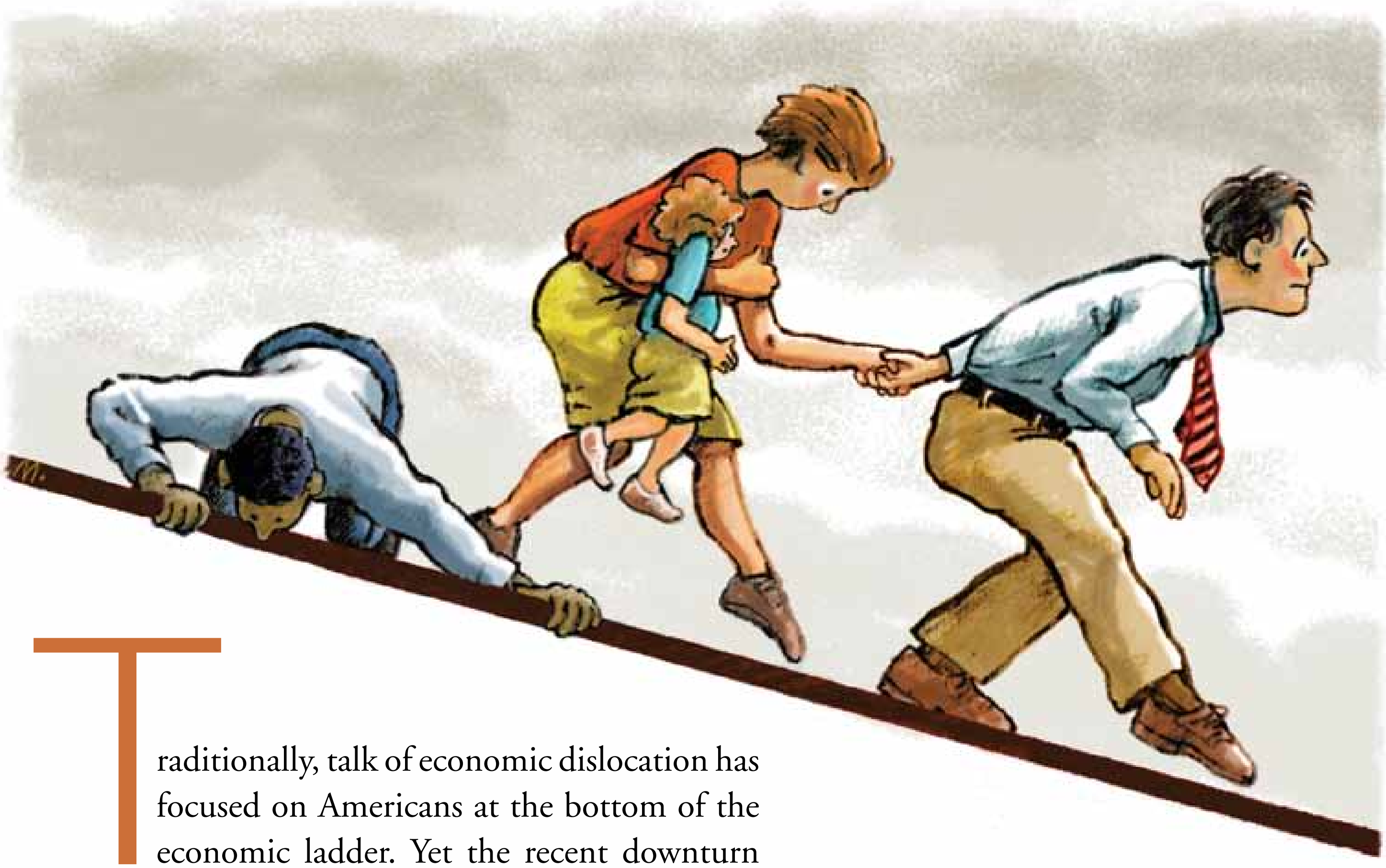
# Understanding Economic Insecurity

## The Downward Spiral of the Middle Class



Traditionally, talk of economic dislocation has focused on Americans at the bottom of the economic ladder. Yet the recent downturn has showcased another side: the risk confronted by most Americans, poor and middle class, of tumbling down the economic ladder without an adequate safety net.

