FINANCIAL HEALTH OF YOUNG AMERICA:
USE OF FINANCIAL TOOLS & ALTERNATIVE FINANCIAL SERVICES

Unique challenges confront today's young adults navigating our financial system. They entered the workforce during a severe recession and as a result, dealt with high unemployment and persistently stagnant wages. In fact, a 2016 Young Invincibles report found that today's young adults earn incomes 20 percent less than Baby Boomers when they were young adults.[i] Meanwhile, globalization and technology also transformed how they work, with automation replacing many occupations and trade opening up competition internationally. Further, they face record levels of student debt, which now exceeds $1.3 trillion.[ii] Young adults make up the largest segment of our workforce,[iii] which means understanding how they grapple with a shifting landscape is vital to ensuring their economic security and that of our country.

Financial inclusion—having access to affordable financial tools and services—is critical because access and use of such tools can improve young adults' income, help them save, and attain financial security.[iv] A growing body of research also indicates that access to financial tools at critical moments can determine an individual's' opportunity to move out of poverty.[v] Conversely, barriers to gaining access to the financial system or financial exclusion can exacerbate poor financial health as individuals and households without access to adequate financial tools tend to save less and are less able to cope with an economic shock.[vi] Following a Young Invincibles report analyzing the financial challenges of today's young people, this document provides a snapshot of the financial health of this generation. It then reviews the use of traditional tools, including checking and savings accounts and alternative financial services (AFS) products like check cashing and payday lending to better understand financial health among young adults.

Our random sample poll of Millennials (ages 18-to-34) and analysis of national data reveal troubling signs of young adult's financial health. Savings are critical to creating a financial buffer in the event of an economic shock like a medical emergency or job loss. However, a majority of Millennials are financially fragile; they have not been able to maintain an emergency savings fund of at least 3 months. Savings accounts are important to accumulating savings and maintaining financial security, but about 1 in 10 Millennials is unbanked—they have no savings, checking, or money market accounts. Many more young adults are underbanked, meaning they have a bank account but still rely on high-cost alternative financial services (AFS). For instance, nearly a quarter of Millennials use money orders and 14 percent of Millennials using check cashing services.[vii] Over a third of Millennials are foregoing credit cards, through credit card use can help young adults build a substantial credit history important to their financial security.

The historical and contemporary financial exclusion of communities of color is especially troubling and illustrates how inequities are perpetuated. Thus, this brief also explores disparities in use of financial tools and alternative financial services to better understand their use among communities of color.

Too Many Young Adults Are Financially Fragile

An important snapshot of financial health is net wealth, or one's assets minus liabilities. In 2016, Young Invincibles examined several economic indicators, comparing Millennials to Baby Boomers when they were young adults. The study found that today's young adults have half the net wealth as Baby Boomers when they were young adults, and attributed the collapse of the housing market, declining wages, and rising student debt to this generational decline.[viii]
Savings, having sufficient living expenses in liquid assets, is another important component of financial health.[ix] Financial planners recommend maintaining an emergency savings fund of *at least* 3 months in the event of an economic shock like job loss or a medical emergency.[x] However, **61 percent** of today's Millennials (ages 18-to-34) compared to **52 percent** of the general public are unable to cover expenses for 3 months because they lack savings, assets to sell, or the support network from which borrow to money.[xi]

Young people of color are uniquely struggling. For example, **54 percent** of white Millennials compared to **65 percent** of Latinx[xii] and **73 percent** of black young adults do not have an emergency or rainy day savings fund of at least 3 months. [xiii][xiv] This racial disparity persists although legal statutes explicitly barring people of color from participating in our financial system have been restricted, systemic racism and implicit bias continue to stratify financial opportunity along racial lines.[xv]

Young Adult Use of Traditional Financial Tools and Alternative Financial Services

Traditional Financial Tools

Traditional financial tools include checking and savings accounts and credit cards can provide important opportunities to build long-term wealth and credit. Promoting the financial inclusion of young people by making financial tools like savings accounts accessible is important to prevent unbanked and underbanked status later in life.[xvi] However, many young adults today are either unbanked or underbanked, while others have shunned credit card use, raising questions about the ability of the mainstream financial institutions to provide these services and how this generation will build wealth and maintain financial security.

