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Features

The Cost of Financial Precarity

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➔ Anxiety about debt and financial stability can severely reduce the productivity and health of employees, which can hurt a company's bottom line. Businesses, government, and philanthropic organizations should embrace the case for improving the financial well-being of workers.

The Cost of Financial Precarity

BY CARRIE LEANA

Illustration by Ariel Davis

Tom lives in Freeport, Pennsylvania. He is 52 and has been working as a truck driver at the same company for more than 20 years. He makes good money—more than \$60,000 per year—enjoys a company-sponsored retirement plan, and has health insurance. He owns a three-bedroom house on two acres of land, helped put a son through college, and continues to help his daughter, who recently went through a rough divorce. From all appearances, Tom has achieved a middle-class life. Yet Tom is deeply worried about his financial situation. He owes \$20,000 on his credit cards, has taken a second mortgage

on his house, and in the past year has had to borrow against his retirement account.

Tom is like many people in the United States who are working full time and even making a “living wage” but are still acutely worried about money. Here we are talking not just about the working poor but also about those whose wages put them squarely in the middle of the income distribution. They live all over the United States, and whether because of insufficient wages, inadequate savings, bad

luck, or some combination of these factors, they can't seem to put enough money away to cover expected future expenses, such as retirement or their children's college costs, much less the unexpected ones that seemingly arise every month.

According to a 2016 report by the Federal Reserve Board, most people in the United States cannot come up with \$400 to cover an unexpected expense without relying on bor-



rowing (i.e., using credit cards or other sources of debt).¹ Households, on average, also carry nearly \$17,000 in credit card debt, with almost half not able to pay off this debt within two years.² National surveys show that, for Americans, money is a more frequent source of concern than work, family, or health issues.³ The name for this persistent feeling of worry affecting more Americans is *financial precarity*.

There is substantial research about the detrimental consequences of financial precarity for individuals, their families, and communities.⁴ Incessant worry about money is associated with poorer health, lower levels of happiness, and increased social isolation. Financial precarity also has a corrosive effect on people's cognitive functioning and their ability to make good decisions.⁵ This is a bad condition for individuals that, if unaddressed, can worsen over time. But a series of studies I have conducted with colleagues demonstrates that people's financial precarity also has significant consequences for the organizations in which they work.

Discussions about the role of employers in the financial well-being of the people who work for them are often framed as a moral issue, with business ethicists admonishing companies to exercise "corporate social responsibility" toward their employees. By contrast, we approach the issue by framing it as an economic question: Do employers receive any gains from the financial well-being of their employees? The findings of our studies say that they do: When people are worried about their personal finances, the costs are borne both by those who experience such worry and by the organizations that employ them. In this regard, it is in *everyone's* interest to address financial precarity.

THE BUSINESS CASE

I am a professor at the University of Pittsburgh who researches work and employment relations. Over the past several years, my colleagues and I have conducted studies with thousands of employees across different occupational groups and socioeconomic strata to examine how financial precarity affects them at work. These studies consistently show that as people become more worried about their financial situations, their work performance falters, with important economic consequences for their employers. The negative relationship between financial precarity and economic performance is explained by the simple fact that people spend much of their time at work, and financial precarity impedes their ability to be productive and perform up to their full potential. Other research has confirmed our findings. For instance, PricewaterhouseCoopers found that more than half of surveyed employees reported being stressed about their finances at work.⁶ Mercer similarly found that people, on average, spend approximately 150 hours per year thinking about their finances while at work, which translates into roughly three weeks of distracted work time annually.⁷

Emerging research in psychology and economics suggests that financial precarity carries a cognitive tax for those who experience it.⁸ One study, for example, found that farmers performed worse on a range of cognitive tests before the harvest, when they were relatively poor, compared with after the harvest, when their financial situation improved.⁹ Our work has drawn from this research to argue that people will carry the cognitive tax of their financial concerns with them as an invisible backpack that slows down their ability

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to perform and be productive as they go throughout their workday.¹⁰ For our initial study on this topic,¹¹ we collaborated with a national transportation company to examine if financial precarity among truck drivers affected their likelihood of having a preventable accident. Despite having only a high school education, most of these workers earned incomes that placed them above the median for households in the United States. Thus, they represented the celebrated "middle class" in America, where we would not expect widespread financial precarity.

