The Association Between High Levels of Mortgage Debt and Financial Well-Being in Old Age: Implications for the Financial Education Field

Research Brief

Final

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Executive Summary

Over the last few decades the share of homeowners age 65 and older with mortgage debt has doubled, while the typical amount of outstanding debt relative to home values among those with this debt has tripled. Older homeowners still paying off mortgage debt face high rates of housing cost burdens (paying more than 30 percent of income for housing). Given that indebted homeowners have less housing equity to tap for critical needs and face the ongoing risk of foreclosure, it might be expected that higher mortgage debt levels would create lower levels of financial well-being among these individuals.

This brief uses both descriptive and multivariate analysis to examine the relationship between the incidence of mortgage debt and housing cost burdens with financial well-being for the population of older adult homeowners in the U.S. using the 2016 National Financial Well-Being Survey. In addition, the study assesses the association between the use of mortgage debt among older adults and measures of financial skill, knowledge, planning, and savings habits. Our research finds that:

- The use of mortgage debt in older adulthood is associated with lower levels of financial well-being even after controlling for many economic and demographic characteristics of respondents. Similarly, older-adults with high levels of mortgage debt are more likely to be financially insecure (defined as having a financial well-being score under 50, which is associated with an elevated risk of material hardship.)
- This association between higher mortgage debt and lower financial well-being appears to be independent of the additional housing cost burden associated with having a mortgage, as holding a mortgage has a detrimental effect on well-being above and beyond the effect of additional out-of-pocket housing expenses.
- Respondents with higher levels of financial skill and those with a habit of savings are less likely to carry mortgage debt into older adulthood even after accounting for financial and demographic characteristics that differ between those with low and high levels of mortgage debt. However, no statistically-significant association was found between financial knowledge and planning and having high levels of mortgage debt.

These findings provide support for the hypothesis that higher levels of mortgage debt late in life impair financial well-being both by increasing housing cost burdens and, independently, by reducing housing equity and the security it can provide. The findings suggest possible avenues for policy including expanding access to financial education aimed at improving financial skills and instilling a habit of savings that are associated with lower levels of mortgage debt.

1. Background

Between 1989 and 2016 the share of homeowners age 65 and over with mortgage debt doubled from 20 to 41 percent while the outstanding loan-to-value ratio of those with such debt tripled from 13 to 39 percent.[1] Carrying mortgage debt late in life is associated with a much higher incidence of housing cost burdens, where households spend more than 30 percent of their income on housing. In 2017, among owners age 62 and over only 16 percent of those who owned their homes free and clear had cost burdens, compared to 40 percent among those still paying off a mortgage.[2] Spending a disproportionate share of income on housing is also strongly associated with cutbacks in spending on food, health care, and transportation, with important consequences for overall well-being.[3]

High levels of mortgage debt also limit the availability of housing equity, which is often tapped late in life in response to a health crisis or loss of a spouse.[4]Furthermore, having unmanageable mortgage debt raises the risk of losing the home and at least some share of accrued equity to foreclosure, further impairing financial security.[5] On the other hand, the rise in mortgage debt may also represent appropriate financial choices to increase housing consumption or to allocate financial resources across other debt and investment opportunities.

While there has been a variety of research documenting the rise of mortgage debt among older homeowners, there has been little assessment of whether the use of high levels of debt late in life are associated with impairment of financial well-being.[6] An analysis by the Consumer Financial Protection Bureau (CFPB) documented that older homeowners with mortgages had lower levels of financial well-being but the study did not employ multivariate analysis to assess this association while controlling for other financial and demographic factors.[7] This study seeks to address this gap in the literature by employing a multivariate analysis of the association between high levels of mortgage debt and financial well-being.

Assuming that higher levels of mortgage debt have a deleterious effect on financial well-being, an important question for policy is whether there is an association between financial skill,

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[1] Joint Center for Housing Studies, "Housing America's Older Adults 2018: A Supplement to the State of the Nation's Housing Report," (September 2018), available at https://www.jchs.harvard.edu/sites/default/files/Harvard_JCHS_Housing_Americas_Older_Adults_2018_1.pdf

[2] Joint Center for Housing Studies, "The State of the Nation's Housing 2018," (June 2018), available at https://www.jchs.harvard.edu/sites/default/files/Harvard_JCHS_State_of_the_Nations_Housing_2018.pdf

[3] Christopher Herbert, Alexander Hermann, and Daniel McCue, "Measuring Housing Affordability: Assessing the 30 Percent of Income Standard," (2018), available at https://www.jchs.harvard.edu/sites/default/files/Harvard_JCHS_Herbert_Hermann_McCue_measuring_housing_affordability.pdf.