Too Many Young Adults Are Unbanked

Approximately 12 percent of young adults (versus 8 percent of the general public) are what's known as unbanked or do not own a checking or savings account, which are considered two of the most basic financial tools and symbols of financial security.[xvii] Being unbanked limits access to credit, financial products and services, inhibiting savings and also increases the costs of everyday transactions. Not having access to most sources of credit also makes it more difficult and costly to establish credit and qualify for a loan. Finally, people who are unbanked often turn to high-cost alternative financial service (AFS)[xviii] providers, including payday lenders and pawn broking services (more on this below). The costs of unbanked status are especially concerning in light of Millennials' economic fragility or their inability to cope with an economic shock.

Like many other indicators of financial health, unbanked status is stratified along racial and ethnic lines: **12 percent** of Latinx and **17 percent** of black Millennials are unbanked (versus 7 percent of white Millennials). These disparities suggest that the consequences of historical redlining and disinvestment by the financial industry are still felt in communities of color. Some financial institutions actually continue the practice of redlining—denying or avoiding providing services to a consumer because of the racial demographics of the neighborhood in which they live.[xixxx] This is important because the most cited reason, among young adults and the general population alike, for choosing a financial institution is the branch location.[xxi] It should come as no surprise then that studies have shown people are more likely to have a bank account and less likely to use non-banks for financial transactions when they have reasonable geographic access to branches.[xxii] We must do more to ensure basic and fundamental financial inclusion for all young adults and their communities.

Why Young Adults Are Unbanked

Many have weighed in to discuss the factors driving young adults to be unbanked or disconnected from the financial mainstream, some explanations include the following:

- **Banking is Unaffordable.** Low and moderate-income young adults face a number of barriers to bank account ownership. For many, the costs of account ownership are unaffordable. Traditional checking accounts carry minimum balances, non-sufficient fund (NSF), and other transactional fees. In fact, a study found that these high transaction costs increased the costs of credit and saving in mainstream financial institutions for lower-income people.[xxiii] High or unpredictable transaction fees like costly overdraft practices can push people out of the banking mainstream indefinitely.[xxiv]
- **Denied an Account.** Low and moderate-income young adults can also be deemed unqualified for a bank account if they have any negative banking history (e.g. by failing to pay a fee) or have a poor credit history.[xxv] It should be noted that young people incur more overdrafts at higher rates than any other age group, putting them at a higher risk of being denied an account.[xxvi] Those who face financial challenges are more likely to have a negative banking history and be shut out of accessing checking and savings accounts. Denying the financial tools important to address their economic challenges only makes it more difficult for young people to achieve financial security. Unfortunately, they are denied access due to controversial bank account screening agencies. Consumer justice and even financial institutions have expressed concern about bank account screening accuracy, consistency, transparency, and lack of error resolution.[xxvii]
- **Banking Deserts.** Many low-income people and people of color live in communities with increased concentration of alternative financial services (AFS) providers[xxviii] and few or no

mainstream financial bank branches, which are both correlated with higher rates of unbanked status.[xxix] Clearly, geographic inaccessibility to banks due to redlining plays an important role in the financial exclusion of young people of color.
- **Lack of Trust.** A 2015 Young Invincibles survey found **39 percent** of young adults have little or no trust at all in banks.

Credit Card Use Down Among Millennials

Responsible credit card use can be a positive tool that helps one build a credit score, making it easier to obtain future credit. While increasing credit card debt burdens can be alarming, there are also repercussions for young adults if they do not have the means to access money for big purchases or build a substantial credit history. However, a 2015 Young Invincibles survey found that half of young adults have little or no trust at all in credit card companies.[xxx] This could be in part because Millennials came of age during the Great Recession and witnessed their parents and community members lose their homes, jobs and struggle to repay increasing credit card debt. Understandably the financial crisis impacted young adults' mindsets, they might be more risk-averse and concerned about accumulating debt.[xxxi] Given this risk aversion and lack of trust, the following credit card ownership rates are not surprising:
- **35 percent** of young adults don't have any credit cards, compared to 21 percent of the general public.[xxxii]
- Millennials with lower incomes and educational attainment are less likely to have a credit card compared to their higher income and educated counterparts.[xxxiii]
    - **52 percent** of low-income (<$40K) Millennials have at least one credit card, while 78 percent of moderate-income ($40K-$99K) and 84 percent of high-income ($100K+) Millennials have at least one credit card.
    - While 89 percent of Millennials with a bachelor's degree or higher have a credit card, **50 percent** of Millennials with a high school degree have a credit card.
- **62 percent** of Latinx and **60 percent** of black Millennials have a credit card (versus 67 percent of white Millennials).
- **30 percent** of young adults have carried a balance on their credit card most or all of the time in the past 12 months.
- **24 percent** of young adults have paid only the minimum payment on their credit card most or all of the time in the past year.

