

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



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FORWARD

In this report we propose a new model of financial aid based on the financial capability perspective as a strategy for strengthening the return on degree and empowering education to become the great equalizer it was meant to be. According to M. S. Sherraden (2013), financial capability consists of both one's ability to act (i.e., financial literacy which consists of their financial knowledge and skills) and the opportunity to act (i.e., financial inclusion). However, we suggest that the current understanding of financial capability, while extremely important, is limited because it does not sufficiently account for the role of asset ownership in determining children's financial capability. In accordance with Sen's (1999a, b) financial capability perspective, we suggest when people own assets the corresponding characteristics of the assets increase their opportunity for being able to use those assets to accumulate more assets, and in turn increase the amount of return they can receive on their degree. As such, they are an integral part of what it means to be financially capable.

Based on this understanding of financial capability, we articulate a model of financial aid for the purpose of strengthening the return on degree that relies heavily on Children's Savings Account. Unlike traditional small-dollar CSAs, we propose a large dollar model of CSAs like what Senator Bob Casey has proposed in his 401 Kids Savings Account Proposal. The amount of the federal investment would be in line with what it would cost to pay for a four-year degree at a public university or Senator Corey Bookers Baby Bonds proposal. To help children pay for college while successfully strengthening the return on degree, we also suggest children need asset disbursements at two different time points: at age 18 when they have to pay for college, and at age 24 when they launch into independent living.

The financial capability model of financial aid proposed in the report consists of the following components:



- **Financial Literacy**

- Financial literacy training K-12
- Financial literacy training in Postsecondary Education

- **Financial Inclusion**

- Automatically Open Childrens Savings Accounts (CSA) for all children at birth

- **Asset Ownership**

- Initial deposit by federal government of \$1k with additional deposits of \$2k per year up to age 18
 - Progressive
 - Phase out deposits based on federal poverty level (FPL) (e.g., 100% of FPL = \$2,000; 125% of FPL = \$1,500; 174% of FPL = \$1,000, down to 500% of FPL = \$0)
 - Disbursement 1 at age 18
 - About \$45K federal investment
- Continued progressive deposits of \$2k per year up to age 24
 - Disbursement 2 at age 24
 - About \$15K federal investment
- CSAs facilitate multiple streams of assets (e.g., family members, employers, philanthropic foundation, communities, private donors, and other entities) beyond the federal investment to flow into a child's account

It is important to point out, similar to how we describe assets, when children earn a degree, they also gain the corresponding characteristics of the degree and the institution that awarded the degree (e.g., prestige of school, social capital, an occupation/marketability, knowledge and skills in a particular field, experience, etc.) which in turn increases their opportunity to improve their financial capability. So, while not explicitly listed as part of the financial capability model of financial aid above, in the case of college graduates, they earn a degree as part of this model. Education is also a strong predictor of financial capability (i.e., financial literacy, financial inclusion, and wealth). And so, we contend, because all the factors work together in this model, they have the potential for providing a multiplicative effect on children's return on degree. A powerful intervention that can deliver multiplicative effects is needed to rebuild faith in education as a path to the American dream and allow it to in fact act as an equalizer in children's everyday lives. The financial capability model of financial aid might just be such a policy solution.

Education As an Antipoverty Solution and Equalizer

The term *American dream* was popularized in James Truslow Adams's 1931 book, *The Epic of America*. The ideal of the American dream—in which effort and ability determine who succeeds and who fails—allows many to perceive that American institutions are just (Rank, Hirschl, & Foster, 2014). The dream—a central driver in the history of America—is associated with the constitutional right that all citizens should have an equal opportunity to the “pursuit of happiness.” The American dream rests on the axiom that effort and ability invested in education is a primary path for achieving a better life regardless of whether you are born poor or wealthy, Black or White. In this spirit, Horace Mann (1848) referred to education as the ‘great equalizer’ in American society.



In 1976, in talking about the function of education in the American welfare system Janowitz wrote,

Perhaps the most significant difference between the institutional bases of the welfare state in Great Britain and the United States was the emphasis placed on public education – especially for lower income groups – in the United States. Massive support for the expansion of public education, including higher education, in the United States must be seen as a central component of the American notion of welfare—the idea that through public education both personal betterment and national social and economic development would take place” (pp. 34 & 35).

For so long an accepted part of the American approach to fostering upward mobility, it must be emphasized that placing education in this central role was not a foregone conclusion. But instead, it was the result of explicit and intentional decisions about how our nation would build social welfare policy structures to complement individual effort and ability. While European nations have relied on the “direct redistributive role of the welfare state to reconcile citizenship and markets”, in part because of our choices not to directly redistribute, the United States has chosen to use education as a lever for ensuring equitable outcomes (Carnevale & Strohl, 2010, p. 83). This distinctly American belief—that economic disparity can be narrowed through individual effort in school, the pursuit of education (early on a high school degree in more recent decades some form of postsecondary schooling) and calculated public investments in educational opportunities—has been around almost from its conception. It is inextricably tied to the American dream.

From a functionalist perspective (Durkheim, 1933), it could be said that the American dream was constructed by the people of the United States. Its function, to serve as a tool to provide its citizens with justification for remaining faithful to American institutions and looking inward at their own investment of effort and ability in times of trial, when happiness is something for the future. The mantra goes something like this, “Yes, I am poor, however I can change my lot in life or that of my children if I work hard and have the ability to succeed in school.” The sense that you can control your own fate is a powerful and important elixir for maintaining the American dream. And wide access to public education has made hope in the American dream tangible too many for centuries (Garfinkel, Rainwater & Smeeding, 2010; Hochschild & Scovronick, 2003). Americans have shown that they are willing to accept a lot of inequality, if there is observed fairness—that there is commensurate return on their own contributions. However, the allure of the American dream can become diluted if enough people have grounds for questioning whether effort and ability invested in education is rewarded equally. There are signs of this happening in America.

However, what if the education system isn't the great equalizer that we believed it was meant to be and is even helping to increase inequality in some circumstances? What if not everyone has the same opportunity to benefit equally from attaining a degree (i.e., equal return on degree)? What can we do to make belief in education as an equalizer tangible? In this report we explore these questions and more to chart a course for understanding how education can become the equalizer it was meant to be in the US economy.

We posit that for education to be an equalizer and provide the maximum return on degree for all students, it must develop students' financial capability through its curriculum and financial aid. Further, we build on financial capability theory by positing that a person cannot be financially capable if they do not own assets. Financial capability encompasses both the knowledge and understanding of financial concepts (financial literacy) and the ability to access and utilize a range of financial products and services (financial inclusion) (Johnson & Sherraden, 2007; Sherraden, M. S., 2013). We then discuss how a large-dollar version of Children's Savings Accounts (CSAs), a type of asset-building account for children, would align with a financial capability model of financial aid that includes not only assets to pay for college, but also assets for when they leave college and begin independently living outside of their families' homes. We propose that for maximizing the return on degree, having initial assets when children leave college are as important as having assets to enter college. Crucially, it is initial assets when they leave home that are a significant factor in determining the amount of assets children can accumulate later in life (Elliott, Rauscher, & Nam, 2018).

EVIDENCE OF GROWING DOUBT THAT EDUCATION PAYS

- In the New York Times, Paul Tough (2023, September 5) writes,
 - *A decade or so ago, Americans were feeling pretty positive about higher education. Public-opinion polls in the early 2010s all told the same story. In one survey, 86 percent of college graduates said that college had been a good investment; in another, 74 percent of young adults said a college education was “very important”; in a third, 60 percent of Americans said that colleges and universities were having a positive impact on the country.*
 - *He goes on to say, A decade later, Americans' feelings about higher education have turned sharply negative. The percentage of young adults who said that a college degree is very important fell to 41 percent from 74 percent. Only about a third of Americans now say they have a lot of confidence in higher education. Among young Americans in Generation Z, 45 percent say that a high school diploma is all you need today to “ensure financial security.” And in contrast to the college-focused parents of a decade ago, now almost half of American parents say they'd prefer that their children not enroll in a four-year college.*



To Become the Great Equalizer, Education Needs to be Paired with Financial Capability

Education provides children with the knowledge and skills they need to succeed at performing an occupation.¹ Further, most economists posit that the time and money people invest in education will provide them with a return on investment (Becker, 1964). For example, according to Carnevale, Cheah, and Wenzinger (2021), the median lifetime earnings of a fulltime worker with a high school diploma are \$1.6 million, while those with a bachelor's degree are \$2.8 million; bachelor's degree holders earn 75% more than if they had only a high school diploma. **However, we hypothesize that the amount of payoff one can receive is determined, at least in part, by the level of financial capability they possess. Because America has put education in the role of equalizing economic outcomes, it must develop in its graduates, strong financial capability for education to fulfill this role.** If the goal of education was simply to have a more educated citizenry, and to receive the non-financial benefits associated with being educated (Heckman, Humphries, & Veramendi, 2018), there would be no need for degree holders to be financially capable.

¹The use of the term occupation instead of, for example, field of study is purposeful because it conveys the sense that, an important purpose of education is preparing children for the pursuit of better economic outcomes. Research indicates that education brings many other types of benefits to individuals and society (Trostel, 2015), but this paper is focused on its economic outcomes. The focus on earnings as reason to attend college has only gone up. For example, in 1976 about 50% of students said that making more money was a very important reason for attending college but this rose to about 73% in 2019 (Higher Education Research Institute, 2019). <https://www.heri.ucla.edu/monographs/TheAmericanFreshman2019-Expanded.pdf>



Practically, what we are suggesting is that just because low-income children have the academic capability to earn a degree in engineering, for example, it does not mean that they have the financial capability to maximize their return on degree. Many people, including smart college graduates, may not have the skills or ability to manage their money effectively (Zap, 2019). And so, while the absolute standard of living of low-income children with an engineering degree might be raised, their relative standard of living compared to their wealthy counterparts with an engineering degree might be less (i.e., unequal return). So, when you compare the lifetime earnings, for example, of the low-income engineering degree holder to people with a high school degree or less, their earnings are far higher and thus their absolute standard of living can also be said to be far higher. However, when you compare their lifetime earnings to other similarly positioned degree holders but who have more financial capability, it is less. And as we know from research, low-income and minority children are more likely to have less financial capability than their wealthier counterparts (Klapper, Lusardi, & Oudheusden, 2015) and that financial capability is associated with having more wealth (Birkenmaier, Kim, & Maynard, 2023).

