Marginal effects	Standard error	Marginal effects	Standard error
Financial distress	0.036***	(0.008)	0.088***	(0.010)	0.008	(0.007)
Female	0.019**	(0.006)	0.027***	(0.007)	0.012*	(0.006)
Foreign	0.013	(0.011)	0.035**	(0.013)	-0.002	(0.010)
Education (ISCED 0-2)	0.073***	(0.009)	0.078***	(0.010)	0.014	(0.008)
Education (ISCED 3-4)	0.038***	(0.008)	0.041***	(0.009)	0.009	(0.007)
Employed	0.003	(0.010)	-0.036**	(0.012)	0.034***	(0.010)
Retired	0.002	(0.011)	0.002	(0.013)	-0.014	(0.011)
Age	-0.008*	(0.004)	0.003	(0.005)	-0.020***	(0.004)
Age squared	0.009**	(0.003)	-0.000	(0.004)	0.016***	(0.003)

Table 20.2 (continued)

Variables	(1) All assets		(2) Financial assets		(3) Other real assets	
	Marginal effects	Standard error	Marginal effects	Standard error	Marginal effects	Standard error
Partner	-0.011	(0.007)	0.005	(0.008)	-0.005	(0.006)
Household size	0.022***	(0.004)	-0.004	(0.004)	0.028***	(0.003)
Poor health	0.050***	(0.014)	0.089***	(0.019)	0.050***	(0.014)
HH equiv. income (log)	-0.003	(0.003)	-0.015***	(0.004)	0.011***	(0.003)
Social network size	-0.011***	(0.003)	-0.012***	(0.003)	-0.004	(0.003)
Homeowner	0.047***	(0.007)	-0.039***	(0.008)	0.002	(0.007)
Financial market part.	0.217***	(0.007)			-0.007	(0.007)
Other assets ownership	0.149***	(0.008)	-0.030**	(0.010)		
Newly retired	0.040***	(0.012)	0.047***	(0.014)	0.030**	(0.011)
Household size increase	0.014	(0.014)	-0.008	(0.018)	0.009	(0.014)
Household size drop	0.082***	(0.012)	0.026	(0.014)	0.081***	(0.010)
Health improvement	0.013	(0.019)	-0.018	(0.025)	-0.010	(0.020)
Health drop	0.070***	(0.013)	0.074***	(0.017)	0.077***	(0.013)
N. Obs.	21,320		12,412		17,190	
Pseudo R-squared	0.0828		0.1060		0.0430	

Significance: \*\*\* = 1%; \*\* = 5%; \* = 10 %

Notes: Controlled for country dummies. Financial distress, employment status, age, having a partner, household size, poor health, income, homeownership, financial market participation, other real assets ownership and size of social network are relative to Wave 4

Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

In Table 20.3 we report estimates for the probability of liquidating assets by age subgroups, in particular we look separately at households whose head is below or above 65, the most common retirement age. For both groups we observe that the liquidation of assets is a strategy used to alleviate financial distress. Household size drops and poor health conditions are important determinants of liquidation in both groups but, notably, a larger role of social inclusion emerges for the 65+: the presence of a partner and the size of the social network are significant protective factors only for the older group.



**Table 20.3:** Probit estimates of assets liquidation between Wave 4 and Wave 5, by age group

Variables	(1) 64–		(2) 65+	
	Marginal effects	Standard error	Marginal effects	Standard error
Financial distress	0.047***	(0.013)	0.028**	(0.010)
Female	0.007	(0.010)	0.031***	(0.008)
Foreign	0.041*	(0.016)	–0.015	(0.014)
Education (ISCED 0-2)	0.059***	(0.014)	0.088***	(0.011)
Education (ISCED 3-4)	0.037**	(0.012)	0.042***	(0.011)
Employed	–0.012	(0.013)	0.085***	(0.021)
Retired	–0.008	(0.017)	0.029	(0.015)
Age	0.005	(0.024)	–0.014	(0.010)
Age squared	–0.004	(0.022)	0.013	(0.007)
Partner	0.001	(0.011)	–0.020*	(0.009)
Household size	0.016**	(0.005)	0.026***	(0.005)
Poor health	0.062*	(0.027)	0.044**	(0.016)
HH equiv. income (log)	–0.001	(0.004)	–0.005	(0.004)
Social network size	–0.008	(0.005)	–0.012**	(0.004)
Homeowner	0.012	(0.012)	0.074***	(0.009)
Financial market part.	0.186***	(0.012)	0.238***	(0.009)
Other assets ownership	0.168***	(0.016)	0.139***	(0.010)
Newly retired	0.029	(0.017)	0.046*	(0.018)
Household size increase	–0.009	(0.021)	0.034	(0.019)
Household size drop	0.082***	(0.015)	0.091***	(0.020)
Health improvement	0.021	(0.034)	0.010	(0.023)
Health drop	0.094***	(0.026)	0.062***	(0.015)
N. Obs.	8,825		12,495	
Pseudo R-squared	0.0680		0.1050	

Significance: \*\*\* = 1%; \*\* = 5%; \* = 10 %

Notes: Controlled for country dummies. Financial distress, employment status, age, having a partner, household size, poor health, income, homeownership, financial market participation, other real assets ownership and size of social network are relative to Wave 4

Source: SHARE Wave 4 release 1.1.1, Wave 5 release 0

## 20.4 Concluding remarks

In this chapter we investigate the role played by assets to support the living standards of the older population during the Great Recession.

Focusing on the longitudinal sample, we observe that the fraction of households in financial distress has remained stable in most European countries between Waves 4 and 5. However, non-negligible proportions of households entered and exited financial distress. Looking at transitions into financial distress, we estimate a significant protective role of education, employment, income, homeownership, participation in the financial market. We find that the larger the size of social network in Wave 4, the lower is the probability of falling into financial distress. Leaving financial distress is associated to higher education and income, employment, having a partner, being homeowner and participating in the financial market. Poor health increases the probability of going into financial distress and makes it more difficult to escape it.

Looking at households who liquidated assets between Waves 4 and 5, we find that a large fraction of financially distressed households (above 50 % in Southern European countries) sold completely their financial assets. The role of financial assets as buffer wealth is confirmed in estimation results. We find also that the size of the social networks plays a protective role, reducing the probability of liquidating financial assets, particularly for individuals aged 65+. The sale of the main residence and other real assets instead appears to be mainly associated to changes in household size and other demographic factors that change over the life cycle.

## References

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