To investigate the link between drivers' finances and their accident rates, we collected survey data from more than 1,000 short-haul truck drivers and matched it with accident logs for the subsequent eight months. Analysis of our data revealed that despite their middle-class incomes, personal finances were a more frequent and extensive source of worry in this population than health or family issues. Consistent with our predictions, we found that drivers who were worried about their finances were more likely to have a preventable accident in the following eight months. We found that this trend was due to the cognitive tax associated with financial precarity: Worry about money made drivers less attentive on the job. Based upon the average cost of a commercial truck accident, we estimated that drivers' financial precarity was associated with at least \$1.3 million per year in additional costs to the company.

We subsequently replicated these findings in a controlled laboratory setting. As part of a series of lab sessions, 90 participants—who were evenly split between men and women and had an average age of 28 years—were first asked about their current financial resources. They were then asked to imagine that their car had a breakdown with a randomly assigned \$150 or \$1,500 cost of repair. Afterward, we had participants complete a set of cognitive tests, as well as drive a route in a simulator that replicated city driving. Random assignment to imagining the \$1,500 expense evoked financial worry for people who had fewer resources available to them. These participants had more traffic violations in the driving simulation, which, as with the truck drivers, were attributable to the cognitive tax of financial precarity.

We have also examined the consequences of financial precarity among workers who were expected to feel more of a financial pinch because their wages and benefits were well below the median. Our participants in this study were certified nursing assistants who provide care to the frail elderly in skilled nursing facilities.¹² In these jobs, empathy with the client is important to the overall quality of care provided to patients. And, indeed, we found high levels of empathy among almost all the aides in our sample. As with the truck drivers, however, financial precarity undermined their job performance. Overall, empathy among the aides was a significant predictor of patient safety. But aides who experienced more financial precarity were less likely to notice threats to the safety of the patients on their watch, despite their high levels of empathy. It's not

that they were less motivated, cared less about the patients, or were less skilled at doing the work. Instead, the cognitive tax imposed by persistent financial worry got in the way of their job performance, as their preoccupation with their financial problems compromised their ability to notice changes in patient health.

We find similar effects even among young people preparing to enter the workforce.¹³ While higher education is considered to be the primary vehicle for economic mobility in the United States, a college education is becoming increasingly expensive. In-state tuition and fees at four-year public institutions have nearly doubled since 1995.¹⁴ Students' total budgets (including housing, food, books, transportation, and other expenses), on average, exceeds their financial aid by \$12,000 per year at four-year public institutions and nearly \$20,000 per year at four-year private nonprofit institutions. This leads many students to struggle to meet their basic financial needs even when they receive financial aid.¹⁵ Given the rising costs associated with college attendance, we expected there to be considerable financial precarity in this population, where the associated cognitive tax can detract from students' ability to focus in the classroom.

To investigate the link between college students' financial precarity and their academic performance, we followed a cohort of incoming first-year students at a large public university. We collected survey data from participating students, as well as information about their SAT scores, first-semester academic performance, and several other factors that have been shown to be predictive of students' academic success, such as demographics, time spent on classes, and socioeconomic background. We found that students who reported having no financial concerns at the beginning of the semester performed up to their potential as indicated by a strong relationship between their SAT scores and first-semester grade point average (GPA). However, among students who reported having significant concerns about meeting their financial obligations in college, the expected positive relationship between SAT scores and GPA disappeared. Thus, students who were worried about paying for college were less likely to realize their academic potential.

When taken together, the findings of our studies illustrate how organizations have a stake in safeguarding the financial health of their employees. We consistently find that financial precarity undermines people's ability to perform across a variety of tasks and contexts. When people are worried about their personal finances, it hinders their ability to be productive and perform. Financial precarity has also been linked to a range of health ailments and conditions, which can further drive down productivity and increase costs. Thus, our research suggests that there is an economic cost associated with widespread financial precarity that is borne by employees and employers alike.

AMERICAN EXCEPTIONALISM

What is to blame for the status quo, in which workers experience persistent worry about paying the bills? Many observers blame individual choice: People overestimate their future earnings and underestimate their future expenses, leading them to spend too much in the present and borrow against this optimism. As a result, companies are investing in financial literacy, educating employees on how

to better manage their spending and investments. The underlying assumption is that if people only knew better, they would not be so prone to financial precarity.

This approach, however, has been largely ineffective in achieving long-term reductions in financial precarity,¹⁶ because financial literacy interventions don't address the source of the problem. The assumption that deficiencies in individual prudence are the primary driver of financial precarity negates the unique economic context of the United States. This may require us to think beyond investments in education toward more robust changes in what people should expect to receive in return for their employment.