This second form of economic hardship is what researchers frequently if imprecisely call *economic insecurity*. Analysts generally use the term to capture the degree to which people are protected against major economic losses. Complicating matters is the fact that economic insecurity is understood to be both a psychological state ("I feel insecure") and an economic condition ("I have a real chance of experiencing economic losses for which I lack adequate protection").

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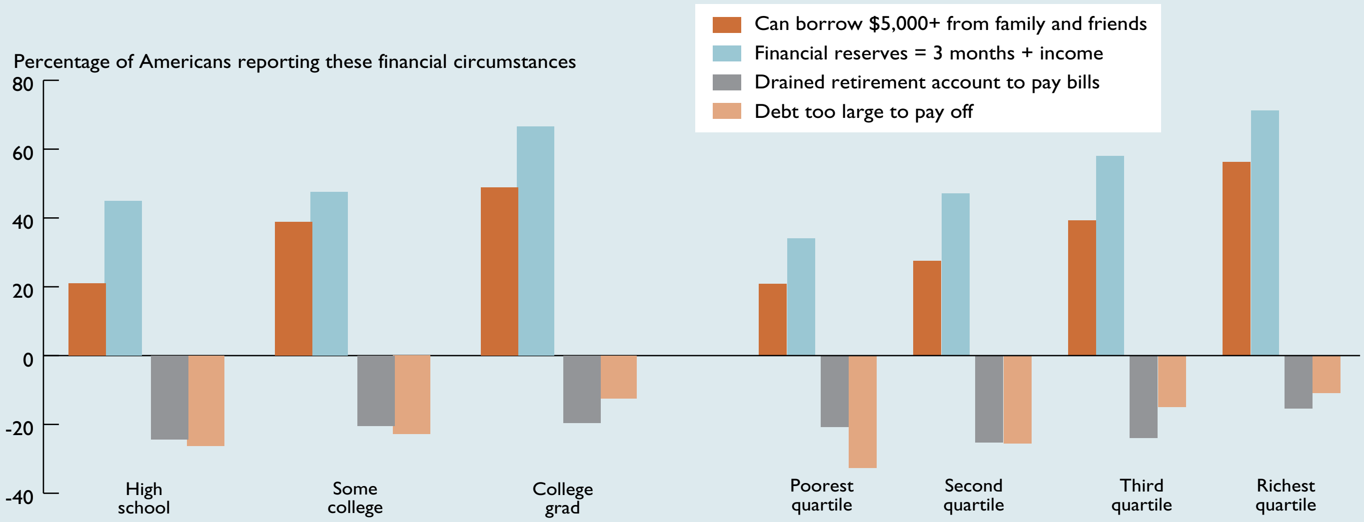
Illustration: Barry Maguire

## Uneven Financial Buffers Against Economic Uncertainty
## Socioeconomic Status, 2009




Source: Jacob S. Hacker, Philipp Rehm, and Mark Schlesinger, "Standing on Shaky Ground."

The study of economic insecurity remains in its infancy. To help fill the gap, I have spent the last several years investigating the key dimensions of economic security and developing a simple integrated measure: the Economic Security Index (ESI).[1] Funded by the Rockefeller Foundation, this project has involved researchers from diverse backgrounds and guidance from a technical committee of top economic experts.

The work's two main parts mirror the two sides of economic insecurity. First, we use the best available panel economic data to develop a measure of the actual risk of economic loss that Americans face.[2] Second, we use opinion surveys to examine how people think about and experience such losses. Our investigations point to a consistent conclusion: The prevalence of insecurity has increased over the last generation, and this insecurity is associated with strong psychological responses and substantial economic hardship.