A. Financial Capability: What It is, and Its Impact on Children's Economic Outcomes

According to M. S. Sherraden (2013), financial capability consists of both one's ability to act (i.e., financial literacy which consists of their financial knowledge and skills) and the opportunity to act (i.e., financial inclusion). Financial capability is built on an institutional theory (Beverly et al., 2008; Sherraden, M., 1991) of asset building. From an institutional perspective, institutions provide people with opportunities to access financial products and services. Regarding financial capability, institutional theory suggests that access to financial institutions and the products and services they provide are a key factor in why low-income and Black children have less financial capability than their wealthier often White counterparts. Institutional theorists point to the following institutional factors as being needed for institutions to be more inclusive: access, information, incentives, facilitation, expectations, restrictions, and security (Barr & Sherraden, 2005; Beverly & Sherraden, 1999; Beverly et al., 2008). Access requires institutional structures to make financial services or products available to everyone. An example of this kind of institutional structure is opt-out enrollment in Children's Savings Accounts (CSAs), as described below.



What the Research Says about Financial Literacy's Impact on Individual's Economic Outcomes

Financial literacy is a component of financial capability (Sherraden, M. S. 2013). Researchers studying financial literacy examine the role that financial knowledge and skills play in determining children's economic outcomes. This research on financial literacy suggests it is an important predictor of whether children can achieve positive financial outcomes.

Evidence that Financial Literacy is an Important Predictor of Positive Economic Outcomes

- Lack of financial knowledge or low financial literacy is negatively related to retirement planning, saving (Behrman, Mitchell, Soo, & Bravo, 2012).
- Lack of financial knowledge is negatively related to wealth accumulation (Christelis, Jappelli, & Padula, 2010; Van Rooij, Lusardi, & Alessie, 2012).
- Low financial knowledge is also associated with paying higher interest rates and fees (Lusardi & de Bassa Scheresberg, 2013; Lusardi & Tufano, 2015).
- The more financially literate you are the more likely you will be to invest in the stock market, and to earn higher (risk-adjusted) returns on their investments (van Rooij, Lusardi, & Alessie, 2011; Clark, Lusardi, & Mitchell, 2017).
- Individuals with low levels of financial knowledge are less likely to diversify their investment portfolios (Guiso & Jappelli 2008; Jappelli & Pandula, 2015).

- The more financially literate you are the better you will be at managing your debts (Mitchell & Lusardi 2020).
- Up to half of wealth inequality may be associated with financial literacy (Lusardi, Michaud, & Mitchell, 2013).
- Financial literacy is a stronger predictor of wealth accumulation than school attainment (Behrman, Mitchell, Soo, & Bravo, 2010).

However, graduates from wealthy, White families come to and often leave school with more financial literacy than their poorer counterparts.

Evidence that Financial Literacy is Unequally Distributed

- In major advanced economies 60% of adults who live in the richest households are financially literate compared with 40% of their counterparts who are poor (Klapper, Lusardi, & Oudheusden, 2015).
- Financial literacy is often lower in low-income and minority communities, and barriers to education can restrict access to key financial information and strategies (Angrisani, Barrera, Blanco, & Contreras, 2021; Lusardi & Mitchell, 2014).
- The Federal Reserve Bank of St. Louis finds that income is highly correlated with higher financial literacy scores (Chien & Karson, 2018).
 - Zubrzycki (2017) finds that 45% of students in higher-income schools earned the top score on a five-point financial literacy scale, compared to 3% of lower-income students.
- On average, African Americans answered 38% (55% Whites) of the questions on a key financial literacy test correctly (P-Fin Index), with only 28% (62% Whites) answering over one-half of index questions correctly (Yakoboski, Lusardi, & Hasler, 2019).
 - They also find that there is a 29% difference in P-Fin Index questions answered correctly between African Americans with household incomes below \$25,000 and African Americans with household incomes of \$100,000 or more.

We posit that the existence of inequality in financial literacy reduces the ability of education to act as an equalizer in the American economic system.

A. Educational Curricula and Classrooms Provide a Tool for Developing Financial Literacy

While questions remain, regarding the policy structures to best facilitate financial inclusion, the best tools available for developing financial literacy are already well known and studied. As these are woven into education's curricula and its classrooms, we will only discuss them briefly here. In 2022, about 23% of high school students (or nearly 1 in 4) had guaranteed access to personal finance courses (Next Gen Personal Finance, 2022). In states where it is not mandated (in 38 out of the 50 states it is not required), 1 in 10 students take a standalone personal finance course prior to graduation (Next Gen Personal Finance, 2022). Research shows high school students who take a standalone personal finance class is an important predictor of student's economic outcomes.

While only a small percentage of students overall take a standalone personal finance course prior to graduating, it is even more bleak for students attending low-income schools or predominately Black and Brown schools. Next Gen Personal Finance (2022) reports that 1 in 20 students attending schools where more than 75% of the students are eligible for free and reduced lunch take a standalone personal finance course. They find a similar ratio for schools where more than 75% of students are Black and Brown. Not surprisingly then, a nationally representative sample of college students reports that only 53% report feeling prepared to manage their money while in college (Zapp, 2019). Therefore, it should also not be surprising that many low-income and black students take out student loans (Huelsman, 2015, Neelakantan, 2023) potentially driving down their return on degree.

Evidence of the Relationship between Personal Finance Courses in High School and Economic Outcomes

- Increase credit scores (Urban, Schmeiser, Collins, & Brown, 2020).
- Decrease student loan default rates (Brown, Collins, Schmeiser, & Urban, 2014).
- Reduce credit card balances while in college (Stoddard & Urban, 2018).
- Reduce the likelihood of having any outstanding debt and being delinquent on debt (Brown, Grigsby, van der Klaauw, Wen, & Zafar, 2016).
- Increase the chance students shift from high-cost private loans to low-cost federal loans to finance their college degree (Stoddard & Urban, 2018).
 - They also find that students from families with fewer resources ended up working fewer hours and replaced working with low-cost federal loans (Stoddard & Urban, 2018). Reducing hours worked is important for academic success in college particularly for low-income students (Carnevale & Smith, 2018).



A policy implication of this section is that efforts to make personal finance courses a mandatory part of all high school curricula can play an important role in helping to develop children's financial capability and in turn education's ability to be an equalizer. **Further, while we could not take the time to discuss here, we posit that financial literacy efforts should extend beyond high school and become a part of postsecondary curricula and classrooms in America as well.** We should also note that the literature on financial literacy is mixed, and we understand that. The mixed results have to do with several factors to include the quality and type of financial literacy being provided (Consumer of Financial Protection Bureau, 2019). However, we are not suggesting that financial literacy or even financial inclusion by itself are enough to position education as an equalizer and assure all students have the opportunity to maximize their return on degree. Instead, we are positing that when students have a degree, receive financial literacy training, have access to financial institutions, and come out of college with assets rather than student debt, education is more likely to succeed at being an equalizer. That is, anyone of these things by itself is unlikely to be successful enough to overcome the large wealth inequality gap that exists in America.

In line with this, as M. S. Sherraden (2013) indicates, financial capability is not only the ability to act, but it also consists of the opportunity to act. In the next section we examine the impact that access to institutions has on an individual's economic outcomes, how financial aid is being used currently to facilitate access to the credit arm of financial institutions, and then how Children's Savings Accounts (CSAs) form of financial aid could facilitate access to the asset building arm of financial institutions positively impacting the return on degree.

IV

Research On Financial Inclusion's Impact on Economic Outcomes

Researchers who study financial inclusion examine the role access to financial institutions plays in determining an individual's economic outcomes. Like the research on financial literacy, the research on financial inclusion indicates that it is an important factor for determining an individual's economic outcomes.

Evidence that Financial Inclusion is an Important Predictor of Positive Economic Outcomes

- Ampudia and Ehrmann (2017) estimate that banked households in the United States have net. wealth that is \$42,000 higher than unbanked households with the same characteristics.
- Célerier and Matray (2019) find that the increase in financial inclusion induced by the Riegle-Neal Act² led to banked households' accumulating more interest-bearing assets, investing more in durable assets, and becoming less likely to face financial difficulties.
- Stein and Yannelis (2020) study the impact of the Freedman's Savings Bank. They find positive evidence that families with accounts had higher income, real estate wealth, and business-ownership rates.
- Florant, Julien, Stewart, Yancy, and Wright (2020) run a simulation and find "by providing Black customers access to financial products at the same rates as white customers (an equal access, unequal wealth scenario), financial institutions could realize approximately \$2 billion in annual incremental revenue." (para. 11).

² To learn more about the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 which allows banks to branch across state lines go to <https://www.federalreserve.gov/boarddocs/supmanual/cch/sec109.pdf>.

- They also find that “if there was no disparity in the average revenue per household between black and white customers (a total parity scenario), which has been largely driven by differences in wealth and income, the full financial inclusion of Black Americans would generate about \$60 billion in additional annual revenue in the financial sector.” (para. 11).

But again, as in the case of financial literacy, access to financial institutions and their support is not equally available. Research shows that low-income and minorities have less financial access than their wealthier, White counterparts. As a result, they miss out on the advantage that access to institutions provides.

Evidence that Financial Inclusion is Unequally Distributed

- Many low-income and minority neighborhoods lack local banks, leading to a phenomenon known as banking deserts. This makes it difficult for these communities to access necessary financial services (Dahl & Fanke, 2017).
 - In 2021 29.3% of Black households making less than \$15,000 per year were unbanked, 26.5% of Hispanic, and only 13.6% of White households (FDIC, 2021).
- Banks often require a minimum balance, which those in low-income communities may struggle to accumulate. This can create a barrier to opening or maintaining accounts.
 - FDIC (2021) reports that this is the number one reason the unbanked give for not having an account.
 - Faber and Friedline (2020) find that Black and Hispanic communities face higher costs than White communities to open and maintain checking accounts, including minimum opening deposits, minimum balance requirements, regular maintenance or service fees, and overdraft fees.
- Low-income and minority communities are often targeted for predatory loans with high-interest rates, which can trap them in a cycle of debt (Engel & McCoy, 2002).
- It is often harder for individuals in low-income brackets and minorities to obtain credit or loans due to poor credit histories or lack of credit (Meier & Sprenger, 2010).
- Online banking and financial services may not be accessible for those who lack internet access or technological proficiency, often the case in low-income communities (Bhutta, 2018).