Alternative Financial Services

Alternative financial services (AFS) include a wide range of services from check cashing to pawnshop loans that are an important option for some, but can be detrimental to one's ability to save and long-term financial well-being. Individuals that have bank accounts, but depend on alternative financial services are considered "underbanked," which can make them more financially insecure because these services are often predatory, reduce take-home pay due to their high-cost, and do not promote saving.[xxxiv] Importantly, one should take into account that relying exclusively on mainstream financial institutions is not inherently beneficial to low- and moderate-income young adults, who are also not served well by the financial system.[xxxv]

Many Young Adults Are Underbanked

Although unbanked rates are concerning, many more young adults are "underbanked," meaning although they have a traditional bank account, they depend on non-banks for their financial needs.

Check Cashing

Young adults use high-cost AFS products at higher rates than the general public. For young people who are unbanked or have no checking account, check cashing is often how they access their money. For those who do have a traditional bank account and turn to check cashing stores for their financial needs because of the immediacy in accessing their money,[xxxvi] the transparency of fees, and service.[xxxvii] Given the uncertainty and long check clearing times at banks, young people need their money as soon as possible perceive check cashing services as their best option.

Young Invincibles' analysis of the Survey of Household and Economics Decisionmaking (SHED) data found that:

- **Nearly a quarter** (24 percent) of young adults have used a money order in the past year.
- **14 percent** of young adults have used a check cashing service in the past 12 months.

Payday Loans

Among non-bank AFS products, payday loans are common. Payday loans are small unsecured loans with exorbitant annualized interest rates, which often have annual percentage rate (APR) of 400% for a two-week loan.[xxxviii] The Consumer Financial Protection Bureau (CFPB) has cautioned that "for some people, these loans become debt traps."[xxxix] The exorbitant fee payments of payday loans have extensive consequences on the borrower's finances, including increased difficulty paying mortgages, rent, and utility bills,[xl] delaying medical care,[xli] delinquency on credit card debt,[xlii] loss of checking accounts[xliii] and bankruptcy.[xliv] Importantly, payday loans also a disincentive to financial service providers from offering more reasonably priced loans.

Data on young adult use of payday loans includes:

- **6 percent** of young adults use payday loans. Young adults (ages 18-to-24) make up nearly a third of payday consumers.[xlv]
- **8 percent** of Millennials have used a pawn shop loan, payday loan, auto title loan or paycheck advance in the past year.
- Though payday loan use is often associated with consumers of low-income backgrounds, moderate-income consumers use payday loans at the same rate. **7 percent** of low and moderate-income young adults have used a payday loan within the past year.[xlvi]
- Still, young adults are likely aware of the dangers of payday loans, with **82 percent** telling Young Invincibles they don't trust payday lenders much or not at all.[xlvii]

As with unbanked rates, communities of color are disproportionately underbanked and use AFS products like payday loans. While 4 percent of white Millennials use payday loans, **13 percent** of black and **10 percent** of Latinx Millennials use payday loans.[xlviii] Communities of color are underserved by mainstream financial institutions and payday storefronts are more likely to be located in and marketed to communities of color, communities with people of lower educational attainment and renters.[xlix] As such, underbanked rates are also higher among people with lower educational attainment and income.[l]

Summary

Though there is a lot more to learn about young adults' traditional and alternative financial services use, the data in this brief and in Young Invincibles' prior reports show young adult financial health is in dire straits. To recap, trends that exacerbate young adults' financial fragility include:

- **Credit Card Use:** 35 percent of young adults don't own a credit card, precluding them from building a robust a credit history and from accessing money for big purchases.
- **Unbanked:** More than 1 in 10 of young adults are unbanked—they have no checking, savings, or money market accounts.
- **Underbanked:** Young adults use high-cost alternative financial services (AFS) products, with young people making up nearly a third of payday consumers.

This brief was authored by Kelly M. Hernandez.

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[xi] Young Invincibles analysis of the Survey of Household Economics and Decisionmaking (SHED), Board of Governors of the Federal Reserve System, 2015.

[xii] Latinx (pronounced "La-TEEN-ex") is a gender-inclusive way of referring to people of Latin American descent. For the purposes of this document the term "Latinx" will be used broadly to include all individuals that are characterized by the Board of Governors of the Federal Reserve System data as "Hispanic" based on the preference of the author.

[xiii] Millennials refers to the population ages 18 to 34 as of 2015.

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