In the United States, the design of the social system depends largely upon employers' discretion to provide critical social safety nets such as health insurance and retirement savings, as well as other welfare-enhancing benefits such as paid sick days and parental leave. Compared with other developed economies, where social benefits are administered primarily by the state, public policy in the United States has favored their provision through private entities over government involvement.¹⁷ Indeed, more than half of the insured population in the United States relies on private health-care coverage from their employer, compared with 36 percent who are covered through Medicare or Medicaid.¹⁸ In fact, the United States leads Organisation for Economic Co-operation and Development (OECD) countries in the percentage of social benefits funded by for-profit companies and NGOs.¹⁹ US public policy has also favored employers' discretion in the extent and types of benefits that workers are entitled to. The United States trails OECD countries in the ratio of the mandated minimum wage to the average wage of full-time workers.²⁰ It is also the only developed country where workers are not guaranteed any paid sick leave²¹ or parental leave.²²

Limited government involvement in the provision and regulation of benefits does not inherently produce widespread financial precarity, but it can create a context that fuels it. When employers rather than the state are tasked with the administration of crucial social safety nets, their provision becomes a component of workers' compensation packages, which are vulnerable to macroeconomic trends, business cycles, and shareholder pressures. Indeed, research has shown that many companies have increasingly shifted costs onto individual workers, which has resulted in reductions in the availability and extent of the benefits they receive. Most US employers, for instance, have jettisoned defined-benefit pensions in favor of defined contribution accounts under employees' direct responsibility,²³ while also expanding employees' share of health insurance expenses.²⁴ These developments create a context for financial precarity to flourish by introducing and increasing uncertainty into people's lives as individuals are asked to shoulder more of the risk for the escalating costs of health care or fluctuations in financial markets in which retirement savings are invested.

REVERSING COURSE

Given the human and economic costs associated with widespread financial precarity in the United States, reversing current trends is not only in the interest of the people who experience it but is also of concern to managers and policy makers. Significantly decreasing financial precarity in society will require changes in social and labor policy, as well as more direct intervention from employers.

Public policy | From a policy perspective, the pervasiveness of financial precarity in the United States and its consequences should prompt a debate over the role of government in ensuring financial security for all. Under current US policy, employers are expected to be conduits for social benefits such as health insurance and retirement savings for a large segment of the population, which makes these benefits a discretionary component of compensation packages. At the same time, employers are given a great deal of latitude in the types of benefits they provide and the extent to which they elect to do so. To address precarity, it may be time to reconsider the role of government in ensuring financial welfare in the United States. Here there are at least two potential avenues of action.

The first approach would be to expand government's direct assumption of responsibility for providing social benefits. Currently, US government investment in financial security is fairly limited in comparison with other developed economies. In fact, out of the 35 OECD countries, the United States ranks 28th in government spending on illness, disability, and occupational injury protections; 34th in spending on labor market programs, including unemployment benefits and training programs; and 32nd in spending on family assistance.²⁵ Collectively, the data suggest that there is considerable room for increased government involvement. This approach has recently gained some traction with regard to medical coverage, with the 2010 passage of the Affordable Care Act and more recent calls by some Democratic Party officials to expand Medicare.

A second approach that is perhaps more attractive to those who prefer limited government involvement is to enact mandated minimums. That is, instead of direct involvement in the provision of social benefits, the employer-based system can remain intact, but with policymakers establishing minimums in the pay and benefits that employers must provide. The minimum wage, a federally guaranteed floor that has been in place for 80 years, is the best-known example of a mandated minimum. Some state and local governments have also enacted regulations regarding employer-provided safety nets, such as guaranteeing a livable minimum wage²⁶ and paid leave.²⁷ Through these regulations, employers are still the primary providers of benefits, but with the stipulation that every employed person receive the minimum necessary to have a basic level of financial security. Essentially, this approach does not lead to wholesale changes in the design of the current social and labor systems, but instead protects people's benefits from economic downturns, business cycles, and other macroeconomic trends. If all employers were required to pay higher minimum wages and benefits, they would not have the incentive to compete on labor costs in a "race to the bottom."

