Financial Planning During Turbulent Times: Role of Household Wealth

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“How We Decide” by Jonah Lehrer

Two identical auctions at MIT for Boston Celtics basketball tickets - only difference is that in one must pay in cash – the other must pay with credit card

How did the bids compare? Average credit card bid twice that of cash bid. Yikes.
PFP Degree Programs

The vast majority of graduate degree programs in personal financial planning are not in business schools, but in schools of consumer science...

Curriculum sweet spot – blend behavioral and technical

That’s the plan today…
Application to Atlanta Metro

Georgia routinely is among the “leaders” in bankruptcy filings.

Characterization of Atlanta Metro…

  Sustained population and economic growth
  Entrepreneurship is strong – people are busy
  Well diversified local economy
  Steady appreciation of real asset values
  “New Money” mentality – movin’ up a level
Return to Behaviors

Experiment where participants have to remember either a *two* or a *seven-digit* number for subsequent use.

Along the hallway to complete the experiment, participants are given the choice of a fruit cup or a (decadent) piece of chocolate cake.

*Seven digit players take the cake.* If the rational brain is busy, the emotional brain can take over.
Behaviors and Experience

How does experience matter in a crisis?

The rational and emotional/intuitive brain can cooperate if neither is dominated.

Pilot of DC-10 flight that suffers complete loss of hydraulic power combines technical and emotional/intuitive power of brain.
Return to Technical Analysis

What is the value of a strong balance sheet?

Corporate perspective…Provides strategic options and the ability to survive difficult times.

Value is a combination of stock and flow

Often the stock of value (balance sheet) receives less attention than cash flow analysis…

Atanasov, Black, Ciccotello, and Gyoshev (2009)
Intersection – Personal Implications

Brain likes to get stuff now…pay later
Rational brain preoccupied with work…here comes the chocolate cake
New money brain has little experience with crises…

New money balance sheet…
Balance sheet built from recent appreciation of assets rather than accumulation or debt pay down.
In the 1990s, this was stock market appreciation
In the 2000s, this was real estate value appreciation
Lifestyle – “Status” Competition

Choose your house and your neighborhood…

Household furnishings to suit
Cars to suit
Schools for children to suit
Vacations to suit
Other “toys” to suit

Once struck, lifestyle costs are very sticky
Throw in a shock to revenue..high unemployment
Balance Sheet Issues

New money balance sheet strains to address income loss…and liquidity squeeze
Recent asset appreciation slows or reverses
Reduced lines of credit
Assets in tax-deferred (401k type) locations very expensive to access

New money brain has never seen anything like this before…complete loss of “hydraulics.”
Georgia Specific – Slowing Growth

Ten-county Metro Atlanta population growth for year ended April 2009 was about 25 K people

Smallest one-year growth since statistics began in 1990
Average growth per year since 2000 – 77 K people
Growth in the Georgia banking sector also slowing

But, with 4.1 M people (Apr 2009), Metro Atlanta population is greater than that of 24 states.
Bottom Line

Georgia is a new money region of the country that has had sustained economic growth over the last 20 years.

Slowing growth and increasing unemployment hit new money lifestyles hard both technically and behaviorally – e.g., GA, FL, AZ, CA

Like corporations, balance sheet strength matters for individuals and families.

Consider the benefits of building balance sheet strength through increased liquidity and reduced leverage.