Patterns and Obstacles to Financial Management

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This study investigated households' use of four recommended financial management practices and possible obstacles to using those practices. These four practices included budgeting, keeping records of expenditures, comparing the records to the budget, and estimating net worth. Data were collected from a sample of non-metropolitan households living in Kansas. Results indicated that keeping records of expenditures was the most common of the four practices, followed by budgeting, comparing records to the budget, and estimating net worth. All four practices were used by 37% of the sample. Respondents who did not use a practice were asked why they did not. Irregularity in income and expenses was the most frequently reported obstacle to budgeting. Respondents persistently reported that they "didn't need to" use the other three management practices. Implications for financial education are discussed.

KEY WORDS: consumer finance, family budgets

Both the popular and the academic literature on family finance consistently recommend four practices as essential prerequisites to effective financial management (Garman, Eckert, & Forgue, 1987; Gitman & Joehnk, 1990; Lang, 1988; Miller, 1988; Stauffer, 1988). The first of these practices is a budget, which shows anticipated income and expenditures, preferably over the course of a year. The second is some form of income/expense or cash-flow statement, which records in detail the income actually received and the expenditures made. A comparison

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of the income/expense statement to the budget is the third recommended financial management practice. The fourth is the preparation of a personal balance sheet, or estimate of household net worth.

Findings from recent surveys suggest that people do not use the recommended procedures, or at least not in the form prescribed. For example, a written budget is considered to be the most basic tool of financial management. Yet the research shows that only a small minority of households use a written budget. Rather, it appears that people make much more informal plans for spending their money. Beutler and Mason (1987) found that fewer than 10% of the respondents in their study had a written budget that covered the course of a year. Mullis and Schnittgrund (1982) reported that of the respondents who said they budgeted, the majority reported a "general idea" that guided their spending, rather than a written plan.

The literature suggests that people do try to keep track of their spending. Godwin and Carroll (1986) found that 73% of the husbands in their sample reported keeping "monthly records of expenditures." Whether such records take the form of detailed income/expense statements is open to doubt. Schnittgrund and Baker (1983) found that their respondents relied on checkbook registers, receipts, and memory to track expenditures. The literature also suggests that personal balance sheets are not widely used. In a study conducted by Lawrence, Carter, and Verma (1987), 31% of the respondents reported preparing an estimate of household net worth. Mueller and Hira (1984) reported that while 32% of their respondents prepared a balance sheet, another 35% reported that they had never calculated their net worth.

Findings such as these raise questions regarding families' approaches to managing their finances. This report attempts to answer three specific questions:

1. What proportion of households try to follow the recommended practices in some form?

2. What combinations of these practices are most prevalent?

3. What discourages people from using recommended practices?

Data and Methods

The data reported here were collected as part of a broader study designed to investigate the impact of selected financial management practices on the perceived and objective financial well-being of non-metropolitan households. Data were collected in Kansas using a two-stage cluster sample wherein non-metropolitan counties comprised the sampling frame for the first stage and residential telephone listings within those counties comprised the sampling frame for the second. Data were collected via mail questionnaires in the spring of 1984. Following the initial mailing, three attempts were made to contact non-respondents, in accordance with the procedures recommended by Dillman (1978). Of the 1,200 households sampled, 672 returned usable instruments.

Demographic characteristics of the sample are summarized in Table 1. The "typical" respondent was a married person in his or her late 40's, who had two years of post-secondary education, and whose total gross family income was between $20,000 and $25,000.

One would not expect the sample to closely parallel the demographic characteristics of the state in which it was collected, since metropolitan households were deliberately excluded from the target population. Comparison of the respondents to the 1980 Census information for the seven counties included in the sample indicated that people under 25 years old were under-represented and people between 45 and 64 were over-represented (Murray, 1984, p. 25). Married people were also disproportionately represented in the sample. Thus, the sample was more representative of mid-life and older married people than it was of the target population as a whole.

Respondents were questioned on their use of four recommended financial management practices: budgeting, record keeping, comparing the records to the budget, and preparing a balance sheet (estimating net worth). Respondents who used a procedure were asked additional questions regarding the degree of implementation; respondents who did not use a procedure were asked why they didn't, and chose their responses from a list of possible reasons plus a category of "Other: please describe."

Table 1
Demographic Characteristics of the Sample

	Percent[a]
Age	
19-24	6
25-44	39
45-64	34
65 and over	21
median = 48	
Education	
less than high school	18
high school	34
post-secondary	48
Marital status	
married	80
divorced	4
widowed	11
separated	<1
never married	5
Household size	
1 person	21
2 people	35
3 people	14
4 people	17
5 people or more	13
mean = 2.7	
Gross household income	
< $10,000	16
$10,000-$29,999	55
$30,000-$49,999	21
$50,000 or more	7
midpoint of mean category = $22,500	

[a]Percentages may not sum to 100 due to rounding

Use of Recommended Financial Management Practices

As shown in Table 2, keeping written records of spending was the most commonly used of the recommended financial management practices, reported by 91% of respondents. Within this group, 32% indicated they used canceled checks to record spending; 23% kept receipts for major purchases, and 23% kept receipts for monthly bills. The questions asked did not address the preparation of an income/expense or a cash-flow statement.

A budget, defined as a plan for spending and saving income, was the second most commonly utilized financial management practice in this study. Just over 80% of the sample reported having a budget. However, analysis of answers to the follow-up questions on this practice revealed that only 8% of the respondents with budgets said that their spending plan was mainly or entirely written; 54% said that their budget was both mental and written, and the balance of respondents with spending plans reported that their plan was mainly or completely mental. The majority of respondents took a very short-term approach to budgeting; only 16% said that their budget covered a year's time or longer, and another 24% said that their spending plan covered a period of "several months."

