Are Poverty and Wealth Inequality Financial Capability Problems at Their Roots?

Bringing Income, Assets, and Financial Literacy Under One Umbrella

It is my observation that different policy proposals, groups of academics, and practitioners have treated income and wealth inequality primarily as an institutional problem (i.e., inadequate plumbing), a lack of wealth problem (i.e., not enough water), or a lack of financial literacy problem (i.e., inability to utilize water for growth and development).I view all three of these issues together under the umbrella of financial capability which I suggest is one of the root issues when it comes to reducing poverty and wealth inequality.

Zheng and I (2023, Nov.) have posited that to be financially capable, children must have access to financial institutions (such as Children's Savings Accounts or CSAs), assets (such as Baby Bond like deposits), and financial literacy (such as financial education training). Therefore, a financial capability approach to poverty is different from income policies whose primary goal it is to make sure families have enough money to meet basic needs. It is also different from an asset approach whose primary goal is to provide children with enough assets to reduce wealth gaps or serve as reparations for past and, quite frankly, continuing wrongs.

From a financial capability perspective, solving poverty is not mainly an issue of feeding, clothing, and sheltering children. Nor is solving wealth inequality mainly a problem of transferring wealth to families to reduce the wealth gap. Both are important for equipping children with what they need to become financially capable, but they are not sufficient on their own. In short, what I am suggesting is that the root cause of poverty and wealth inequality is lack of financial capability. If a goal of social welfare policy is to make children financially capable, then ending poverty and wealth inequality would be byproducts not the primary goals of social welfare policy.

In this way, a financial capability perspective is reflected in the saying, "give a person a fish, and you feed them for a day. Teach a person to fish, and you feed them for a lifetime". However, teaching in the context of financial capability emphasizes experiential learning which means inclusion in financial institutions and having access to income and assets are necessary parts of learning.

However, a part of what keeps some people from embracing transfers of income and wealth is the fear that it will only lead to the need for more transfers down the road. I am suggesting that this is more likely when children are not given access to all the tools, they need to become financially capable people. And so, when they do not have access to plumbing and water as well as the financial knowledge on how to use them to produce new assets (i.e., when they are not financially capable), if they get out of poverty, they might be more likely to fall back into poverty shortly after the programs end. Individually, plumbing, water, and financial literacy can be powerful tools for treating symptoms associated with poverty and wealth inequality such as eliminating hunger, increasing wealth, and reducing bad credit scores. However, they might not be as effective at addressing the underlying disease that is causing the symptoms to surface in the first place, lack of financial capability. Because they cannot produce assets on their own, once they exhaust what has been given to them (i.e., eat all the fish), they might end up needing more to be given to them. If not, hunger, wealth inequality, and lack of financial knowledge return creating seemingly endless cycles of poverty among some groups. So, yes, a policy that focuses on anyone of these strategies might be effective at reducing symptoms for a time, and data can be produced showing this, but because they are not able to attack the root cause, the symptoms might simply return over time.

Generally, the CSA movement has been associated with the effort to create the plumbing so that everyone can have access to water, the Baby Bonds movement (probably the Reparations movement as well) to supplying enough water to allow for growth and development, and the financial education movement with assuring children have enough financial knowledge to be able to use the plumbing and water to become producers of assets for their own growth and development. You cannot get to financial capability without each one of these, so these efforts have been vitally important to making a financial capability approach possible. It seems to solve poverty a financial capability framework is needed that brings all three poverty and wealth alleviation strategies under one umbrella. Shifting the conversation from we need this one or that one to we need this set of policies each equally important to achieving the goal of equipping children to produce their own assets. A byproduct of such an approach might not only be the reduction of poverty and wealth inequality, but the building of a coalition big enough and strong enough to turn proposals into legislation.

https://aedi.ssw.umich.edu/sites/default/files/documents/Blog/CSA_Umbrella.pdf

[1] Elliott, W. and Zheng, H. (2023, Nov.). What if education isn't the great equalizer? Reimagining financial aid from a financial capability perspective, the role of children's savings accounts and assets. University of Michigan, School of Social Work, Center on Asset, Education, and Inclusion (AEDI). https://aedi.ssw.umich.edu/sites/default/files/documents/Reports/unequal-returns/unequal-returns-full-report.pdf

To learn more about how the financial capability perspective of poverty and wealth inequality can be used to help children become producers of wealth and why it is important see the following report:

What if Education Isn't the Great Equalizer? Reimaging Financial Aid from a Financial Capability Perspective, the Role of Children's Savings Accounts and Assets

You can find the report at: https://aedi.ssw.umich.edu/unequal-returns-on-degree.