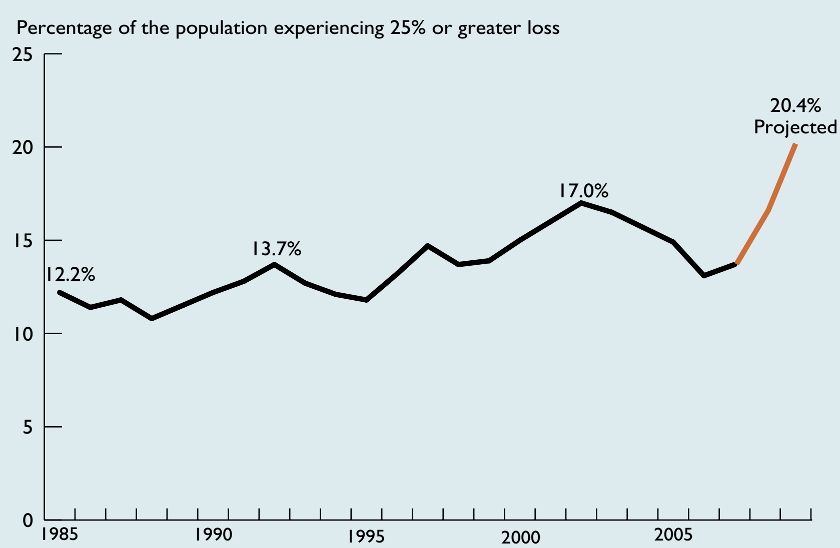
## Economic Security Index

The first major product of our work is the ESI. The ESI represents the first attempt to incorporate into a single unified measure several key influences on economic security: income loss, out-of-pocket medical spending, and households' financial safety net. It is unique in measuring these dimensions using panel data on economic experiences rather than public opinion data on individual perceptions of those experiences.

In our index, the insecure are those whose household income declined by at least 25 percent from one year to the next (after adjusting for inflation) and who lacked an adequate financial safety net to make up for that decline. "Income" included not just earnings but all sources of government and private support, including unemployment benefits, gifts from friends, and retirement benefits. We also measured families' out-of-pocket medical spending and subtracted that amount from income. Thus our measure looked at big drops in income occurring either because household income fell or because medical costs spiked. Our definition of an "adequate financial safety net" is based on the typical post-drop recovery paths of people whose incomes fall by 25 percent or more. We excluded those who had enough liquid wealth to compensate for lost income until they regained their prior income level.

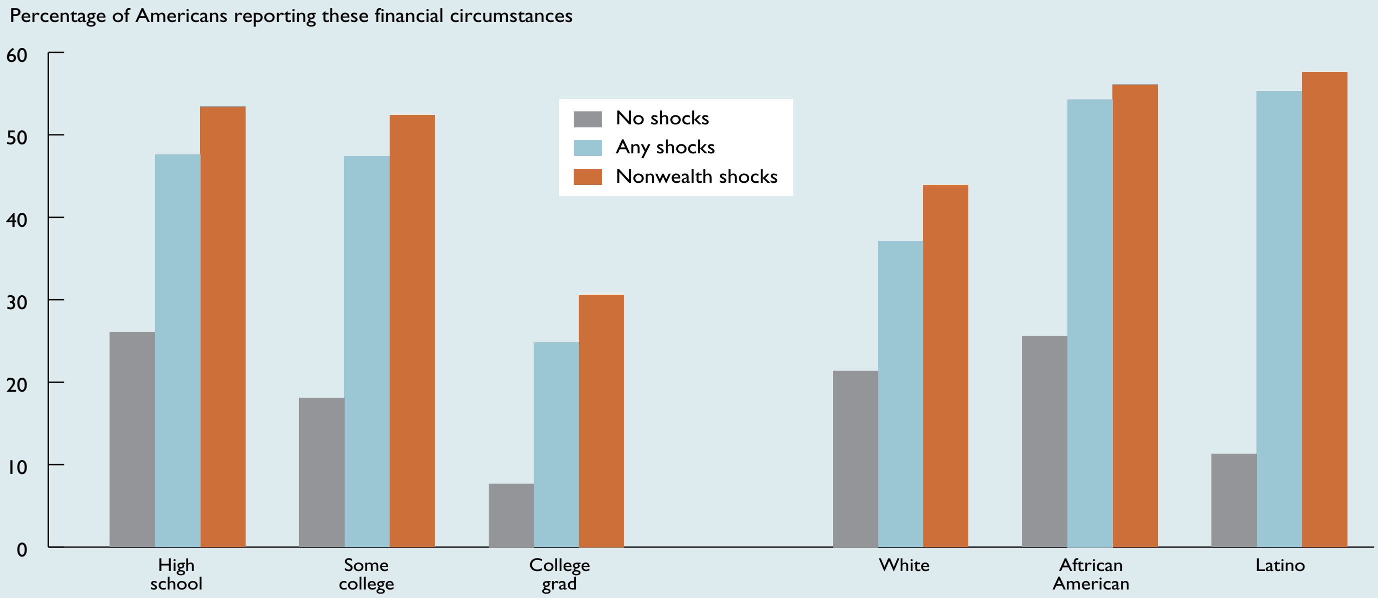
For a family making $50,000 a year (close to the national median), a 25 percent-plus drop means a drop to $37,500 or less