A. Financial Aid Provides One of the Best Tools Within Education for Facilitating Financial Inclusion

If we accept education has a role as an equalizer, then a part of its role would be preparing college students to be financially capable, that is, putting them in the best position to leverage their degree and get the maximum return from it. And if we accept a role that education must play is to develop financial capability in its students, then it would also have to have a role in facilitating access to financial institutions. This is because access is a component of financial capability (Sherraden, M. S., 2013). **In this report, we posit that the best or most readymade tool education currently has for providing access to financial institutions is through financial aid.**

B. Financial Aid Currently Provides Access to Financial Institutions Through its Student Loan Program

You might ask, “how can financial aid provide access to financial institutions?” We suggest that it already does through the student loan program. When children are given access to student loans, they are given access to the credit arm of financial institutions such as banks even if they would not normally be deemed credit worthy (i.e., financially capable of using credit well). Students can receive Federal Direct Stafford Loans regardless of their



credit history, current income, or their potential income postgraduation. **It is one of the few types of loans that a person can receive regardless of their financial capability for paying them back.** Because many, particularly low-income and Black students, might not be financially capable of taking on the amount of loan debt they are eligible to receive while in college, it should not be surprising then that they struggle to pay back loans after they leave college (30% of Black student compared to 10% White students reporting defaulting at least once on their federal student loans; Neelakantan, 2023). Giving students access to loans they are not financially capable of paying back as a policy for making education more accessible seems dubious from the start, and at the very least counterproductive in terms of assuring the opportunity for an equal return on degree. Nonetheless, when we suggest that financial aid can be used to provide students access to financial institutions, this is not a new role for financial aid and it should not strike anyone as unusual or shocking, it is a role that financial aid is already playing.

C. Student Loans Reduce the Return on Degree and Access to Institutions

Somewhat paradoxically, even while providing access to the credit arm of financial institutions, financial aid in the form of student loans can weaken people's ties with the asset arm of financial institutions, particularly among low-income and Black degree holders. One way they can do this is by increasing the amount of a borrower's monthly gross income that has to go toward debt repayment (i.e., debt-to-income ratio) (Blagg et al., 2022). Financial institutions use this ratio in their decisions to provide loans such as for a car or home. Student loans can also negatively impact students credit scores if they end up delinquent or in default on their student loans (Blagg et al., 2022).

Evidence that Low-Income and Black Students are More Likely to Rely on Student Loans, Have More Trouble Paying Them Back, and they have Damaging Effects on Children's Economic Outcomes

- **More likely to take out student loans**

- About 84% of bachelor's degree recipients at public colleges who receives Pell Grants borrow for the credential, compared to 46% of those who never received Pell (Huelsman, 2015)
- About 66% of White students took out student loans in 2017 compared to about 86% of Black students (Neelakantan, 2023).

On average, Black student borrowers have about \$32,000 in student loans, this is about 12% more than the average amount of White student borrowers (Neelakantan, 2023).

- **Reduce chances of enrolling and graduating from college**

- After conducting a review of literature on the effectiveness of student loans to increase enrollment in college, Heller (2008) concludes that existing research indicates that educational loans have little or even a negative impact on college enrollment.
 - Perna (2000) finds that student loans reduce the chance that Black students enroll in four-year colleges.
 - Low-income students are sometime averse to taking out student loans to pay for college (Baum & Schwartz, 2013).
- Kim (2007) finds that higher student loan debt in the first year of college reduces the probability of graduating among low-income and Black students.

- **Harder time paying back student loans after graduation**

- Four years after earning a bachelor's degree, black graduates in the 2008 cohort held \$24,720 more student loan debt than white graduates (\$52,726 vs. \$28,006), on average (Scott-Clayton & Li, 2016).
- According to Jackson and Jones (2020), “a Black bachelor’s degree recipient is more likely to default than a White college dropout [42% vs. 11%, respectively], and Black borrowers from families in the highest income quintile have higher default rates than White borrowers in the lowest income quintile [34% vs. 23%, respectively]” (parg. 5; bracketed information added).

- **Damaging effects on children’s economic outcomes**

- Research indicates that college graduates with student debt take jobs that have higher initial salaries but lower potential wage growth (Minicozi, 2005).
 - Hiltonsmith (2013) finds that college graduates with student loans start of earning more than students without college debt but end up earning less by the time they reach their 40’s, and significantly less by their mid-50s.
- Make it less likely to start a new business (Ambrose, Cordell, & Ma, 2015).
- Delay buying a home (Blagg et al., 2022; Cooper & Wang, 2014) one of the biggest assets for most Americans hold (Schuetz, 2020).
 - Defaulting on student loans can reduce credit scores by 50 to 90 points (Blagg, 2018).
- Delay saving for retirement (Egoian, 2013) when it is well established that even very short delays have a substantial impact on the amount of retirement savings (Charles Schwab, 2023).
- Reduce overall net worth (Elliott & Nam, 2013).

In general, financial aid in the form of student loans can result in a delayed economic launch into adulthood. Elliott and Rauscher (2016) measure mobility as the likelihood and rate of achieving median household net worth among four-year college graduates or above who were at least age 22. After controlling key differences, they found that acquiring the relatively small amount of \$10,000 in student loans is associated with an 18% decrease in the rate of achieving median net worth. And so, while most of the focus of this report is on lifetime return, it also matters how long or later in life individuals experience equal returns on degree.

But it is also true, for some, student loans can strengthen connections with financial institutions if they can payback their loans on time and without becoming delinquent or defaulting. But as the findings above indicate, it just so happens that wealthy,

White students are in the best position to pay back their loans on time because they start off with stronger financial capability in the first place. So, while student loans as a form of financial aid can be said to provide students with access to banking institutions and credit markets, too often they restrict the access for low-income and Black students after they leave college. We are not suggesting that financial aid should not provide access to financial institutions, cut rather that the type of financial aid matters. Giving credit to students who are not financially capable of paying it back is not the right type of access for strengthening the return on degree.

To strengthen the return on degree and empower education to be an equalizer, we posit the type of access financial aid should focus on providing is to the wealth building arm of financial institutions and not the credit arm. Although student loans are often what comes to mind when we think of financial aid, Children Savings Accounts (CSAs), sometimes called Child Development Accounts (CDAs), are a form of financial aid that can be used to provide students with access to the asset development arm of financial institutions.

KEY POINTS ON STUDENT LOANS AND THE RETURN ON DEGREE

- Have no effect on college enrollment or sometimes a negative effect on enrollment.
- Reduce the chances student complete college.
- Not inclusive (some students are loan averse).
- Can negatively impact credit scores.
- Can be predatory because they give student access to the credit arm of financial institutions.

V

CSAs Make Full Financial Inclusion Possible: An Antidote to Wealth Inequality?

Children's Savings Accounts (CSAs) are savings vehicles, most commonly designed for higher education savings. While they have specifically designed features (incentives and explicit structures) to encourage asset building among disadvantaged youth and families, they are meant to universally serve all young people. Unlike basic savings accounts, CSAs leverage investments by individuals, families, communities, employers, local, state, and federal governments, philanthropists, foundations, and others as a way of building assets (Elliott, 2023, March).

CSAs are gaining traction around the country. In 2022 almost five million children had a CSA in (Prosperity Now, 2022). They are a potentially powerful tool to improve educational attainment and make existing institutions—K-12 schools, universities, the financial aid system—work better, especially for disadvantaged students. In the absence of passage of national CSA policy, some states and localities have developed their own children's savings initiatives (128 nationally in 38 states), including programs that incorporate elements of CSA design into State 529 College Saving Plans (Prosperity Now, 2022). While the details vary, these CSA-style investments in children's futures include publicly funded initial contributions and matching contributions for low-income savers, opening accounts for children at birth or in some cases when they reach specific educational milestones (such as kindergarten enrollment). Some programs are also experimenting with financial literacy initiatives (Goldberg, Friedman, and Boshara, 2010).

Among the 38 states with a CSA program, there are seven that have a statewide program (California, Illinois, Maine, Nebraska, Nevada, Pennsylvania, and Rhode Island) (Sherraden, M. & Clancy, 2021). All seven states built their programs upon their State 529 Savings Plan structure. A group of CSA experts (Cisneros et al., 2021) identified 8 key principles for designing CSAs at scale:

- Eligibility for all—everyone is included and gets a stake
- Automatic enrollment—remove barriers to enrollment
- Automatic initial deposit—jump-start wealth accumulation
- Start young—maximize wealth-building potential
- Targeted additional deposits—those with greater need get more
- Centralized savings plan—enable implementation and reduce costs
- Investment growth—augment the wealth building capacity of families
- Simplified investment options—make decisions easy

Several of these principles are particularly important for helping understand why CSAs might be the best tool for providing students with access to the asset development arm of banking institutions.

CSAs are designed specifically to overcome the problem of inequity in financial capability. One feature mentioned among the 8 key principles for CSA policy design has been shown to be particularly adept here, automatic enrollment. Research shows that within the SEED for Oklahoma Kids (SEED OK) experiment, after 14 years 100% of SEED OK treatment children who were automatically enrolled into the program had an account with assets whereas only 5% of children in the control group had a 529 account with assets (Clancy, Beverly, Schreiner, Huang, & Sherraden, M., 2022, June). There doesn't seem to currently exist a better way to achieve full inclusion than through automatic enrollment. Full inclusion into the asset development arm of financial institutions seems like an absolute requirement. For education to be able to reach the goal of being an equalizer it must have an institutional structure that allows it to reach everyone.

Further, unlike student loans which focus on providing students with credit to pay for college, CSAs provide a financial structure to provide all students with assets to pay for college. This is highlighted by the key principle of automatic deposits. Existing CSA programs have provided relatively small initial deposits of anywhere from \$5, to \$1,000 in the case of the SEED OK experiment. But even these relatively small initial deposits have resulted in the accumulation of real assets for low-income and minority students in these accounts. For example, at age 14 the average treatment child in SEED OK, a group that includes low-income and Black children, has about \$4,373 dollars in their account (Clancy, Beverly, Schreiner, Huang, & Sherraden, 2022, June).³ While this is certainly not enough to pay for college, it demonstrates that CSAs can be a fully inclusive financial institution that facilitates asset building. Later in this report we will discuss how CSAs can be further developed to build enough assets to pay for college and provide children with money to launch into adulthood.

³ If they took the extra step and opened their own OK 529 to save in, the average balance is \$14,045 (Clancy, Beverly, Schreiner, Huang, & Sherraden, 2022, June).

