Exploring Consumers' Financial Fragility in Europe: Over-indebtedness, Rainy Days Funds and the Role of Financial Literacy

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The study sheds light on financial fragility of individuals in Europe. Using data from a 2015 survey on three European countries (Sweden, Italy, and Spain) with more than 1,000 observations, either the excess of borrowing, related with over-indebtedness phenomena, and the lack of funds for "rainy days" are analysed in order to investigate the presence of specific groups within the population that are more likely to sink in a financial fragile status, struggling with their finances. The role of financial literacy in explaining such phenomena is taken into account.

Over-indebtedness is measured in two different manners. The first one considers over-indebted individuals that hold debts that exceed five times their annual income (not considering mortgages for buying their house). The second measure is wider and includes individuals that own debts for more than one time their annual income. The chance to fall into this over-indebtedness status has been estimated, by different regression models, referring to a set of socio-demographic variables that includes age, gender, income, education and job status, and taking into account different measures of financial literacy, assessed by the answers to different sets of multiple choice questions. The availability of 50 questions on financial knowledge, related to ten different areas of knowledge and that include questions with a different degree of difficulty, allowed to test the role of financial literacy on consumer financial behaviors much more carefully than what previous studies did (usually by a limited number of items).

Financial fragility is a concept related with the chance that unexpected events - either permanent (e.g. unemployment, sickness, etc.) or contingent (e.g. car crash, unexpected house repair, etc.) - could push consumers into financial troubles. The lack of immediately available funds for these "rainy days" equal to the amount of money needed to cover basic living expenses for at least three months represented the measure of financial fragility in this study. Coherently with the previous case, socio-demographic variables and different measures of financial literacy were related with financial fragility in order to highlight who are the most financial fragile individuals.

The chance that people could be aware about their financial fragility has been included in the study by a self-assessed measure of financial hardship. Using answers to the question "*In a typical month, how difficult is it for you to cover your expenses and pay all your bills and obligations?*", people that answered "very difficult" or "difficult" have been analyzed using the above mentioned approaches.

Results confirm the hypothesis that over-indebtedness, lacks of emergency funds and difficulties to make ends meet are more frequent in certain groups of the population. Even if some differences exist between the different phenomena and between Countries, low income and low educated individuals seem to be more likely affected by financial fragility. At the same time, if financial knowledge itself seems to be not enough to prevent extreme over-indebtedness scenarios, there are clear evidences that people with more financial knowledge tend to save for rainy days more frequently then others, even after controlling for other variables (e.g. income, mortgages, other debts), and they are less likely to report as "difficult" or "very difficult" to pay their bills and other obligations.

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