## The ESI: Americans Experiencing Major Economic Losses, 1985-2007 (with 2008-2009 projections)




Source: Jacob S. Hacker, Gregory A. Huber, Philipp Rehm, Mark Schlesinger, and Rob Valletta, *Economic Security at Risk.*

## Unmet Needs by Education, Race/Ethnicity (with and without shocks)

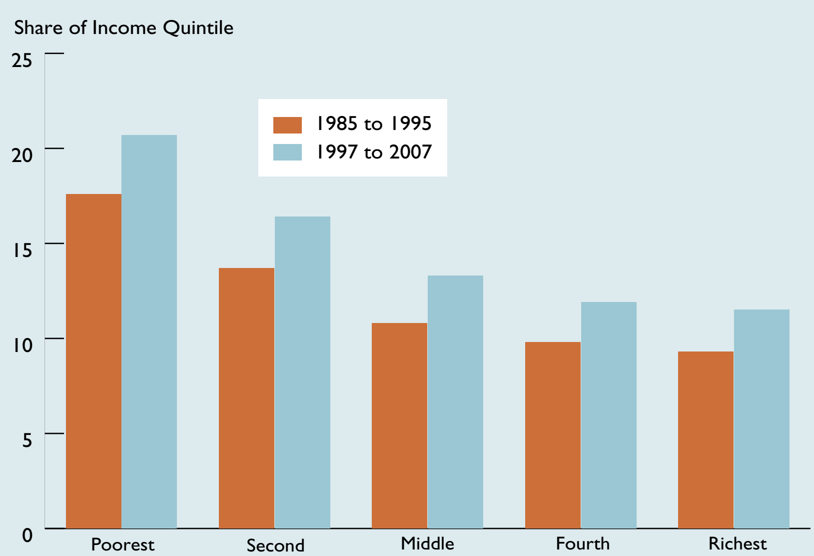



Source: Jacob S. Hacker, Philipp Rehm, and Mark Schlesinger, "Standing on Shaky Ground."

in a single year. In a survey we conducted during the downturn, more than half of respondents reported that they would face hardship if they experienced a drop of that magnitude.

Across the economy's ups and downs there was a gradual but persistent rise in overall economic insecurity. The ESI examines government data from 1985 to 2007, with projections for 2008 and 2009 validated through our independent poll.[3] (See "The ESI: Americans Experiencing Major Economic Losses, 1985-2007.") In 1985, 12 percent of Americans were defined as insecure by the ESI. In 2010, the share was projected to hit 20.4 percent. The long-term trend has been upward. Unsurprisingly, economic security erodes during downturns, but between downturns, it does not bounce back.[4] Using a more limited data source, which allows examination of income drops only (not medical spending or wealth), we find that insecurity started rising in the 1970s.

## The Prevalence of Large Economic Losses, by Income Quintile and Period




Source: Jacob S. Hacker, Gregory A. Huber, Philipp Rehm, Mark Schlesinger, and Rob Valletta, *Economic Security at Risk.*

The extent of economic security varies. Those with the most income and education have faced the least insecurity. The less affluent, those with limited education, African Americans, and Hispanics have faced the most. Virtually all groups, however, have experienced significant increases in insecurity over the past 25 years. For example, the ESI increased by between one-fifth and one-quarter among all income quintiles between 1985-1995 and 1997-2007. (See "The Prevalence of Large Economic Losses by Income.") The risk of economic loss has become an issue squarely confronting the American middle class.