Further, because CSAs were designed with the understanding that low-income and minority students often start off behind economically, a key feature of CSAs is targeted ongoing deposits. For a financial aid strategy to ensure that education truly catalyzes equitable outcomes, it must provide more resources to the economically disadvantaged. Unlike in the case of student loans, where increasing the amount low-income students can take out can have a negative economic impact on them post-graduation, thereby increasing economic inequality, giving low-income students more assets does not pose the same dangers. In fact, giving low-income students more assets can have the opposite effect, reducing inequality. For example, policy simulations show that if a universal CSA program had been established in 1979 with a progressive initial deposit of \$7,500 for low-wealth households (less than \$5,000 net worth) with incremental declines to \$1,250 for the highest-wealth households (\$25,000 net worth or more), the Black/White wealth gap would be decreased by 23% (Sullivan, Meschede, Shapiro, Asante-Muhammed, & Nieves, 2016). Similarly, research shows reducing the amount of debt students have would reduce inequality. Hueslman, Draut, Meschede, Dietrich, Shapiro, & Sullivan (2015) find that eliminating student debt among those making \$50,000 or below reduces the Black-White wealth gap by nearly 37% among low-wealth households, and a policy that eliminates debt among those making \$25,000 or less reduces the Black-white wealth gap by over 50%.

A. CSAs are a Form of Financial Aid that Can also Help Prepare Children for College

Existing CSAs have been designed to not only give low-income children access to the asset arm of financial institutions to build wealth to pay for college, and for launching them into adulthood, they also have been shown to have impact on children's preparedness for college. As such, CSAs have the potential to make financial aid a tool that can impacts children's early social and emotional development, academic performance, likelihood of enrolling in college, and likelihood of persisting to graduation from college, as well as financial aid that can serve as a two-generation strategy.



Evidence of the Early Effects of CSAs

• Quasi Experimental Findings

- Children’s improved math and reading scores (Elliott, 2009; Elliott, Sorensen, Zheng & O’Brien, 2023).
- Improves children’s educational expectations (Elliott, 2009; Elliott, Zheng, Saborl, & O’Brien, 2021).
- Reduces wilt among children who have the academic ability and expect to attend college but fail to do so shortly after high school graduation (Elliott & Beverly, 2011).
- Low-to-moderate income children are more likely to enroll in college and graduate from college when they have school-designated savings⁴ of \$1 to \$499 or \$500 or more (Elliott, Song, & Nam, 2013).
- Black children are more likely to enroll in college and graduate from college when they have school-designated savings of \$500 or more (Friedline, Elliott, & Nam, 2013).

• Experimental Findings

- Improved parental educational expectations for their children (Kim, Sherraden, Huang, & Clancy, 2015).
- Improved social emotional development among young children, particularly among low-income children (Huang, Sherraden, Kim, and Clancy, 2014).
- Reduced punitive parenting practices (Huang, Nam, Sherraden, & Clancy, 2019).
- Reduced maternal depression (Huang, Sherraden, & Purnell, 2014).
- Helps build assets for college (Clancy, Beverly, Schreiner, Huang, & Sherraden, 2022, June).
- Improved college enrollment and persistence (Azzolini, Martini, Romano, & Vergolini, 2018).

B. CSAs Help Create an Environment for Dreaming Tangible Dreams

An important aspect of CSAs that requires more discussion is their power to make dreams and hopes tangible. A part of what was discussed in the introduction was the importance of the American dream for maintaining the American way of life, and education to

⁴ School designated savings is a proxy for having a CSA. It is when children say they have their own person savings account and have mentally set aside some of the money in the account to pay for school related expenses.

making the Dream tangible in people's lives. Tangible dreams have grounds in a person's circumstances and are not merely wishful (Elliott, 2023, March). Education is increasingly seen as not being a tangible path to the American dream (Tough, 2023, September 5) because of the weakening of the return on degree that has resulted (Emmons, Kent, & Ricketts, 2019), in large part, from the cost of college and the use of student loans to pay for it.

CSAs have the potential to restore belief in education as a tangible path for achieving the American dream because they help children build assets which are linked to children's futures. Elliott (2023, March) has suggested that CSAs have the potential to transform what might have been a mere wishful dream for a child (e.g., I aspire to go to college) into a tangible dream (e.g., I expect to go to college). Research on CSAs is consistent with them having the power to make dreams tangible. For example, participating in a CSA program can strengthen parental educational expectations for their children (Kim, Sherraden, Huang, & Clancy, 2015), as well as children's educational expectations for themselves (Elliott, 2009; Elliott, Choi, Destin, & Kim, 2011). CSAs provide children and their families with the power to purchase a piece of their child's future today, making the future feel tangible and worth investing in (Elliott, 2023, March).

C. Postgraduation Impacts Add to CSAs Potential for Strengthening the Return on Degree

However, to be a strong candidate for strengthening the return on degree, it also matters how CSAs impact children's post-college outcomes. Research suggests that having savings can act as a type of gateway to having a more diversified asset portfolio as an adult.

Evidence that CSAs Can Act as a Gateway Financial Instrument to a Diversified Asset Portfolio

- Children between ages 15 to 19 who have savings are more likely to have a savings account, credit card, stocks, bonds, vehicle, and a home at age 22 to 25 than if they did not have savings of their own between ages 15 to 19 (Friedline & Elliott, 2013).
- While owning a savings account as a young adult only contributed \$50 toward liquid assets, the added contribution of combined stock and retirement accounts—themselves products of savings account ownership—was \$5,283 (Friedline, Johnson, & Hughes, 2014).
- Pew Charitable Trust (2013) finds capital income has a strong relationship with moving up the economic ladder. They find that Americans who move from the bottom of the income ladder had six times higher median liquid savings, eight times higher median wealth, and 21 times higher median home equity than those who remained at the bottom. So, by building a more diversified asset portfolio, CSAs lead to increased asset accumulation, which, in turn, may lead to higher odds of moving up the economic ladder.



Research on parental financial support is suggestive that CSAs, which mimic early parental investments, are likely to increase children's income and wealth postgraduation. And, because asset transfers run in different directions for Black children, than for White children, this is a keyway CSAs can counter racial wealth gaps. Specifically, Rauscher (2016) finds that predicted household income and net worth is higher for adults who received parental financial support for education than for those receiving no parental educational support when such support exceeded \$600 in the case of increasing children's income and exceeded \$2,200 in the case of increasing children's net worth.

Further, CSAs also provide potential for making financial literacy training in schools more tangible to students. Financial education combined with an actual investment account with money in it may provide students with an environment ripe for developing financial capability (Johnson and Sherraden, 2007; Sherraden, M. S., 2013). That is, educational environments where experiential learning can take place go beyond mere games and simulations. You can easily imagine a world where every child in a school has a CSA account and teachers use these accounts in a personal finance course or even math class to develop lesson plans that give students real life experience with concepts like saving, investing, interest, and money management. Research shows that experiential learning promotes increased engagement and retention of financial knowledge by students (Beutler & Dickson, 2008; Mandell & Klein 2007). However, before we can discuss the role that asset ownership plays in being financially capable, we first must discuss how financial literacy and financial inclusion are linked together to form the current notion of financial capability.

VI

The Link between Financial Literacy and Financial Inclusion

In line with financial capabilities theory (Johnson & Sherraden, 2007; Sherraden, M. S., 2013), research shows that financial literacy and financial inclusion (i.e., access to financial institutions) are associated with one another. Using experimental data from SEED for Oklahoma Kids (SEED OK), Huang, Nam, and M. S. Sherraden (2013) find evidence that financial access significantly increases the chances that families in the treatment group hold a CSA but not in the control group. Furthermore, there is evidence in this study that suggests financial knowledge facilitates holding a CSA but only when financial access is available. Huang and colleagues (2015a, 2015b) also find evidence that having access to a CSA (i.e., treatment status) positively moderates the relationship between financial knowledge and asset accumulation (i.e., savings amount and total assets). **This indicates that financial capability requires both improved financial knowledge and financial inclusion.** It also suggests that financial capability is linked to asset accumulation. Further, it supports the hypothesis that financial capability is an important factor for predicting return on degree.

Some research suggests that financial literacy is an important determinant of financial inclusion (Hasan, Le, & Hoque, 2021). That is, financially literate people are more likely to have access to financial institutions. But while financial literacy is positively associated with having access to financial institutions, some research suggests that financial inclusion is a stronger predictor of economic outcomes than financial literacy. For example, Sun, Chen, Ansong, Huang, and Sherraden (2022) find evidence that financial literacy and financial access reduce economic hardship but that financial access plays a bigger role in reducing financial hardship than financial literacy. However, for this report, sorting out which comes first, or which might be the most important factor, is of less importance. What matters here is that both play a role in individuals' overall financial capability, and financial capability is important for predicting individuals' and families' economic outcomes.



VII

Asset Ownership as Part of What it Means to Be Financially Capable

In this report, we posit that the current notion of financial capability falls short, because it does not include ownership of assets. **Because the current understanding of financial capability relies on an institutional theory for building wealth (Sherraden, M. S., 2013), it does not include ownership of assets as a component of what makes a person financially capable; at best it is treated as a contextual factor.** That is, it emphasizes access to institutions as the key determinant for building wealth. However, we posit that it is hard to think about the opportunity to act without including ownership of actual assets. What does it mean to have all the financial knowledge in the world and access to financial institutions, when you don't have the assets to use them? It is like having a degree but no job. The access you had to education and the knowledge you gained while in school provides you with little to no financial benefit. That education ends up seeming like a waste of time, and you quickly put it to the side and pursue opportunities that you think will have an impact on your life.

When people own assets, they gain the corresponding characteristics of the assets (e.g., cash flow in the future, financial security, ability to take risks, property rights, etc.) which in turn increases their opportunity to improve their capability. However, the degree to which owning assets alone increases what children can achieve is also tied to their ability to utilize the asset. Maximizing the economic returns on a degree requires a certain level of financial capability, and the level of financial capability a child has is determined by the level of financial knowledge, skills, access to institutions, and assets they have (for a more technical discussion on how assets are connected to financial capability drawing from capabilities perspective, see Appendix A).

