

## What's Your Financial Health Score?

*Can a 5-question test predict how wealthy you will become?*

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**In the future, will you become wealthier or poorer?** Who knows, right? It seems like you would need a crystal ball to really answer that question given life's up and downs. What if the answer is right in front of you? What if you can determine it from your present financial behaviors?

**Two economists present a brief questionnaire – and an audacious claim.** The Center for Household Financial Stability at the Federal Reserve Bank of St. Louis published an article titled “Five Simple Questions That Reveal Your Financial Health and Wealth.” The authors, William Emmons and Bryan Noeth, argue that your answers to these questions can effectively predict your financial future.<sup>1,2</sup>

Q: Did you save any money last year?

Q: Did you miss any loan or mortgage payments in the past year?

Q: Did you have a balance on your credit card after the last payment was due?

Q: Do liquid assets make up at least 10 percent of the value of your total assets?

Q: Is your total debt service (i.e., the cash you devote each month to paying principal and interest) less than 40 percent of your income?<sup>1</sup>

The Federal Reserve has actually asked these questions of consumers for decades as part of its Survey of Consumer Finances. Studying the eight SCFs conducted from 1992-2013, Emmons and Noeth looked at the answers respondents provided to these questions and the level of personal wealth they reported. Their assertion: “In summary, good financial health – as measured by our simple five-question scorecard – is highly correlated with the accumulation of wealth.”<sup>2</sup>

As part of their research, Emmons and Noeth scored the answers. A financially positive answer to a question was assigned 1 point; a financially negative answer, 0 points.<sup>2</sup>

The average total score (across more than 38,000 households) was 3.01. The highest average score to a question was 0.91 (the one about debt load being less than 40 percent of income) and the lowest average score to a question was 0.27 (the one about the percentage of liquid assets among total assets).<sup>2</sup>

**There was a surprising conclusion.** The authors found that education was no reliable indicator of personal wealth. When it came to being rich or poor, well-educated individuals had no leg up on lesser-educated individuals.<sup>2</sup>

**What's your score?** If you are able to successively answer the above questions with “yes,” “no,” “no,” “yes” and “yes”, your household is probably in pretty good financial shape – or better. In simple terms, those answers would get you a 5.0.

**Here's the bottom line.** If you save money consistently and maintain a good cash position, if you make loan and mortgage payments on time and pay off 100 percent of your credit card debt each billing cycle, if you avoid debts that put a strain on your budget ... congratulations. You are doing the right things on behalf of your financial life and promoting your chances to build wealth.

If you'd like to see the precise methodology the researchers used and their definition of a "positive" and "negative" answer for each question, you can go online and download Issue 10 of the St. Louis Fed publication *In the Balance* (which contains the article and the scorecard) at [stlouisfed.org/publications/itb/](http://stlouisfed.org/publications/itb/).

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**Citations.**

1 - [stlouisfed.org/newsroom/displayNews.cfm?article=2390](http://stlouisfed.org/newsroom/displayNews.cfm?article=2390) [12/15/14]

2 - [stlouisfed.org/publications/pub\\_assets/pdf/2014/In\\_the\\_Balance\\_issue\\_10.pdf/](http://stlouisfed.org/publications/pub_assets/pdf/2014/In_the_Balance_issue_10.pdf/) [12/14]