## Risk Perceptions and Insecurity

The research team commissioned a two-wave survey that was fielded between March

## Economic Shocks

**Employment**

- unemployed not by personal choice (respondent or immediate family member)
- lost more than a month of work be
- cause of serious illness or injury

**Health Care**

- lost health insurance
- major out-of-pocket medical expenses as the result of serious illness or injury (respondent or immediate family member)
- paid much more for health insurance than expected

**Wealth**

- retirement benefits at work cut substantially
- value of investments or retirement funds declined substantially
- value of house declined substantially

**Family**

- divorced or separated from spouse
- spent a substantial sum helping out extended family
- spouse/partner passed away

**The prevalence of insecurity has increased over the last generation, and this insecurity is associated with strong psychological responses and substantial economic hardship.**

2008 and September 2009, the Survey of Economic Risk Perceptions and Insecurity (SERPI). The SERPI measures economic insecurity in employment, medical spending, family needs, and wealth. It permits examination not just of the share of Americans experiencing economic shocks, but also of the imprint the shocks have on their lives.

In the 18 months preceding fall 2009, fully 93 percent of households experienced at least one substantial shock to their finances. (See "Economic Shocks.") Although most common were shocks to family wealth—not surprising given the decline of the housing and stock markets—nearly seven in 10 households saw their earnings unexpectedly fall or their nondiscretionary expenses rise.

Furthermore, these nonwealth shocks were associated with serious economic hardship. The SERPI measured households' ability to meet basic needs through a combination of questions regarding food security (members of the household going hungry), housing instability (eviction or inability to pay the mortgage), and unmet medical needs (skipping doctor visits out of concern for costs). Households experiencing major economic dislocations were, on average, three to four times more likely than otherwise comparable households to report being unable to meet more than one basic family need, such as food, shelter, or medical care. Although these economic uncertainties were greatest for the least affluent or educated, they were surprisingly broad based. For example, more than half of families with income between $60,000 and $100,000 that experienced employment or medical disruptions were unable to meet at least one basic economic need.

Nevertheless, personal protections against such risks were less evenly distributed. Buffers such as savings and the ability to borrow from family members were more likely in households with advantaged socioeconomic characteristics, whether advantage was measured in terms of income or education. (See "Uneven Financial Buffers," p. 26.)

The consequences of economic shocks for economic well-being were notably more severe for less advantaged Americans—measured here in terms of education. (See "Unmet Needs," p. 27.) Differences by race and ethnicity also loomed large. African Americans face greater risk and report weaker personal buffers and higher levels of unmet needs during economic shocks. Latinos report comparable levels of unmet needs during economic shocks, and both groups report much higher levels of unmet needs than whites. More surprising, Latinos who do not experience economic shocks report lower levels of unmet needs than other groups, suggesting that they may have personal or social supports that are missed in analyses looking only at income or wealth.

Unfortunately, insecurity has become a dominant motif in Americans' economic lives. Yet no measure is offered alongside other measures of economic status, such as the poverty and unemployment rates. Nor does any regularly funded national survey track even a small share of the factors shaping Americans' economic security. The ESI and SERPI partially fill these gaps. There is still a pressing need for more research on the causes, consequences, and differential impact of economic insecurity and its effects on an increasingly broad swath of the U.S. population.

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### Endnotes

1 See Jacob S. Hacker, Gregory A. Huber, Philipp Rehm, Mark Schlesinger, and Rob Valletta, *Economic Security at Risk: Findings from the Economic Security Index* (New Haven: Yale Institution for Social and Policy Studies, 2010); and Jacob S. Hacker, Philipp Rehm, and Mark Schlesinger, "Standing on Shaky Ground: Americans' Experiences with Economic Insecurity," www.rockefellerfoundation.org/news/publications/standing-shaky-ground-americans.

2 Panel data tracks the same people over time.

3 The projections were based on a model of the relationship between the ESI and aggregate economic conditions, such as unemployment and growth in gross domestic product.

4 See www.economicsecurityindex.org.