VIII

Being Educated is a Predictor of Financial Capability but Holding a Degree Does not Provide the Same Return on Degree by Income and Race

Financial capability theorists operationalize the opportunity to act, a component of being financially capable, as having access to financial institutions (Sherraden, M.S., 2013). However, in this section we posit that the opportunity to act shouldn't simply be understood to mean access or inclusion.⁵ To fit our belief that we live in a meritocracy, it must include the idea of having the prospect of producing equal outcomes by acting. And we propose for your actions to have the opportunity to produce similar outcomes as other actors, you must not only have access to institutions but also to wealth. Not surprisingly, in our capitalist system, institutions respond to people differently when they have wealth (Sherraden, M., 1991). And the evidence presented in this report suggests that this difference matters for the return on degree people receive.

Another way to think about this is, does opportunity actually exist in an economy where wealth inequality plays a big role in determining winners and losers separate from their own actions? **If you have access to an institution but that access does not allow you to achieve a similar outcome as others by acting, then the opportunity to act is different in a way that matters. It can be said that it is different in a way that is out of sync with the American sense of meritocracy. And so, it is not enough that low-income children have access to higher education, financially literacy classes, or financial institutions, they must also have access to wealth.** They must also be able to produce similar economic outcomes having acted to attain a degree as similarly educated wealthy children do. This is contrary to what we currently see, today; low-income and Black children act to earn a degree, but they don't receive the same return on that degree.

⁵ Acting here means something like using my person resources (i.e., effort and ability) within an institutional context like school to achieve my own interest.

Evidence that Shows Education Produces Unequal Income Premiums

- Hershbein (2016) finds that bachelor's degree holders from low-income families start their careers earning about one-third less than those from high-income families.
- Return on degree for low-income students (i.e., Pell Grant recipient) is less for low-income students across all types of institutions (Carnevale, Cheah, & Van Der Werf, 2022).
 - Specifically at the bachelor's level, over the course of their lifetime, low-income students earn \$951,00 compared to \$1,006,000 for their counterparts at public institutions; \$863,000 versus \$967,000 at private nonprofit institutions.
- One year after graduation, the median income for Black graduates is \$36,000, compared to \$40,000 for white graduates (De La Fuente & Navarro, 2020).

Evidence that Shows Education Produces Unequal Wealth Premiums

- Researchers find Black students (\$52,147 income/\$32,780 net worth) receive less benefit from having obtained a college degree than their White (\$94,351 income/\$359,780 net worth) counterparts (Emmons & Noeth, 2015).
- Hamilton, Darity, Price, Shridharan, and Tippett (2015) find that Black families who have a head of household who graduated from college have about 33% less wealth than White families who have a head of household who dropped out of high school.
- As a result of the findings observed, using modeling, Traub, Sullivan, Meschede, and Shapiro (2017) found that even if Blacks graduated college at the same rate as Whites, this would only slightly reduce the racial wealth gap.

More recent research suggests that the wealth premium that education has typically produced is shrinking or in some cases has vanished in more recent years. This research finds that a small wealth premium remains for White college graduates born in the 1980s when compared to White high school graduates (Emmons, Kent, & Ricketts, 2019). However, in the case of Black college graduates born in the 1980s, they find the wealth premium had disappeared altogether when compared to Black high school graduates during the same time (Emmons, Kent, & Ricketts, 2019). They point to the rising cost of college and student debt as a reason the wealth premium that a college degree has provided is disappearing.

In the next section we review research that shows that the amount of wealth you start off with is a key determinant of how much wealth you can accumulate. This also supports the notion that to be financially capable, you must start off with a certain amount of wealth.

IX

You Need Wealth to Build Wealth, Initial Levels of Assets Matter for Determining the Return on Degree

While the current understanding of financial capability does not include asset ownership (Johnson & Sherraden, 2007; Sherraden, M. S., 2013), in this section we provide evidence indicating that a key determinant of being able to build wealth is starting off with wealth. As such, asset ownership helps define what people can achieve financially. **In accordance with Sen's (1999a, b) financial capability perspective, in explaining why initial assets matter, we suggest when people own assets the corresponding characteristics of the assets increase their opportunity for being able to use those assets to accumulate more assets, and in turn increase the amount of return they can receive on their degree.**

The fact that having wealth is linked to being able to accumulate more wealth might be the strongest argument for why financial capability should include wealth accumulation, but also for why later we propose that to strengthen the return on degree financial aid should not only provide assets for children when they reach college age, but also at the age when children become independent adults living on their own.

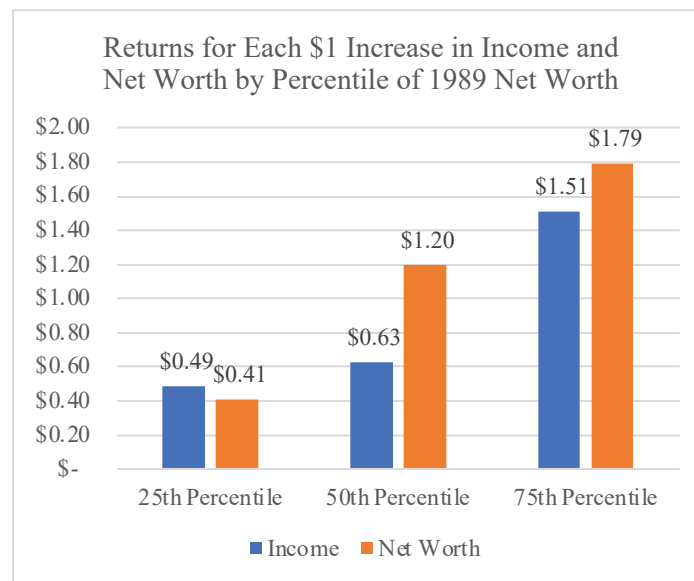


Evidence that Starting off with Wealth is a Determinant of Being Able to Accumulate Wealth

- Shapiro, Meschede, & Osoro's (2013) findings help shed some light on why this might be. They find that a \$1 increase in income translates to a \$5 increase in wealth for White families but only a 70-cent increase for Black Families.
 - But, importantly for this discussion, they also find when Black families start off with similar levels of assets, they have a return of \$4.03.
- Elliott, Rauscher, and Nam (2018) find that the power of income for generating wealth is determined at least in part by the amount of wealth older adults start off with as younger adults; that is, to build wealth you must have a certain amount of wealth as younger adults.
 - They also find that older age adults living at the 50th or 75th percentile as younger adults can expect to generate more wealth from each dollar, they earn than those living at the 25th percentile as younger adults.
 - This is like Shapiro et al. (2013) findings on race, but regarding income level.
- Growing up with wealthy parents as a child is linked to being more likely to be wealthy as an adult (Davenport, Levell, & Sturrock, 2021; Pfeffer & Killewald, 2019).
 - Similarly, Fagereng, Mogstad, and Ronning (2021) provide causal analysis of the importance of initial assets. They link Korean-born children who were adopted at infancy by Norwegian parents, on wealth and socioeconomic characteristics. Their mediation analysis examined the following four factors: children's education, income and financial literacy, and direct transfers of wealth from parents. They found that changes in these mediator variables explained nearly 40% of the average causal effect on these children's accumulation of wealth. The direct transfer of wealth was the most important mediator.
- Importantly, Elliott, Rauscher, and Nam (2018) find evidence that suggests while holding a degree makes a substantial difference in the amount of net worth younger adults have when they are older, a college degree matters more when younger adults start off with assets than when they do not.
 - Similarly, Conley (1999) finds that parental net worth is a more important predictor of young adults' net worth than education, income, or age.

These findings provide evidence for the contention that the amount of wealth a college graduate starts off with is likely very critical to education's ability to act as an equalizer.

A. It is Also Not Enough to Own Some Assets to Start Off With, You Must Own Enough to Turn Back the Tide of Inequality



Research suggests that for empowering children to build assets, the initial assets CSAs provide children to start off their adult lives matter, and amount matters when it comes to low-income and Black children and attempting to overcome inequality. For example, in the case of low-income children, Elliott, Rauscher, Nam (2018) find evidence that initial assets even among low-income children are predictive of the amount of assets they will have later in life. However, only in the case of the lowest percentile is income a stronger predictor of later wealth than initial net worth. That is, income still matters more for building wealth than assets do for the lowest wealth groups. They speculate that this is because low-income young adults start off with fewer assets. This suggests, for low-income families to experience the full power of owning wealth, the amount they start off with matters. Also, in the evidence section above, we discussed how Shapiro, Meschede, & Osoro's (2013) find that while initial wealth accounts for much of the Black/White wealth gap, even when having similar levels of wealth to start with doesn't completely close the wealth gap that Black Americans face suggesting race has its own impact. Therefore, we propose that progressivity is a key principle for any federal policy and the size of deposits in CSAs matters for strengthening the return on degree.

Education has a return on a degree problem. However, the evidence suggests that the size of the wealth gap in America is so large that attaining a bachelor's degree by itself—even when coupled with financial literacy and access to financial institutions—is unlikely to fully overcome the problem. **It must be understood, even if education provides a strong return on degree to financially literate students who are financially included, the size of the chasm it is being asked to close is too vast. Graduates who are low-income and/or Black will still need assets that they can leverage to receive the full return on their degree.** What is the size of the wealth gap we expect education to close?



The Size of the Wealth Gap is Too Big for Education and the Current Financial Aid Model to Close

In 2016 median family wealth among lower-income families was \$11,300, for middle-income families it was \$115,200, and for upper-income families it was \$848,400 (in 2018 dollars) (Pew Research Center, 2020, January). The racial wealth gap is even larger. McKay (2022, October), an economist with the Federal Reserve Bank of Minneapolis, runs a simulation to paint a picture of the size of the Black/White wealth gap in America

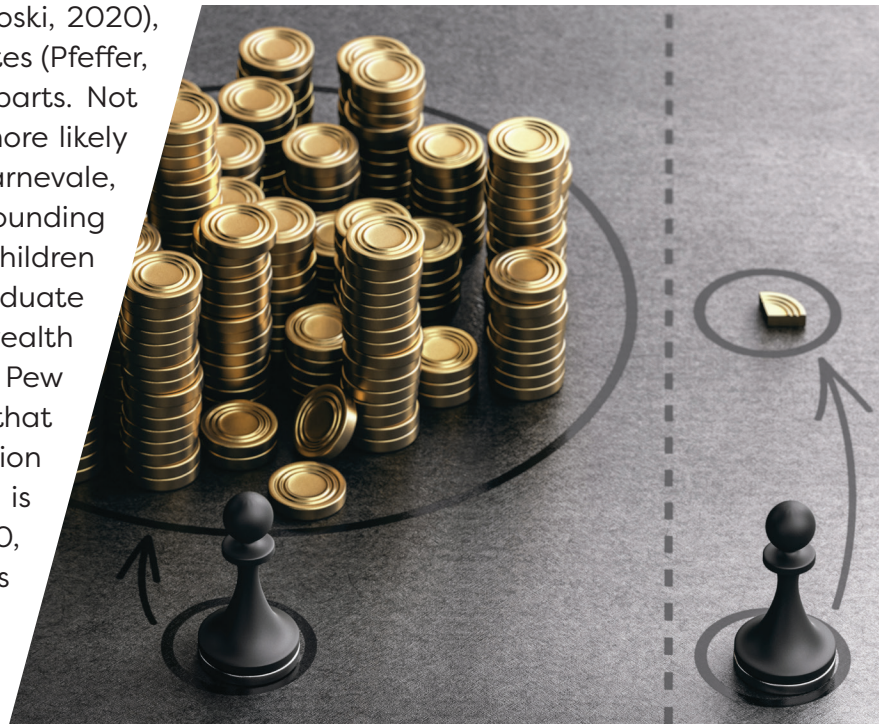
White Americans hold 84 percent of total U.S. wealth but make up only 60 percent of the population—while Black Americans hold 4 percent of the wealth and make up 13 percent of the population. Put another way: The wealth of the richest 400 Americans is approximately equal to that of 43 million Black Americans. (para, 21).

