

Social Network as Safety Net: The Role of Emotional Support in Avoiding Financial Distress

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The Social Finance Literature

- Financial economists have increasingly recognized the fundamental role of social networks in determining financial outcomes (Hirshleifer, 2015; Kuchler and Stroebel, 2021).
- How do social networks/interactions affect household financial decisions/outcomes?
 - ▶ Source of informal financing;
 - ▶ Transmission of information (i.e., a social learning channel);
 - ▶ Tool for the enforcement of norms (e.g., social stigma);
 - ▶ Directly enter the utility function (e.g., keeping up with the Joneses).

This Paper

- Building on the simple idea that social interactions often come with psychological benefits, I investigate in this paper the **psychological** aspect of social networks/interactions.
- I focus on emotional support, which refers to having someone available to listen, care, sympathize, provide reassurance, and make one feel valued, loved and cared for.
 - ▶ Adverse emotional states such as sadness, frustration, and anxiety are an inevitable part of life.
 - ▶ Often times people seek emotional support from their networks of family, friends, and acquaintances.
 - ▶ The importance of emotional support has been further highlighted by the recent coronavirus pandemic.

This Paper (Cont.)

- Regarding household financial outcome, I focus on financial hardship, which is both **prevalent** and **persistent**:
 - ▶ Four in 10 adults have difficulty handling an unexpected expense of \$400 (Federal Reserve Board, 2020).
 - ▶ Some have frequent trouble with money and their children face similar prospects (Athreya, Mustre-del-Río, and Sánchez, 2019; Kreiner, Leth-Petersen, and Willerslev-Olsen, 2020).
- Why some households are financially fragile while many others are not is still not fully understood.
- Research question: Is emotional support an important determinant of household financial fragility?

Roadmap

1. Data & measurement
2. Baseline findings
3. Potential concerns
4. Underlying mechanisms

Data

1. The National Longitudinal Survey of Youth 1979 Child and Young Adult cohort (NLSY79 CYA): 2008–2018.
 - A panel of biological children of the female respondents in the NLSY79, which itself is a nationally representative panel survey of 12,686 individuals aged between 14 and 22 in 1979.
2. The Health and Retirement Study (HRS): 2004–2018.
 - A longitudinal study that surveys a nationally representative sample of individuals over the age of 50.
3. The Household, Income and Labour Dynamics in Australia (HILDA) Survey: 2001–2020.
 - A nationally representative longitudinal study of Australian households.

Measuring Emotional Support

- I use the following four questions in the NLSY79 CYA:
 1. How much do you feel loved and cared for by your **relatives**?
 2. How much can you open up to your **relatives** if you need to talk about your worries?
 3. How much do you feel loved and cared for by your **friends**?
 4. How much can you open up to your **friends** if you need to talk about your worries?
- For each question, a respondent's rating ranges from 1 to 5, where 1 means "not at all" and 5 means "a great deal."
- Sum all four ratings and convert to percentile ranks.

Measuring Emotional Support (Cont.)

- In the HRS sample, emotional support is measured along four dimensions: (i) from **spouse**; (ii) from **children**; (iii) from **other immediate family members**; and (iv) from **friends**.
- Respondents are asked:
 1. how much they can open up to each source about worries;
 2. how much each source really understands the way they feel.
- For each question, a respondent's rating ranges from 0 to 3, where 0 means "not at all" and 3 means "a lot."
- Sum all eight ratings and convert to percentile ranks.

Measuring Emotional Support (Cont.)

- In the HILDA sample, emotional support is measured based on two statements:
 1. there is someone who can always cheer me up when I am down;
 2. I do not have anyone that I can confide in.
- Each statement is on a scale from one to seven, where one means “strongly disagree” and seven means “strongly agree.”
- The scoring for the second statement is reversed so that higher scores correspond to higher levels of emotional support.
- Sum these two scores and convert to percentile ranks.

Financial Hardship Indicators

- NLSY79 CYA: if the household had either “quite a bit” or “a great deal” of difficulty paying bills over the past year.
- HRS: if it is either “very difficult” or “completely difficult” for the household to meet monthly bill payments.
- HILDA: two indicators indicating whether the household could not pay (i) mortgage/rent and (ii) electricity, gas or telephone bills on time in the past year because of a shortage of money.
- I focus on this aspect of financial hardship primarily because information about payment difficulties is available in all three household surveys. My findings are robust to various alternative indicators.

Regression Specification

- I estimate:

$$y_{it} = \alpha + \beta \cdot \text{Emotional support}_{it} + \gamma' \mathbf{X}_{it} + \varepsilon_{it}$$

- y : financial hardship indicators.
- \mathbf{X} : gender, race, age, educational attainment, marital status, and health status of the respondent, as well as family income and home ownership.
- Region by survey wave fixed effects are additionally included to absorb all sources of variation across regions over the years.
- Standard errors are clustered at the household level.

Baseline: NLSY79 CYA

	Payment difficulties
Emotional support	-0.088*** (0.007)
Controls	Yes
Observations	23,917
R^2	0.045

- A one standard deviation reduction in emotional support:
 - ▶ \Rightarrow a 2.5 pp increase in the prob. of a household having great difficulty in paying bills;
 - ▶ representing an increase of 27% relative to the sample mean;
 - ▶ A lack of college education corresponds to a 3.0 pp increase in the prob. of a household having great difficulty in paying bills.

