How Single Men and Women Think Differently about Financial Risk — and Both Need More Financial Guidance

Efstathia Korkou, City University of New York

Individuals and households are, on a daily basis, required to make decisions related to consumption, savings, and investments. All of these financial decisions are plagued by risk – a complex concept with negative connotations and no single, agreed upon method of measurement. When faced with financial risk, individuals exhibit varying levels of risk aversion. This can be understood as reluctance to take risk, a well-known and often-studied characteristic of human behavior that happens when people face uncertain circumstances and consequences from present choices.

In decisions about investments, risk can be understood in terms of variation in returns on investment. Among investors, researchers have linked risk aversion or risk tolerance (the willingness to take on risk, the opposite of risk aversion) to individual characteristics like age, investment time-horizon, need of cash on hand, size of investment portfolio, income, investment knowledge, and attitudes about price fluctuations.

Of course, every investor is unique; hence the list of individual-level factors related to risk tolerance or aversion can be very long. However, gender is one investor characteristic that has gotten relatively little attention. Only a little research has been done on the relationship between an individual's gender and his or her investment decision making. In the 1990s, a stream of studies suggested that female investors are more conservative than men, in that they exhibit greater aversion to financial risk. Studies highlighted worrisome consequences, linking women's relatively high risk aversion to a reduced ability to meet long-term investment goals – such as acquiring enough wealth to retire comfortably. With lower average earnings and longer life expectancies – and thus, lengthier retirements than men – women were often strongly advised to take on higher risks in their investment strategies in order to secure higher returns for their retirement. Could they accept such advice if they are more risk averse?

Changes in Gendered Risk Aversion over Time

With earlier research findings and the aftermath of the 2007-08 financial crisis in mind, I have re-examined women investors' risk aversion. More specifically, building on the seminal works of economists Nancy Ammon Jianakoplos and Alexandra Bernasek – I have explored whether, in recent years, gender differences in financial risk aversion have increased, decreased, or stayed the same. Jianakoplos and Bernasek used data from the 1989 U.S. Federal Reserve Board's Survey of Consumer Finances to examine the risky asset holdings of households. They tested for gender differences by examining risky asset holdings by single women and single men. Along with other researchers, they found evidence of decreasing relative risk aversion for all single-headed households, but also found that single women still had greater risk aversion than single men.

In my own research, I replicated the Jianakoplos and Bernasek research with the same 1989 data and used the same approach again with data from 2013. My results from 2013 show that single men and women are both becoming more risk averse – or less likely to take risk. And I also find that longstanding gender differences persist. Why are both single men and single women more likely to avoid risk in 2013 than 1989? One possible reason is that the 2007-08 financial crisis made most people painfully aware of their vulnerability and exposure to risk, and thus, more aware of the need to protect their financial holdings against the possibility of a large, negative event like that financial crisis.

Policy Recommendations

Given my analysis of the 2013 Survey of Consumer Finances data and recent trends for single men and women, a number of recommendations make sense for policy makers, researchers, and others concerned about the health of the economy:

- The financial decisions of all households headed by single men or women should be monitored more closely. This is especially true for investment decisions related to retirement – including choices about whether to participate in employer's 401(k) plans and other thrift saving accounts.
- Risk taking patterns of single parents and other single household heads with young dependents in their households should also be monitored carefully. The 2013 data suggests growing relative risk aversion among single female parents, and a constant risk aversion among single male parents, even though there is some evidence that, over time, single mothers with additional young dependents are willing to take more financial risks.
- Single-headed households should be given an extra push to take on reasonable risk in their investment portfolios. One way to accomplish this would be to make 401(k) and other retirement plans something workers must opt out of, rather than positively opt into.
- Because single parents are more vulnerable to financial hardship yet more risk averse, they can especially benefit from financial counseling and investment advice.
- Further research is needed to understand how individuals' financial literacy influences their willingness to take risks – because single college graduates actually take significantly fewer financial risks than their peers with less than a sixth grade education.

Because the acceptance of risk is necessary at the macro level for a healthy economy and necessary at the individual level for smart retirement plans – it is essential that policymakers, civic and business leaders think carefully about the importance and spread of financial education. Given what we know about relatively high risk aversion among college graduates, it is important to better understand how education about finances, not just education in general, might help people become willing to take rational financial risks. Available evidence suggests that financial education should be implemented early and for more people, and such instruction should emphasize people's need to take wise and timely financial risks to secure the financial returns they need for their retirements and to meet other important life challenges.

Read more in Efstathia Korkou "Women and Financial Risk Aversion: A Study Over Time" (paper presented at the 43rd Annual Conference of the Eastern Economic Association, 2017).