So, given the size of the wealth gap, it is not surprising that education fueled by the current financial aid model is unable to produce equal returns on a degree.

However, wealth inequality not only shows up in the return on the degree. It also has impacts starting early in the education process and these impacts overlap and accumulate over time. For example, children who grow up wealthier are more likely to have higher test scores during their early education (Yeung & Conley, 2008), more likely to attend so called Ivy-Plus⁶ colleges which provide access to selective leadership positions in the US and the opportunity for larger earnings postgraduation (Chetty, Deming, & Friedman,

⁶ Chetty, Deming, & Friedman (2023) define Ivy Plus schools as the eight Ivy League colleges, plus Chicago, Duke, MIT, and Stanford.

2023), receive more financial aid (Helhoski, 2020), and graduate from college at higher rates (Pfeffer, 2018) than their lower wealth counterparts. Not surprisingly, wealthy children are also more likely to grow up with an educated parent (Carnevale, Fasules, Quinn, & Campbell, 2019) compounding wealth inequality. Findings show that children who have a parent who is a college graduate are also more likely to have more wealth postgraduation. Specifically, the Pew Research Center (2021) finds evidence that the median wealth of first-generation households with a college graduate is \$92,500 less (\$152,000 vs. \$244,500, respectively) than for college graduates with a parent who was also a college graduate. What these findings together suggest is that wealth is inextricably linked to education in America, and to the outcomes people can achieve



through investing in education (i.e., return on degree). We contend that wealth is the straw that stirs the drink when it comes to education and its ability to act as an equalizer.

To be financially capable, we posit that you not only need knowledge, skills, and access to institutions, you also need assets. This can be seen in all the data presented in this section, but maybe it is most vividly reflected in data on the highest achieving low-SES children compared to the lowest achieving high-SES children regarding education. Carnevale, Fasules, Quinn, & Campbell (2019) find that a kindergarten student from the bottom 25% of socioeconomic status with **test scores from the top 25%** of students has a 31% chance of earning a college education and working a job that pays at least \$35,000 by the time they are 25, and at least \$45,000 by the time they are 35. However, a kindergarten student from the top 25% of socioeconomic status with test scores **from the bottom 25%** of students had a 71% chance of achieving the same milestones.

We assume a very similar situation to what Carnevale et al. (2019) found would occur when it comes to the current understanding of financial capability, which does not include wealth. **Without wealth, being the most knowledgeable and skilled financially will not overcome being born asset poor—even with access to financial institutions (e.g., Fagereng, Mogstad, & Ronning, 2021). To be financially capable, where it means having the opportunity to achieve an equal return on a degree based on the amount of effort and ability exercised in school, degree holders must also have a foundation of assets from which to begin.** In the next section we examine Children's Savings Accounts (CSAs) as a potential mechanism for modeling financial aid after a financial capability perspective for strengthening the return on degree.

XI

Modeling Financial Aid After a Financial Capability Perspective that Includes Assets: CSAs, A Tool for Strengthening the Return on Degree

The small-dollar version of CSAs (initial deposits of \$5 to \$1,000) that currently exist best align with the current understanding of financial capability which consists of being financially literate and having access to financial institutions (e.g., Sherraden, M. S., 2013). **The initial deposits in small-dollar CSAs are used as a tool for overcoming barriers to access (i.e., initial fees to open an account and/or enough extra money to encourage engagement).** The initial deposits are not looked at as a primary tool for reducing wealth inequality itself. No one would say putting \$5 to \$1,000 in an account is going to make a substantial difference in solving wealth inequality in America or for paying for college. No, in line with current notions of financial capability and institutional theory, the purpose of these small-dollar deposits is to provide children with access to financial institutions, which is in itself important. In the current model of financial capability access is seen as the necessary tool for children and their families to build assets. And it can be understood how the small-dollar version of CSAs focused on access to institutions produces positive economic outcomes given the literature on financial literacy and financial inclusion and their positive effects on economic outcomes (for a systematic review of this literature see, Birkenmaier, Kim, & Maynard, 2023).

A. CSAs Provide Children with the Opportunity for Assets to Flow into Their Account from Multiple Streams

However, it is also important to point out, that the small-dollar version of CSAs is still unique and possibly a much more powerful tool for building wealth than a lot of other financial interventions because they facilitate multiple streams of assets to flow into these accounts (Elliott, 2022, March). That is, CSAs (small-dollar or large-dollar) provide an institutional structure that allows for third party (e.g., family members, employers, philanthropic foundation, communities, private donors, and other entities) contributions as well as government contributions (i.e., federal, state, county, or city). In line with this, we have suggested that CSAs are not individual development accounts, but instead they are community accounts established by the community on behalf of a child (Elliott, 2023, March). As community accounts, it is not the responsibility of families or the government to finance children's futures, but that of the whole community. And if you remember the size of the wealth gaps in America, you might quickly realize that no one source is likely to provide enough assets to level the playing field.

The ability to facilitate multiple asset streams is one of the things that makes CSAs such a potentially powerful financial institution for building wealth particularly among low-income and Black students who have lower levels of financial capability because of systematic inequities and their economic circumstances. From this perspective, CSAs act as a type of financial scaffolding for transporting streams of resources (i.e., assets) to children and their families through a financial aid system that must be reimaged to be able to augment students' financial capability so that education can act as an equalizer. And so, when I say that small-dollar CSAs have not prioritized the role of asset ownership in children's financial capability, it doesn't mean that they aren't possibly still the best financial institution available for building a financial aid system whose goal it is to augment education's ability to act as an equalizer. As much as it is a mistake to underestimate the importance of asset ownership in financial capability, it is also a mistake to underestimate the importance of the institutional structure children have access to for asset building. We posit that all three are needed to strengthen the return on degree: assets, access to financial institutions, and financial literacy.

HOW SOME CSA PROGRAMS ARE TAPPING INTO THEIR POWER TO PROVIDE ACCESS TO MULTIPLE STREAMS OF ASSETS

Read the Following Case Studies:

- Keystone Scholars
- Early Award Scholarship
- Oakland Promise
- CollegeBound Saint Paul
- New York City Kids RISE

Find at: <https://aedi.ssw.umich.edu/unleashing-the-power-of-children-savings-accounts>

B. A Large-Dollar Version of CSAs Better Aligns with Financial Capability That Includes Asset Ownership

Unlike the current version of CSAs which is small-dollar and focused exclusively on paying for college, in *Assets and the Poor*, Michale Sherraden (1991) imagined the possibility of a multipurpose account (e.g., education, start a business, buy a homeownership, or prepare for retirement) that was started with a significant federal investment. Further, he initially imagined a much more robust asset building policy for the poor. Senator Bob Casey's (2021) 401 Kids Savings Account Proposal we suggest is a return to Sherraden's (1991) original vision for CSAs in many ways. It is a large-dollar multipurpose CSA. The 401 Kids Savings Account legislation proposes putting \$500 per year into a CSA created within Section 529 Qualified Tuition Programs. Accounts would be created for all families with a modified adjusted gross income below \$75,000 (\$150,000 married), with phase-out starting above that income level. An additional \$250 per year would be allocated for households eligible for the earned income tax credit. Not considering other funds whether it is personal savings, savings match, third party investments, or even investment earnings, there would conservatively be about \$9,000 to \$13,500 in federal dollars invested in an account at the time children reach 18. Moreover, Senator Casey's proposal also allows the funds to be used for post-secondary education and training, purchasing a home, starting a small business, or it can be rolled over into an ABL account or Roth IRA. There are other features such as the opportunity for matched savings, but for the purposes of this report, what is important is that Senator Casey's proposal taps into the CSA infrastructure and even expands on it by including the opportunity for building assets for purposes that might come after college such as buying a home, starting a business, or retirement.

While we propose a higher amount, more in line with Baby Bonds proposals (e.g., Booker, 2023), Senator Casey's proposal is a model for what a large dollar CSA structure that aligns with a financial capability perspective of financial aid could look like. As already discussed, CSA programs in general would have to be coupled with financial literacy training in the schools and universities to fully capture all aspects of financial capability. However, it is also worth pointing out that Senator Casey's proposal would provide a structure for providing low-income children, in particular, to have experiential learning opportunities that would augment financial literacy courses.

C. Children Not only Need Assets to Pay for College, But They Also Need Assets to Launch Successfully into Adulthood

Current models of small-dollar CSAs focus on paying for college. But as we have tried to illustrate in this report, education's return on degree problem cannot be solved solely by helping children pay for college. Because this problem is also about students' financial capability (including asset ownership) upon leaving college, a CSA designed to help solve the problem must provide children assets not only at age 18 but also at age 24.



According to the U.S. Bureau of Labor Statistics (2014) the time when most young adults move out of their parents' home and launch into adulthood is between the ages of 24 and 27. Further, most students earning a bachelor's degree in the U.S. graduate between ages 22 and 24 (Bogglers, 2022, July 4). In line with this timing of a second disbursement, Baum (2014) finds that the "earnings premium for a college education grows as workers age. Full-time workers ages 25 to 34 with bachelor's degrees have a 53 percent earnings premium over high school graduates. That premium grows to 72 percent for those ages 35 to 44, and to 79 percent for workers ages 45 to 54" (para. 5). Given that the premium on a bachelor's degree is at its least from age 25 to 34, about the time most children are setting out to become independent from their families, an asset infusion at this time might be most effective at strengthening the return on degree. This is particularly true for low-income young adults who will not receive the same support from their families that wealthier children receive.

