European Commission

SCIENCE FOR POLICY BRIEFS

Financial buffers of households in the wake of the COVID-19 crisis*

Headlines

- The availability of financial buffers can be used to assess the vulnerability of households following lockdown measures and potential income losses.
- In many EU countries, the fraction of households with savings of less than 1000 euros is at least 20% of the population.
- In most EU countries, more than half of the households have liquid savings worth less than two months' income.
- Workers in the retail and tourism ("accommodation and food") sectors are particularly vulnerable as they have less than one monthly income as a financial buffer. This will most likely affect Southern European countries where tourism constitutes a larger share of GDP.
- Income support is particularly important for those households that have insufficient financial buffers.

Financial buffers and COVID-19

Following the COVID-19 crisis, policy makers in almost all member states have implemented lockdown measures, limiting economic and social activities. This note provides first evidence of households' financial capabilities to endure a lockdown and face potentially substantial income losses.

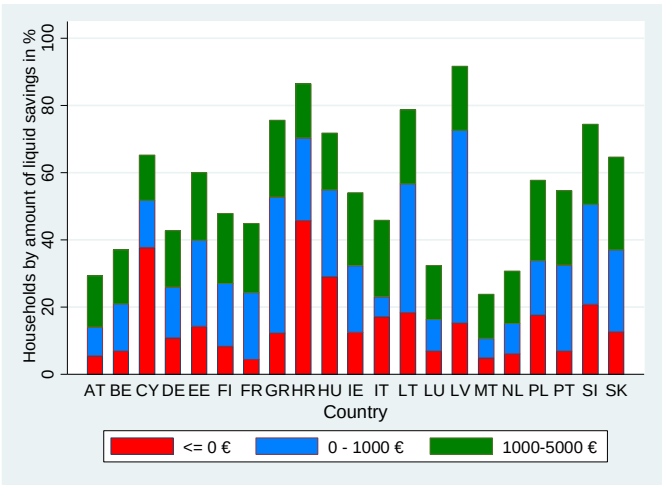
For our analysis of financial buffers, we consider

- the share of households with less than 1000 euros (or equivalent) in liquid savings across countries;
- how this share is distributed across income and age;
- the size of the buffer stock of savings in terms of gross monthly income that households have at their disposal and its distribution across income and age;
- the sectors of the economy in which household heads are employed.

The availability of liquid savings is an essential buffer in case of income or job loss. For example, having a non-permanent contract or variable earnings constitute a risk to an employee's income stream that can be mitigated by saving. Using their savings, households can also maintain levels of consumption similar to those preceding the lockdown measure and can fulfil predefined expenditure commitments such as rents and existing mortgages. Financial buffers also play a key role in reducing the risk of falling into poverty. Therefore, liquidity can also be an important determinant of the social acceptance of the confinement measures.

Figure 1 displays the distribution of (ppp-adjusted) net savings across the countries in the data set.

Figure 1: Households by amount of liquid savings in %



Source: Own calculations based on HFCS microdata, wave 3.

*Julia Le Blanc, JRC, 2020

Joint Research Centre

Quick guide

The evidence for this note is provided by the recently published 3rd wave of the **Household Finance and Consumption Survey**, conducted by the national central banks of the Eurosystem and a number of statistical institutes. The HFCS collects household-level data on households' finances and consumption for all euro area countries and Croatia, Hungary and Poland. The fieldwork took place for most countries in 2017. Anonymised microdata from the third wave was made available to researchers in March 2020. The 2017 data for Spain are not published yet.

Our measure of **household financial buffers** is net liquid assets. Liquid assets are assets held in deposits, mutual funds, bonds, non-self-employment assets, traded shares and managed accounts. Credit card debt and overdrafts are subtracted for the final measure of net liquid assets (or savings) that can be accessed immediately for consumption. The amount of assets refers to the year 2017. To account for different purchasing powers across the countries in the sample, nominal values were ppp-adjusted.

As incomes are taxed differently across countries, the relevant income measure would ideally be net income. However, **household income** in the HFCS is recorded as gross annual income, including all employee income, self-employment income, rental income, income from financial assets, income from pensions, and income from social transfers. To arrive at the measure of monthly incomes saved, annual household income is converted to monthly income. Income refers to the year 2016.

For the **sector of employment**, the HFCS provides NACE codes on level 1 for all employed and self-employed individuals. As the analysis of the impact of the lockdown on households' financial buffers can only be done on a household level in this data set, we use as reference the sector in which the household head is employed. The sector of employment of the household head therefore approximates the household's main source of income. Due to the macroeconomic significance and varying sample sizes for some countries of the sample, some sectors are aggregated. We report the following sectors: Agriculture (A), Manufacturing (C), Construction (F), Wholesale and Retail Trading (G), Transportation and Storage (H), Accommodation and Food Services (I), Professional, scientific and technical activities; administrative and support service activities (M-N), Public administration, defence, education, human health and social work activities (O-Q), Arts, entertainment and recreation; other service activities; activities of household and extra-territorial organizations and bodies (R-U).