A little over two thirds of the respondents indicated that they compared their actual spending to their budget. Of these, 45% reported making the comparison on a monthly basis. Estimation of net worth was the least frequently used financial management practice in this study. Of the respondents who estimated net worth (50% of the sample), about 64% did so on a yearly basis.

Table 3 shows how families combined these practices to form their own financial management patterns. Over six in ten households used three or more of the recommended practices. The most common pattern was to use all four practices (37%), followed by the pattern which included all procedures except the estimation of net worth (21%).

Table 2
Percentage of Households Using Selected Financial Management Practices

Practice	Percentage Yes	Percentage No
Budgeting. Do you generally make some kind of a plan before spending your money?	82	18
Record keeping. Do you generally keep written records of what you've spent?	91	9
Comparing records to budget. Every so often, do you compare what you planned to spend to what you actually spent to see if any changes need to be made?	69	31
Estimating net worth. Every so often, do you estimate your household's net worth, that is, do you add up the value of everything you own, then add up all your debts, and compare the two in order to see how you're doing financially?	50	50

Many obstacles could deter people from using financial management practices. These practices require time; effort; some knowledge about the family's spending, assets, and debts; and sometimes cooperation among family members in sharing information. What do families see as the main reasons they do not use recommended procedures? As shown in Table 4, having "no choice about spending" and "irregularity in expenses and/or income" were the most often cited obstacles to budgeting. However, if the responses "income too unpredictable," "expenses too unpredictable," and "both income and expenses too unpredictable" are combined, 41% of those who reported an obstacle to budgeting cited irregularity in income or spending as an impediment. Households that did not keep written records of spending, and

Table 3
Percentage of Respondents Reporting Selected Patterns of Financial Management

Pattern	Percent[a]
Do nothing	2
Use one procedure	
. records only	10
. plan only	5
. estimate net worth only	1
Use two procedures	
. plan and record spending	12
. record spending and estimate net worth	5
. plan and estimate net worth	1
Use three procedures	
. budget, record spending, and compare spending to budget	21
. budget, record spending, and estimate net worth	5
Use all four procedures (budget, record spending, compare spending to budget, and estimate net worth)	36

Note. Anomalous cases were assigned to the most logical category. For example, people who indicated that they had no budget and no records, but compared the budget to the records, were categorized as "doing nothing."

[a]Percentages may not sum to 100 because of rounding.

households that did not compare spending to a budget most commonly reported they "don't need to."

Table 4
Perceived Obstacles to Using Recommended Financial Management Practices

Obstacle	Percent[a] Reporting
Obstacles to budgeting (n = 119)	
no choice about spending	25
both income and expenditures unpredictable	18
expenses too unpredictable	15
no need to plan	14
income too unpredictable	8
takes too much time	7
tried making a plan but couldn't stick to it	4
don't know how to plan	1
other	7
Obstacles to recording spending (n = 61)	
don't need to	39
can't get other people in the household to keep track of spending	21
takes too much time	12
don't know how	8
can't remember to record spending	3
other	16
Obstacles to comparing spending to budget (n = 204)	
don't need to	45
have no plan for spending	30
takes too much time	11
have no records of spending	3
other	11
Obstacles to estimating net worth (n= 328)	
never thought about it	47
don't need to	26
takes too much time	9
don't know how	5
other	14

[a] Percentages may not sum to 100 because of rounding. Respondents could indicate more than one answer; therefore the percentage shown is the percentage of total responses.

In contrast, almost half of those who did not estimate net worth reported that they simply had "never thought about it," but here again, the response "don't need to" was chosen by almost a fourth of those who did not estimate net worth.

Discussion

The findings regarding budgets are consistent with those reported in earlier studies (Beutler and Mason, 1987; Mullis and Schnittgrund, 1982). It appears that people do make some plans for spending their funds, but few households make budgets that are primarily written and few make budgets that cover more than a month or two. A plurality of the respondents in this study rely on their checkbook registers as a way of keeping track of expenditures, which was also true of the respondents in Schnittgrund and Baker's (1983) study. More respondents in this study than in earlier ones report estimating their net worth. The difference in results may be partly due to differences in the wording of the item, and partly due to the number of mid-life and older households in the study who may be considering the impact of net worth upon their financial status in retirement.

In terms of the three questions posed at the beginning of this report, the findings can be summarized as:

1. While almost all households in this study use at least one of the recommended financial management practices, only a minority use all four.
2. While households combine the practices into a variety of patterns, two patterns account for 57% of the respondents.
3. Lack of time and lack of knowledge are not commonly cited as obstacles to the use of recommended practices.

The findings raise questions regarding the extent to which households are willing to actually use (rather than endorse) the management practices that financial educators traditionally recommend. There appear to be some barriers to the adoption of recommended financial management practices that this study has not uncovered. Financial educators and advisors should ask themselves and their clients what other factors discourage households from using these practices.

One possibility suggested by the results concerns the regularity of income and expenses. In many households income and expenditures are not easily predicted over a year's time. For example, income may be hard to predict for self-employed business people, people whose work is seasonal, or wage employees whose hours fluctuate greatly. Similarly, households in which a member suffers a chronic or recurrent health problem may find it hard to accurately predict medical expenses. Financial educators may need to pay more attention to the challenge of budgeting under conditions of uncertainty.

The relatively high proportions of respondents saying they "don't need to" record spending, compare spending to a budget, or estimate net worth is somewhat puzzling. These respondents may in fact be indicating that they see no value in engaging in these practices. The fact that almost half the respondents who did not estimate net worth say they "never thought about it" suggests that people need more information about this financial management practice.

The results of this study pose at least two challenges for financial educators and researchers. The first is to better understand the factors that discourage households from using recommended financial management practices. The second is to develop ways to help households overcome those obstacles.

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