[4] James Poterba, Steven Venti, and David A. Wise, "What determines end-of-life assets? A retrospective view," (October 2015), available at https://www.nber.org/papers/w21682.pdf

[5] Lori A. Trawinski,"Nightmare on main street: Older Americans and the mortgage market crisis," (August 2012), available at https://www.aarp.org/content/dam/aarp/research/public_policy_institute/cons_prot/2012/nightmare-on-main-street-AARP-ppi-cons-prot.pdf

[6] See for example J. Michael Collins, Erik Hembre, and Carly Urban, "Exploring the Rise of Mortgage Borrowing Among Older Americans,"(2018) available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3171777 and Consumer Financial Protection Bureau, "Snapshot of older consumers and mortgage debt," (2014) available at https://files.consumerfinance.gov/f/201405_cfpb_snapshot_older-consumers-mortgage-debt.pdf

[7] Consumer Financial Protection Bureau, "Financial Well-being of Older Adults," (2018), available at https://files.consumerfinance.gov/f/documents/bcfp_financial-well-being-older-americans_report.pdf.

knowledge, or practices and lower levels of such debt. These relationships would imply opportunities for consumer education to reduce the use of debt. While the existing literature does examine the relationship between financial planning and net worth, including the level of home equity, there are no existing studies that specifically examine how financial skill, knowledge, and practices are associated with the use of mortgage debt late in life.[8] This study also seeks to address these open questions.

More specifically, the questions addressed in this study are the following:

- How do high levels of mortgage debt relate to a household's financial well-being among older homeowners?
- Is housing affordability associated with the financial well-being of older-adult homeowners?
- To what extent does the incidence of high levels of mortgage debt and the resulting affordability challenges result in financial insecurity for older adult homeowners?
- Do homeowners with high amounts of mortgage debt exhibit lower levels of financial knowledge, skill, or planning relative to homeowners with low levels of mortgage debt?

2. About the Study

This study employed multivariate regression analyses to isolate the association between financial well-being and both mortgage debt and housing cost burdens. To do so, we focus on the financial well-being of individual respondents age 62 and over, controlling for their personal and household characteristics.

This analysis used the CFPB's National Financial Well-Being Survey (NFWBS), a survey conducted in 2016 of 6,394 adults meant to be representative of the general population, including 2,253 respondents age 62 and over. We restrict our sample of interest to older adult homeowners and after accounting for nonresponses to relevant survey questions we examine a sample of 1,035 respondents.

In our study, our key variables of interest include:

- **Financial well-being**: A continuous measure of financial well-being derived from a 10-item survey scale developed by the CFPB. According to the CFPB, financial well-being is a "state of being wherein a person can fully meet current and ongoing financial obligation, can feel secure in their financial future and is able to make choices that allow them to enjoy life."[9] The scale itself ranges from 0 to 100, with higher scores indicating greater financial well-being.

[8] See, for example, Annamaria Lusardi and Olivia Mitchell, "Baby Boomer Retirement Security: The Roles of Planning, Financial Literacy, and Housing Wealth." Journal of Monetary Economics 54 (2007) and Annamaria Lusardi and Peter Tufano, "Debt Literacy, Financial Experiences, and Overindebtedness." (2009), available at https://www.nber.org/papers/w14808.pdf

[9] Consumer Finance Protection Bureau, 2015. *Measuring financial well-being: A guide to using the CFPB Financial Well-Being Scale*.

- **High mortgage debt**: The NFWBS captures whether a homeowner has mortgage debt of less than $50,000, or $50,000 and greater. Respondents with mortgage debt of $50,000 or more are considered to have high levels of debt.
- **Housing costs and affordability**: The monthly housing costs of the homeowner or, alternatively, the ratio of housing costs to household income to account for differential ability to pay for housing that varies with income.
- **Financial skill, knowledge, planning, and savings habits:** A series of measures of financial acumen and habits are captured by the NFWBS and used in the study to assess their association with high levels of mortgage debt.

This study also accounts for a number of other factors that might affect a respondent's financial well-being and its use of mortgage debt, including household income, the amount of savings, home value, education level, labor force attachment, health status, marital status, gender, racial/ethnic minorities, whether they financially support children, geographic region, and whether they live in a metropolitan area.

3. Findings

Our findings support our hypothesis that higher levels of mortgage debt are associated with lower financial well-being among older adults and that this association holds even after accounting for housing costs. The results also find some association between financial skill and a habit of savings and lower levels of mortgage debt, pointing to potential policy levers for reducing mortgage debt among older homeowners.