In identifying age 24 for a second disbursement, I am suggesting that there are two critical periods where transfer of assets can play a significant role in using financial aid to augment education's ability to be an equalizer by strengthening the return on degree: (1) when children transition from high school to postsecondary education or directly into the labor market, and (2) when most children today are becoming independent adults in America. The idea of moving from one time point to two for asset distributions is in line with Michael Sherraden's (1991) original vision of what a CSA would look like. He did and still does refer to these accounts as Child Development Accounts (CDAs) because when he introduced them, he introduced them as lifelong accounts designed to assist children's development. As the field evolves, it is just moving closer to this vision of them, and this would be another step in that direction.

D. Large-Dollar CSAs Equivalent to the Cost of College

When most people think of the concept of free college, they can only think of not charging students to attend college (i.e., tuition free college). But another form of free college is providing children with assets in a CSA to pay for college (i.e., asset accumulation version of free college). This better aligns with a financial capability perspective of financial aid, and we posit would be more effective at strengthening the return on degree. Building on the idea that free can also be accomplished through a CSA, in addition to having two time points for disbursement, we would suggest connecting the size of the government investment in CSAs for an individual child at age 18 to what it would cost to provide children with a free college education. Currently, the average cost of attendance at a public 4-year college in-state institution in the 2022–2023 school year is \$11,260 which would be \$45,040 for four years (College Board, 2022).

This is in line with Senator Corey Booker’s (2023) Baby Bonds proposal, for example. His proposal, which also would phase out based on income level (i.e., the poor get more), would provide every child with an initial deposit of \$1,000 at birth and then an additional \$2,000 every year after until they turn 18. As a result, a child whose family’s annual income is 100% of the federal poverty level would have about \$46,215 in their account when they were 18. The Baby Bond’s proposal is estimated to cost about \$60 billion a year (Committee for a Responsible Federal Budget, 2019).

In addition, given we suggest there is also a need for additional assets to launch children into independent living and strengthen the return on degree, we suggest an additional investment of \$12,000 by the federal government. These payments would occur like Senator Booker’s proposal, an initial \$1,000 at birth for all children, and \$2,000 every year after phasing out in a similar fashion based on income (e.g., 100% of FPL = \$2,000; 125% of FPL = \$1,500; 174% of FPL = \$1,000, down to 500% of FPL = \$0), but after the first disbursement at age 18 (about \$45,000), payments would continue through until age 24 when a second disbursement would occur (about \$15,000). These amounts only include the federal investment. But as already discussed, CSAs are community accounts that allow for multiple streams of assets to flow into these accounts.

BABY BONDS AND CSAS SHARE A SIMILAR ORIGIN STORY

Previously Elliott (2022, October) has discussed how Baby Bonds share the same origin story as CSAs. And while this is true, it is important to point out that Baby Bonds are not built on a financial capability framework. And for reasons already presented in this report, it limits their utility. But again, because both CSAs and Baby Bonds share a similar origin story, Baby Bonds could be adapted to be more like a large-dollar CSA to fit a financial capability framework.

E. We Can't Afford Not to Make the American Dream of Equitable Return on Education Real in Americans Imagination

Senator Booker proposes to increase tax rates on investment income and inherited assets and estates to pay for his proposal. This would create about \$700 billion dollars in additional revenue, reducing the deficit by \$50 billion while paying the \$650 billion his proposal is estimated to cost (Committee for a Responsible Federal Government, 2019). But an asset accumulation version of free college proposal is not only a proposal for solving wealth inequality, it is a proposal to pay for college. As such, it is reasonable to see funding currently being spent on financial aid as a source of revenue to pay for this proposal. For the 2021-2022 school year, the federal government spent a total of \$234.6 billion on student aid, of that, \$82 billion was spent on federal student loans alone. There is also the budget that is currently being spent on the hidden welfare state (i.e., tax deductions with social welfare objectives that largely benefit wealthier families), about half a billion, a part of which could help fund such a proposal (Howard, 1997). The money is there, particularly for a program like this that extends beyond education and has the potential to be a main cog in solving wealth inequality as well as poverty long term. It just requires acknowledging that education in America is part of the social welfare system and that we invest in education as a way of creating not only a more educated citizenry, but to bring to life our ideal of living in a meritocracy.

Importantly, investment in asset building programs in America has a history of paying off. For example, in 1944 the US spent \$14.5 billion (about \$139.6 billion in 2020 dollars) on the GI Bill, nearly doubling the number of college graduates between 1940 and 1950 (Wells, 2022). Although this might have seemed expense to many, according to a congressional cost-benefit analysis it not only improved millions of lives, but after eight years, it had returned every dollar invested nearly seven-fold in economic output and federal tax revenue (Joint Economic Committee, 1988). A recent cost-benefit analysis estimates that for every \$1 invested in CollegeBound, a CSA program for all children born in the City of Saint Paul, society will receive \$9 back, “associated with increased income, improved health, additional tax revenues, and savings to the judicial and education systems” (Diaz, 2023). Investment in asset building programs as a way of financing education and strengthening the return on degree just makes sense.



XII

An Asset Accumulation Version of Free College Might Be Better than Tuition Free College

By proposing an asset accumulation version of free college, we are suggesting that CSAs are a better way to achieve free college. **That is, it is better to have children grow up with assets to pay for college, much like wealthy children do, than not charging them for college when they reach age 18.** This is because CSAs have been shown:

- to facilitate financial inclusion (Beverly, Kim, Sherraden, Nam, & Clancy, 2015)
- to improve financial capability (Birkenmaier, Kim, & Maynard, 2023)
- to increase wealth accumulation (Huang, Nam, Sherraden, & Clancy, 2015b)
- to have many social and psychological effects on parents and children that are linked to being prepared to attend college (Elliott & Harrington, 2016)

As a type of community account, CSAs provide scaffolding for additional assets to flow into these accounts beyond federal investments (Elliott, 2023, March). Moreover, the notion of tuition free college is limited to not charging for college, and thus places the focus on access to college as the problem largely ignoring the return on degree problem America has. In contrast, the asset accumulation version of free also has implication for wealth inequality, and ultimately poverty. Further, because an asset accumulation version of free college can potentially act as a strategy for greatly reducing or eliminating wealth inequality, it can potentially open additional federal (likely others as well) revenues to be used beyond expenditures on education. As Friedman (2015) points out, “The United States has a large existing tax policy to encourage asset building—more than half a billion

dollars in annual income tax expenditures is devoted to subsidizing homeownership, retirement savings, higher education, business investments, and other types of assets” (p. 390). However, currently most of these benefits go to the wealthy, Howard (1997) referred to this as the “Hidden Welfare State”. These monies would be better used to fund CSAs if for no other reason than all could benefit from them (i.e., inclusive).

It is also worth noting, in general these are very critical stages where an asset supported launch is needed regardless of whether a child attends a four-year college or some other form of postsecondary education or training. This is also why we have chosen an age, rather than upon graduating from postsecondary education or training. Some children would choose to use these funds to pay for college when they reach 18, as an investment in their human capital with the idea of being able to receive both the income and wealth premium a degree comes with. These premiums are likely to return to their previous levels, if not higher, because students would not leave with debt, but instead leave with assets (Emmons, Kent, & Ricketts (2019). Others might use it to pay for college simply so that they can enter an occupation they enjoy. Others would choose something other than college, but all would receive this investment. Phase outs (i.e., the wealthy would not receive additional funds, but all would receive an account) would occur based on income like Senator Casey’s proposal. The accumulated assets from the different streams of assets mentioned in this report, to include investment earnings, would remain in the account and continue to grow until age 24. These funds would serve to launch young adults into independent living while strengthening the return on degree and better positioning education as an equalizer.

Key Points on CSAs and the Return on Degree

- Facilitate financial inclusion by connecting children/families to financial institutions.
- Produce early social and psychological benefits—shown to be important predictors of future educational success—in children and their families.
- Create an environment for dreaming tangible dreams.
- Provide assets to pay for college, to achieve an alternative form of free college.
- Increase access to college and raise completion rates.
- Provide an institutional structure for developing financial capability.
- Provide a type of scaffolding for multiple streams of assets to flow into an individual child’s account.
- Act as a gateway to a diversified asset portfolio as an adult.
- Provide young adults with asset to launch into independent living.
- Reduce wealth inequality.

Finally, because these financial aid funds would not only be for students attending college but for children who reach the ages of 18 and 24 who choose not to attend college, **adoption of the financial capability framework of financial aid requires a shift from an understanding of financial aid as an investment in education itself, to understanding it as an investment in economic mobility more generally.** We have invested as a country in education to be a primary tool for providing everyone an equal opportunity to achieve financial outcomes in line with their use of effort and ability. If this is the case, then providing financial aid to all students for that purpose regardless of whether they attend college or not would fulfill the very purpose of providing everyone an equal opportunity to achieve financial outcomes consistent with their effort and ability.



XIII

The Financial Aid Continuum

Figure 1 places the different forms of financial aid on a continuum for strengthening return on degree based on a financial capability perspective. In sum, regarding the return on degree, CSAs are at the opposite end of the financial aid continuum than student loans. They exceed other forms of financial aid in providing an inclusive institutional structure for developing the financial capability of students while empowering them with the ability to accumulate assets.

Figure 1. A Financial Aid Continuum for Strengthening the Return on Degree Based on Financial Capability



The other forms of financial aid listed on the continuum do not provide an institutional structure for developing financial capability of students, nor do they provide students with access to financial institutions' asset-building arm. In fact, student loans reduce the amount of assets students have upon graduation, and merit-based aid often unfairly excludes low-income and minority students because wealthier children can provide institutions with more tuition dollars (Burd, 2020). While free college is inclusive and reduces the reliance on debt to pay for college, it also does not provide an institutional structure for developing financial capability, and it does not give students access to financial institutions asset building arm. Furthermore, it does not impact children's early social and psychological outcomes in the same way CSAs have been shown to do.