Employers | The current system places considerable responsibility for the financial welfare of society on the shoulders of employers. While there is evidence that they in turn have shifted a good bit of that responsibility onto individuals,²⁸ employers are nonetheless well-positioned to reverse some of the trends in financial precarity. Our research suggests that doing so could lead to big payoffs, but it may require a closer evaluation of the quality of jobs that employers offer to their employees, and whether those jobs can provide a minimum standard of living commensurate with the expectations of a developed economy. According to the US Bureau

of Labor Statistics, 6.3 percent of the labor force is in poverty despite holding full-time jobs,²⁹ while nearly a third of Americans are considered low-wage workers.³⁰ Moreover, employers are increasingly designing jobs in ways that can introduce uncertainty into their employees' personal finances, such as variable pay and fluctuating schedules. Many retailers, for example, have moved to "just in time" scheduling where employees are called in to work or sent home based on hourly fluctuations in customer volume. Employers who wish to reap the benefits associated with financial well-being in their workforces could do so by increasing their minimum compensation to a living wage, providing more stability in scheduling and pay, and improving the benefits they offer, such as low-deductible health coverage and retirement savings with an employer contribution.

In conjunction with improvements in job quality, employers can develop interventions targeted at specific personal financial challenges within their workforces. Several of our recent studies address how particular interventions, aimed at action rather than just education, can be effective in reducing financial precarity. For example, in the transportation company we worked with, employees were provided with a menu of financial wellness initiatives.³¹ These initiatives fall into two main categories: (1) problem-focused activities that directly address a component of personal finance, such as reducing debt or developing short-term savings; or (2) information-focused activities that alert employees about their personal finances, such as through a detailed credit report or a review of their retirement savings account. We found that employees' participation in more problem-focused activities led to decreases in financial precarity while information-focused activities were far less effective. We also found that decreased financial worry was associated with improvements in health symptoms such as better sleep, more energy, and less physical pain—all factors that affect job performance. Moreover, the program was implemented at relatively low cost (about \$120 per employee) and offered considerable benefits in the form of a healthier and more productive workforce.

In another study,³² we randomized incoming freshmen at a public university to receive biweekly text messages that provided them with easy access to financial resources available on campus. This intervention reduced financial precarity among students with more financial need and boosted their academic performance.

Studies like these demonstrate that such interventions can not only result in reduced financial precarity among individuals but offer benefits to their organizations as well.

FREEDOM FROM FEAR

Employers have a central role in the financial welfare of American society. Robust evidence shows that financial precarity is widespread in the United States as wages have stagnated, benefits have dwindled, debt has increased, and most Americans have been unable to adequately save for emergencies or retirement. Our research demonstrates the "business case" for greater employer concern for the personal finances of their workers by linking financial precarity to economic outcomes. Across several studies, we consistently find that people do not leave their financial concerns at the door of their workplace (or school), but rather carry them into their place of employment, to the detriment of

their productivity and job performance. Aside from productivity, other research has linked financial precarity to health problems, which have further implications for the employer's bottom line.³³ Addressing this crisis requires the combined efforts of the public, private, and philanthropic sectors.

From a public policy perspective, it is necessary to consider the responsibility of government in ensuring a minimum level of financial security in the population. The current approach places crucial social benefits at the discretion of employers, who are increasingly shifting responsibility onto individuals. Yet as our research shows, this system is not beneficial to anyone involved. From a business perspective, employers have an array of tools at their disposal for reducing financial precarity among workers. These include paying livable wages with predictable hours and affordable benefits; adopting problem-focused interventions to address the financial struggles employees face; and monitoring the organization for precarity "hot spots" where workers and the organization may be at particular risk. Our research suggests that these interventions can be effective at reducing financial precarity while also boosting productivity and organizational performance.

The philanthropic community has been and can continue to be a catalyst for solutions. For example, Commonwealth is an NGO that works with industry to encourage employers to make workers' financial security a specific goal, and pilots interventions aimed at increasing savings, assisting nontraditional workers, and addressing the challenges of income uncertainty. The Center for Economic and Policy Research (CEPR) seeks to inform changes in policy and practice by providing rigorous analysis of economic trends and their social implications for employees. For example, research by CEPR co-director Eileen Appelbaum and sociologist Ruth Milkman shows the significant benefits and negligible costs of employers' offering paid sick leave to employees.³⁴ There are also many behavioral science initiatives that introduce "nudges" to help employees and others make better financial decisions. In this vein, behavioral economists Shlomo Benartzi and Richard Thaler offer a good example: They have developed a successful program they label "Save more tomorrow," which, to date, has auto-enrolled millions of participants in retirement savings that are pegged to future increases in earnings.³⁵ Philanthropists have also supported the interventions aimed at addressing financial precarity that my colleagues and I have developed. Such initiatives offer evidence-based changes that can be brought to scale by employers and policymakers. They are crucial beacons in demonstrating what is possible.

We are far from powerless in addressing financial precarity. Although the necessary changes I have outlined here are not quick fixes, their implementation will leave all of us better off. ■

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