3.1. *Older adults with high levels of mortgage debt have lower levels of financial well-being*

Holding high levels of mortgage debt is associated with a nearly 5-point decrease in the level of financial well-being, even after accounting for the respondent's level of income, savings, self-reported health, marital status, and other characteristics of the homeowner. While this 5-point decrease might seem small, it results in a substantial increase in the likelihood that older-adult homeowners are financially insecure (defines as those with financial well-being scores of 50 or under).[10] In our preferred model, having high levels of mortgage debt is associated with a 17 percent chance of being financially insecure, if you assume otherwise average homeowner characteristics. By comparison, if this same homeowner had low levels of mortgage debt, they would have only a 9 percent chance of being financially insecure.

[10] We use a financial well-being score of 49 and under as a threshold for determining whether an individual is financially insecure. This coincides with financial well-being score ranges that are very low (0–29), low (30–37), and medium low (38–49) on the test of well-being. Such respondents are more likely to have difficulty covering their monthly expenses. See Consumer Financial Protection Bureau, "Getting started with measuring financial well-being: A toolkit for financial educators." (January 2019), available at https://files.consumerfinance.gov/f/documents/cfpb_financial-well-being_toolkit.pdf.

3.2. The association between mortgage debt and financial well-being is about more than just housing costs

Homeowners with high levels of mortgage debt tend to have higher housing costs than those with little or no mortgage debt. This plays some role in their lower financial well-being. Indeed, each additional 10 percent of income spent on housing is associated with a 1-point reduction in well-being for older adult homeowners. However, this relationship, while statistically significant, is small in magnitude. Furthermore, even controlling for housing costs, there is an independent relationship between high levels of mortgage debt and lower financial well-being.

As a result, we conclude that increased housing costs alone do not drive differences in well-being between homeowners with high and low levels of mortgage debt. Instead other factors, including the potential psychological burdens of carrying high levels of housing debt, the risk of foreclosure, or the more limited ability to tap home equity in the future, are independently connected to well-being.

3.3. Improving financial skill and instilling saving as a habit might make older adults less likely to carry high levels of mortgage debt

Homeowners with greater financial skill and who claim saving is a habit are both less likely to carry high levels of mortgage debt into older adulthood. The association with financial skill, as measured by the CFPB financial skill scale, is statistically significant, but the magnitude of the effect is relatively small. An increase in the financial skill score of 11 points is associated with a 5-percentage point reduction in the likelihood of having high mortgage debt for the average homeowner. Moreover, habitual savings for the average older-adult homeowner is associated with an even larger 14-percentage point decrease in the likelihood of carrying high levels of mortgage debt. This is true even after accounting for differences in income, home value, location, and other economic and demographic characteristics that differ between those with low and high levels of mortgage debt. Moreover, this effect is as large for homeowners with very little savings as it is for those with considerably more savings, indicating that the willingness and desire to save has some effect on the incidence of high debt independent of the ability to save.

4. Conclusion

The continued rise in the incidence and level of mortgage debt among older-adult homeowners over the past several decades has been a major concern for housing analysts and policymakers. Older-adult homeowners with mortgage debt are more likely to spend a higher share of their income on housing, forcing difficult tradeoffs in spending with other necessities such as food and health care. These concerns are only compounded given the continued growth in the population of older adults over the next several decades.

This study validates a number of these concerns, finding a strong link between the incidence of high mortgage debt and lower financial well-being (and a greater likelihood of financial insecurity), even when holding household income, savings, home value, and other household economic and demographic characteristics constant. Some, but not all, of this relationship is explained by the corresponding increase in housing costs associated with mortgage debt. Still, holding mortgage debt is found to have an independent negative relationship with well-being.

This study also proposes potential mechanisms for alleviating the burdens of high levels of mortgage debt. Habitual savings and, to a lesser extent, financial skill, are both associated with a meaningful decrease in the likelihood that older-adult homeowners have high levels of mortgage debt. Financial education geared towards encouraging savings and improving financial skill, both before and during older adulthood, are possible remedies to mitigate the increase in high levels of mortgage debt for this population.

Further research should shine a light on the timing and structure of these financial education programs. Additional questions for researchers that would clarify, extend, and fortify the findings of this research include: (1) Does the mere incidence of mortgage debt matter more so than the level of mortgage debt? (2) Does the relationship between mortgage debt and financial well-being vary with age? If so, at what age (and what amount) is mortgage debt most associated with lower levels of financial well-being? and (3) By what mechanism(s) does the incidence of high mortgage debt, independent of affordability, most effect well-being?