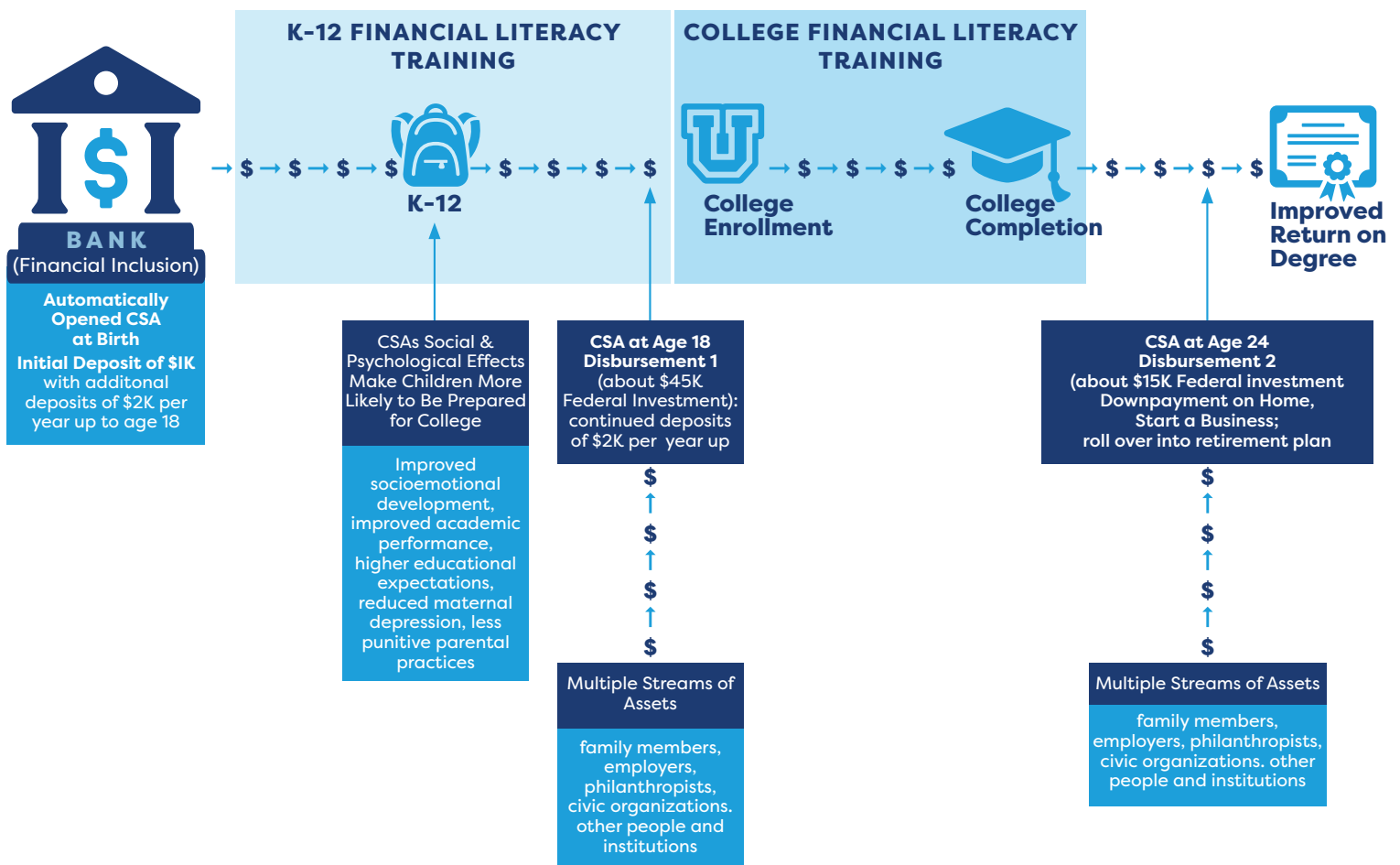
XIV

Conclusion

If all children had similar levels of education and faced similar economic conditions, children who worked harder and had more ability would be more likely to achieve a greater economic return on their degree than those who did not work as hard or who had less ability. This feels like what the ideal of meritocracy is meant to be. In this report we suggest that achieving this is impossible without leveling the playing field by ensuring that all children have similar access to financial knowledge and skills, similar access to financial institutions for building wealth, and enough wealth upon graduating that they have the same opportunity to build wealth later in life that their wealthier counterparts do. But as we have shown in this report, this does not currently exist. So, how do we get there? How do we make education the equalizer it was invested in to be.

In this report we suggest reimagining financial aid from a financial capability perspective that includes asset ownership. See Figure 2, it depicts a financial capability model of financial aid for strengthening the return on degree. In this model, CSAs provide all children with access to institutions (i.e., financial inclusion). Financial literacy training, delivered through K-12 schools, represents another component of financial capability. The last component of financial capability is assets. The CSAs' scaffolding allows for multiple streams of assets—including repurposed investments in financial aid, as well as contributions from families, community institutions, and other government revenues—to flow into the accounts all along the education pipeline, up to age 24. In addition to connecting children to the asset building arm of financial institutions and equipping children with an asset foundation from which to launch into adulthood, then, CSAs, provide scaffolding for delivering multiple streams of assets, the context for experiential learning within financial literacy training, and indirect social and psychological effects associated with improved educational outcomes. That is an integrated, expansive, and equitable model for making education a truly equalizing force within the lives of American families.

Figure 2. Financial Capability Model of Financial Aid



What makes the financial capability perspective of financial aid so potentially powerful is how each factor (CSAs, financial literacy, financial inclusion, assets, and education) increase the other factors' potential for producing wealth. We already discussed in this report and provided evidence for how financial knowledge and skills can lead to increased financial inclusion and wealth accumulation. We also discussed how CSAs are linked to financial literacy and inclusion, even how it is linked to improved educational outcomes. **However, we should also point out that holding a degree works like how we have described owning assets does. When children earn a degree, they also gain the corresponding characteristics of the degree and the institution that awarded the degree (e.g., prestige of school, social capital, an occupation/marketability, knowledge and skills in a particular field, experience, etc.) which in turn increases their opportunity to improve their financial capability.**

In this report, to conserve space we have not provided evidence on the link between earning a college degree and accumulation of financial assets particularly among low-income children (Wolla & Sullivan, 2017) even if the wealth premium is stronger for some and decreasing over time due to high cost of college (Emmons, Kent, & Ricketts, 2019). Nor

did we provide evidence on how education is linked to financial capability (Xiao, Porto, & Mason, 2020) and access to institutions (Yen & Qi, 2021). **Because all the factors work together to increase wealth accumulation, and strengthen each other's effect on wealth accumulation, they can be said to have a multiplicative effect on children's capability for increasing their wealth return on degree.**

In sum, the evidence indicates that wealthier children come to college and leave college with more financial capability—including more assets. With educational experiences shaped by multiple disadvantages, it is no wonder that education has never lived up to its designated role as an equalizer. Even considering only those who make it through the gauntlet to a graduation, degree holders are unequally prepared to maximize the return on their degree. We can see this in research presented in this report that indicates that lower income college graduates and graduates of color are not able to achieve similar returns on degree as their wealthier White counterparts do. Americans see providing economic opportunities for all as a main purpose of education, and keeping the American Dream alive requires that the education system delivers those opportunities. It is unfair and unwise that cultivating financial capability has not been an integral part of education. The knowledge that education must be combined with financial capability if that education is to serve the equalizing functions society expects must alter our understanding of the purpose of financial aid and the type of financial aid needed. Indeed, this evidence suggests that financial aid must provide children with the financial capability to leverage their degree truly, equitably, and durably—for their own economic success and that of our country.

APPENDIX A

Using Sen's Capabilities Approach to Understand the Role of Assets in Financial Capability

To evaluate people's well-being, the concept of functioning is proposed as an alternative to utility in utilitarian economics (Sen, 1999a). Functioning represents what the person succeeds in being and doing with the commodities and characteristics at their command or being/doing. In Sen's framework

$\left\{ \begin{array}{l} c(.) = \text{the function of converting a commodity vector into a vector of desirable characteristics} \\ f_i(.) = \text{a personal utilization function that } i \text{ can actually make use of commodities} \\ F_i = \text{the set of utilization functions } f_i \text{ } i \text{ can choose from} \\ h_i(.) = \text{"the happiness function of person } i \text{ connected to the functioning realized by } i \end{array} \right.$

If the person i chooses the utilization function $f_i(.)$, then with the possessed commodities, the achieved functions will be expressed as

$$b_i = f_i(c(x_i))$$

which represents functionings, which can be either beings or doings.

For a given individual, there are limited ways that they can feasibly utilize commodities, then their possible functionings are represented by the set $P_i(x_i)$

$$P_i(x_i) = [b_i \mid b_i = f_i(c(x_i)), \exists f_i(\bullet) \in F_i]$$

It is also the case that a person's choice of commodity is restricted to some set X_p , then their feasible functionings will be further restricted to the set $Q_i(X_i)$

$$Q_i(X_i) = [b_i \mid b_i = f_i(c(x_i)), \exists f_i(\bullet) \in F_i \text{ "and" } \exists x_i \in X_i]$$

Q_i can be referred to as the "capabilities" of person i , representing the range of choices in functionings available to them, based on their utilization of commodities and their ownership of these assets.

When it comes to the notion of financial capability, the possession of assets, therefore, is not merely the holding of economic goods but the holding of potential functionings. It is the foundation upon which capabilities are built (Sen, 1999a). Assets provide the means for individuals to realize a subset of functionings from a broader subset of them (Sen, 1999b). Assets, therefore, are not simply to be assessed in terms of their immediate utility or exchange value but rather in terms of their capacity to be converted—through the individual's unique utilization function—into a diverse array of functionings. This conversion crystallizes the concept of financial capability as an enabler for individuals to pursue a multiplicity of pathways toward well-being, rather than merely accumulating wealth (Sherraden, 1991).

Meanwhile, the breadth of X_i , the set of possible commodity vectors (i.e., assets in financial capability) defines the extent of one's financial capability, indicating the diversity of options and the freedom an individual possesses to achieve various life outcomes. A broad X_i signifies a rich array of potential functionings, implying a greater freedom to select pathways that lead to desired achievements and states of well-being. It is this breadth of choice, facilitated by the assets one can potentially command, that true financial capability is realized.

Therefore, assets are integral to expanding an individual's capability set, enhancing their potential well-being and autonomy. This reframes financial capability not just as the actual wealth or utility derived from assets but as the latitude of choices and potential life courses these assets enable.

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