The red part of each bar displays the fraction of households with zero or negative liquid savings,[1] the blue part is the fraction with positive savings but less than 1000 euros, and the green part refers to the fraction of households with between 1000 and 5000 euros. The remaining share up to 100% refers to savings of more than 5000 euros. Liquid savings have been PPP- adjusted to reflect the different price levels across countries.

In most countries, the fraction of households with savings of less than 1000 euros is at least 20% of the population; the fraction of households with zero or negative liquid assets is particularly sizeable in Italy and Cyprus and in Central and Eastern Europe.

A sizeable share of households with low amounts in liquid assets makes a prolonged lockdown without important revenue support unsustainable.

Households' savings in terms of monthly incomes

The previous results suggest that a sizeable part of the population would have difficulties to withstand a prolonged period without earnings. However, these facts do not provide information about how long the period could be.

Households' liquid savings as a fraction of monthly (gross) income refers to the number of monthly incomes that households have saved[2]. It gives an indication of how long households can keep up their living standards in case of a complete loss of income.

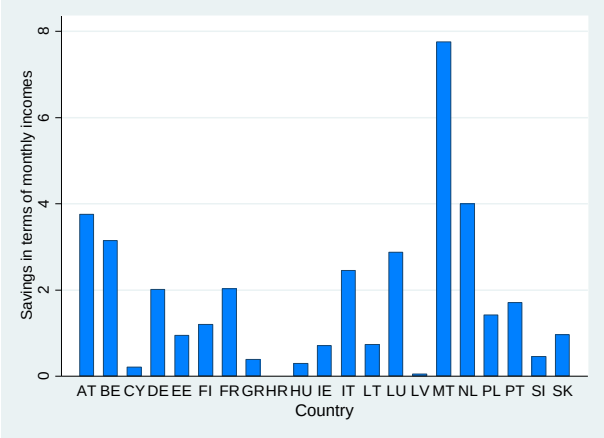
In most countries, the median number of monthly incomes saved is less than two months of (gross) income but there is heterogeneity across countries in the sample – see Figure 2. In particular, in

[1] The fraction of households with negative savings refers to those households whose credit card debts or whose overdrafts are higher than their savings in current accounts or other liquid forms of saving at the time of the survey.

[2] This indicator is calculated at the household level, i.e. for each household we divide the amount of liquid savings by monthly income. To aggregate to the country level, we take the median number of monthly incomes saved.

some countries strongly hit by the Great Recession and in the Central and Eastern European countries, financial buffers are small.

Figure 2: Median number of monthly incomes saved



Source: Own calculations based on HFCS data, wave 3.

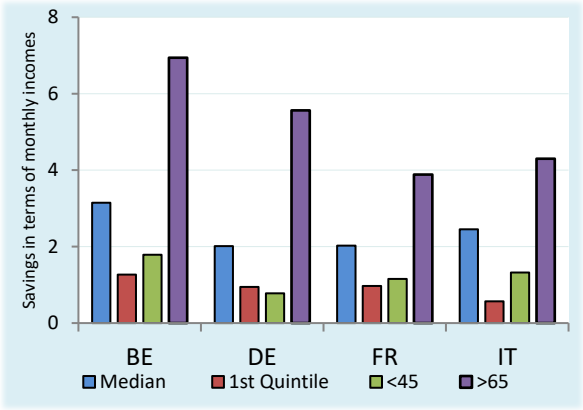
Figure 3 displays more detailed analysis for a selection of countries and highlights potential vulnerabilities by subgroups. For comparability, the blue graph displays the stock of savings in terms of the median number of monthly incomes already shown in figure 2. Households in the lowest income quintile have savings worth only about one month of income, and in the case of Italy of only one half month.

In many countries, this group holds hardly any buffer. In the absence of appropriate policies the poorer part of the population cannot maintain the current levels of consumption.

Another vulnerable part of the population consists of the younger age groups who have not yet been able to accumulate financial buffers and do not benefit from a constant stream of pension income. The median number of monthly incomes saved increases monotonically with age until age 55, revealing that younger households have accumulated fewer assets in terms of income or have their savings in an illiquid form, typically a mortgaged house.

Indeed, younger households in all countries have fewer monthly incomes saved than their older counterparts (shown in the last bar).

Figure 3: Distributional aspects of savings for selected countries



Source: Own calculations based on HFCS data, wave 3.

Sectoral decomposition

Finally, resilience to the lockdown can be considered from the point of view of different sectors. Different sectors of the economy will be unevenly affected by the lockdown measures, both as a result of the length and intensity of the lockdown and of the exposure of these sectors to the crisis. If vulnerable groups are more likely to work in those sectors, the distributional impacts of the COVID-19 crisis can be larger than average for them.