Baseline: HRS

	Payment difficulties
Emotional support	-0.077*** (0.008)
Controls	Yes
Observations	27,917
R^2	0.084

- A one standard deviation reduction in emotional support:
 - ▶ \Rightarrow a 2.2 pp increase in the prob. of a household reporting substantial difficulty in meeting monthly bill payments;
 - ▶ representing an increase of 23%.

Baseline: HILDA

	Housing PD	Utility PD
	(1)	(2)
Emotional support	-0.047*** (0.004)	-0.090*** (0.006)
Controls	Yes	Yes
Observations	119,199	119,199
R^2	0.051	0.104

- A one standard deviation reduction in emotional support:
 - ▶ \Rightarrow a 1.3 (2.4) pp rise in the probability of a household being late on housing payments (utility payments);
 - ▶ representing an increase of 19% (18%).

Non-Emotional Support?

- Financial assistance?
 - ▶ Estimates of the effect of emotional support on financial hardship are slightly larger than those in the baseline among households that receive little to no financial assistance.
- Practical help (e.g., informal child and elderly care)?
 - ▶ Estimates are comparable in magnitude to those in the baseline among (i) never-married single individuals; and (ii) individuals with no work-limiting conditions.
- Informational support (e.g., financial advice)?
 - ▶ Estimates remain largely the same among (i) narrow-minded individuals; and (ii) those who do not seek information/advice from family and friends when it comes to retirement planning.

Emotional Support?

- I perform a heterogeneity analysis along the personality dimension focusing on one of the Big Five personality traits—neuroticism, or emotional instability.
 - ▶ This is a trait characterizing a tendency toward negative feelings such as anxiety and depression.
- I find a stronger buffering effect of emotional support on financial hardship for individuals with higher levels of emotional instability.
- ⇒ My findings indeed reflect the **emotional** aspect of social support.

Potential Concerns

- Omitted variable bias: there may be unobserved characteristics that affect both emotional support and the likelihood of financial hardship.
- Comparisons between siblings: eliminate confounding factors that are fixed within the family the siblings grew up in.
 - ▶ Individuals with weaker emotional support in adulthood than their siblings are more likely to experience financial hardship.
- Within-individual analysis: differences out time-invariant confounding individual heterogeneity.
 - ▶ As emotional support dwindles, individuals are more likely to experience financial hardship.

Potential Concerns (Cont.)

- Reverse causality: e.g., individuals in better financial situations may spend more time with family and friends and therefore enjoy stronger emotional support from them.
 - ▶ Results are robust to using instead emotional support lagged by five and 10 years as the key explanatory variable.
- To further alleviate the concerns, I instrument for emotional support with frequency of socialization.
 - ▶ The IV regressions confirm the existence of a strong, negative relationship between emotional support and financial hardship
 - ▶ The Conley, Hansen, and Rossi (2012) test result suggests that my findings are robust even under substantial violations of the exclusion restriction.

Mechanisms

- So far, I have established that individuals who lack emotional support are more likely to experience financial hardship.
- The next natural question is, why would emotional support affect the likelihood of financial hardship?
- To investigate this question, I evaluate the role played by emotional support both **before** and **after** realization of negative shocks.
- I start by exploring whether emotional support improves financial preparedness.
 - ▶ Motivated by the importance of planning ahead for household financial well-being (e.g., Ameriks, Caplin, and Leahy, 2003).

Mechanisms (Cont.)

- To capture financial preparedness:
 - ▶ NLSY79 CYA: whether the household sets aside emergency funds that would cover expenses for three months in case of sickness, job loss, economic downturn, or other emergencies.
 - ▶ HILDA: whether the household saves regularly by putting money aside each month.
- Individuals who lack emotional support are less likely to set aside emergency savings as well as to save regularly.
 - ▶ I provide further evidence that a lack of emotional support limits household financial planning horizon.
 - ▶ Consistent with the interpretation that these individuals are less likely to have the bandwidth to formulate as well as to execute long-term financial plans.

Mechanisms (Cont.)

- To investigate the role of emotional support after negative shocks are realized, I focus on **unemployment events**.
- I find that unemployed job seekers who lack emotional support are less likely to find a job.
- I also show that emotional support boosts unemployed job seekers' confidence about their ability to find a job.
 - ▶ The unemployed job seekers with strong emotional support are more likely to have written, phoned, or applied in person to an employer for work in the past four weeks.
 - ▶ Such an increase in job search effort by the unemployed individuals with strong emotional support lines up well with their higher propensity to end their unemployment spell.

Conclusion

- Individuals who lack emotional support are more likely to experience financial hardship.
- Further investigation reveals that emotional support has:
 - ▶ A preventative effect: individuals with strong emotional support can better overcome psychological barriers that impede the execution of financial plans;
 - ▶ A restorative effect: they can better cope with an adverse shock after its realization as emotional support boosts their confidence.
- Overall, this paper underscores the importance of the psychological dimension of social networks in shaping household financial outcomes.