The analysis concentrates on those sectors that, along with high vulnerability to the virus and high proximity of workers at the workplace, have a sizable impact on the overall economy and/or are expected to face a sharp fall in demand.[3] We consider agriculture, manufacturing, construction, wholesale and retail trade, transportation and storage as well as the accommodation and food services sector. The remaining services sectors are pooled together in three groups: professional and scientific activities and support services, public administration including education, defence and arts, entertainment and all other services. For the sake of exposition, we consider the aggregation of countries, but country-level results are available and country-specific comments are added when necessary.

In the EU[4], only a small fraction of employees (5%) works in the agricultural sector. Around 6% of work in construction followed by Wholesale and Retail Trade (14.6%) and Manufacturing

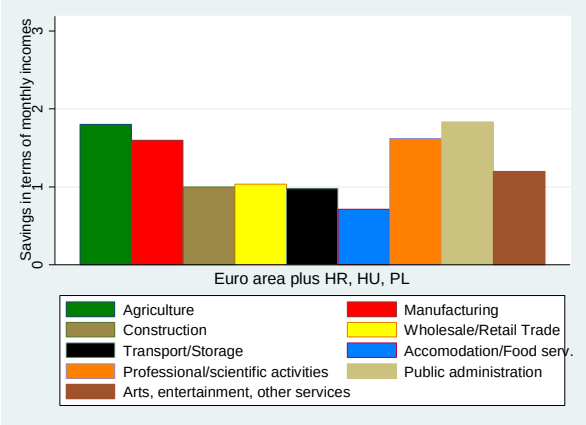
[3] See INAIL (2020) (in Italian): https://www.inail.it/cs/internet/comunicazione/pubblicazioni/catalogo-generale/pubbl-rimodulazione-contenimento-covid19-sicurezza-lavoro.html.

[4] See Eurostat: National Accounts Employment Data by Industry.

(14.7%). The Accommodation and Food services sector is small with an employment share of 4.8% with the exception of Austria, Cyprus, Greece, Italy, Ireland, and Portugal where more than 8 % of employees are employed in this sector. The Transportation and Storage sector (5.10%) is equally small. All remaining households work in the remaining service sectors.

Figure 4 displays for the EU countries in our data set how different households' financial coping capacity is distributed across sectors. The figure shows net liquid savings of households in terms of monthly incomes.

Figure 4: Median number of monthly incomes saved by sector of employment



Source: Own calculations based on HFCS data, wave 3.

Households working in Agriculture might be relatively unaffected, as they have on average 2 months of savings in most countries. Additionally, the agricultural sector is mostly unaffected by lockdown measures. Finally, the disruption in international trade might to some extent contribute to supporting the sector as countries might prefer self-sufficiency.

Workers in manufacturing have relatively sizeable buffers (mostly 1-2 months of earnings), but the effect of the lockdown could be substantial due to the fall in demand in this sector. Also, households working in Wholesale and Retail Trade have on average 1 month of gross household income saved but might suffer from the lockdown measures and the closures of shops.

The vulnerability to the COVID crisis is more serious for construction workers and those employed in the transportation and storage sector, whose savings are less than one month of gross income and whose earnings are often not guaranteed in periods of inactivity. Construction workers appear particularly exposed also looking at the Great Recession.

Workers in the Accommodation and Food sector, due to a higher variability and seasonality of earnings, might be expected to have higher than average savings. The data shows the opposite. Households whose main earner works in the Accommodation and Food services sector have the smallest buffer stocks saved.

Overall, there is a high degree of heterogeneity of households' vulnerability to a persistent income loss across sectors. On average, construction, accommodation and food services and the trade sector will be most affected by a lockdown. A prolonged lockdown may not be sustainable for these sectors unless revenue support measures are adopted to ensure that the inactivity period does not lead to a permanent loss of productive capacity and income.

Conclusions

The availability of liquid savings can act as an essential buffer in case of income or job loss. In most countries, the fraction of households with relatively low savings –either in terms of PPP-adjusted euro values or in terms of the number of monthly incomes- is at least 20% of the population. The fraction of households with zero or negative liquid assets is particularly sizeable in Italy, Cyprus and in Central and Eastern Europe.

Within countries, the lower income groups and the younger age groups are particularly vulnerable to being left without any assets as they have small buffer stocks of liquid assets.

Households working in construction, wholesale and retail trade and in the accommodation and food services sector have accumulated small financial buffers and might suffer from a lockdown of these sectors.

The conclusions are still only indicative. The assessment of the COVID-19 crisis across different countries is a complex endeavour, as it depends not only on the liquid resources available to the private sector, but also on the different provision of public services and on the generosity of pensions, on the degree of redistribution, on the presence of unemployment benefits and of other automatic stabilizers.