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## Financial management in households

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**Key words:** management, funds, financial decisions, settlement of liabilities, savings, investments

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**Summary:** The main objective of a household is to meet its members' needs and aspirations. In order to achieve it, the household has to pursue the appropriate financial policy. As a result of budgetary restrictions, consumers face the necessity to consider numerous financial issues and take proper decisions.

The subject of the article is the finance of households. It discusses the financial decision making process in households and fund management in a household. It shows the conditions of accumulating savings and retaining them, pays attention to their diverse character, presents the goals of saving in Polish households. Moreover, the article discusses the conditions of converting savings into investment and the risk related to it. It also shows the size and the structure of financial assets of Polish households.

### 1. Introductory remarks

The main objective of a household is to meet its members' needs and aspirations. In order to achieve it, the household has to pursue the appropriate financial policy. A condition of fulfilling needs and aspirations is the possession of proper income and its skilful management. As a result of budgetary restrictions, consumers face the necessity to consider numerous financial issues and take decisions regarding expenses, savings, borrowing and investing.

The financial aspect is present in the whole activity of a household—in buying, borrowing and keeping goods. It also performs a significant role when taking decisions concerning the method of paying for a purchase—whether to buy for cash or

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buy on credit. For these reasons, financial behaviours of households have become a subject of interest of broader and broader group of various economic institutions, first of all banks and insurance companies. Recognizing and understanding these behaviours by banks and insurance companies is a condition of attracting consumers with good creditworthiness.

Not only financial institutions but also state authorities are interested in financial behaviours of households. For the latter, the knowledge about financial behaviours of households is important when organizing assistance for consumers who have found themselves in the situation of a problematic debt. Paying attention to cash management, saving and borrowing is also important from the point of view of the consumer protection. One of the objectives of the state policy towards a consumer is the protection of households with low income, particularly against misleading information concerning credit opportunities and all kinds of financial mistakes that may arise from them.

## 2. Making financial decisions

In every household, various financial decisions are made. The decisions concern: managing funds, financing purchases, accumulating savings and multiplying wealth. Decisions regarding these issues may be made individually or collectively, jointly by all members of the household. However, the latter may be made in a various personal arrangement, e.g. the husband and the wife, parents with children, all members of the household (1, p. 32).

An important factor shaping financial behaviours of consumers is *the role of a husband and a wife in making decisions in the family*. Depending on what role the husband and the wife perform in decision making, we can indicate five types of managing finance by married couples (2, pp. 446–447):

- with the *dominating role of the husband*, the finance is managed by the husband and he provides the wife with money for everyday domestic shopping;
- with *joint management with a bigger share of the husband*, financial issues are dealt with by both spouses. They have a joint current account and a savings account. The husband pays bills, watches over the repayment of the mortgage loan and performs most of the financial transactions. This type of financial management occurs mainly in households with higher income;
- with *independent management*, the husband and the wife manage their own financial issues and they have their own current and savings accounts. Only in case of important purchases they communicate with each other. This type of financial management occurs mainly in households with high income, e.g. when both spouses have income;
- with *joint management with a bigger share of the wife*, both spouses deal with financial issues. Financial transactions are conducted by the wife. This type of management occurs mainly in households with average income;

- with the *dominating role of the wife*, all financial issues are managed by the wife and she gives her husband some pocket money to cover his expenses. This type of management occurs mainly in households with low income.

In reality, the presented types of managing finance are more complex and to a great extent depend on who earns money, who does shopping and who pays bills.

It should be noted that as a rule the main breadwinner has bigger influence on financial management than other members of the household. The possessed knowledge on finance also plays an important role. The one who is an accountant by profession often deals with the finance of the household, too.

### 3. Managing funds

Consumers meet the majority of their needs by means of products they come into possession by purchasing them. 'Doing shopping has both an instrumental and a hedonistic character, doing everyday shopping and shopping for pleasure, respectively. The hedonistic function may have both the individual and the social dimension. The man gains new experience and meets other people. Shopping may bring pleasure and for many consumers it is a form of relaxation. This is proven by crowds of buyers appearing in shops on Sunday' (2, p. 438).

Not every purchase is felt by consumers as a pleasure. Only the purchase of elective goods or a periodical purchase of, for example, clothes, jewellery, personal computers or cars, can be a pleasure. On the other hand, everyday shopping for needed things is considered necessary and important but not giving pleasure.

In numerous households, one person is responsible for shopping, paying bills and other tasks related to financial management. The role of a purchaser in a one-person household is usually performed by the consumer himself/ herself. In multi-member households, the role of the purchaser is divided among a few people or is performed by a person particularly predisposed to it. Most often it is the husband or the wife.

The roles of the husband and the wife in initiating a purchase, gathering information about the product and taking final decisions about the purchase, as well as with reference to individual elements of the purchase, are varied. The husband more often takes decisions about the purchase than the wife does when he has a higher level of education and professional status than his wife, when the wife does not work professionally, when there are a lot of children in the family and in the early stages of the marriage life, when children are young. Moreover, the husband more often makes decisions about the purchase of expensive goods, often having prestigious significance. On the other hand, the wife makes decisions about the purchase of products related to the furnishing of the flat and running the household.

Behaviours of households on the market are very diverse. They may be rational or irrational.

A household behaving rationally plans shopping. It confronts its expenses with its income and takes balanced decisions on how to spend it. A rationally behaving consumer is the one who goes to a shop with the shopping list and buys in accordance with it. A consumer who does not control the content of his or her basket or trolley with the previously prepared list of necessary products buys much more than the one who controls it. It is also worth noting that the shopping list lets omit numerous traps set by merchandisers for consumers to persuade them to buy—exposing of goods in the shop adequately and arranging them on shelves, the lightening of the shop, fragrances, selected music, the structure of prices (PLN 99.99), etc.

Irrational behaviours stand for shopping without a plan. When doing shopping, consumers behaving in such a way are guided by what they see on the shelves. They walk along the aisles and realize that they need oranges, cherries in chocolate, cocoa or coffee. This method of doing shopping makes them buy more than they were going to, often of unnecessary things. Consumers behaving in such a way are easier to be persuaded to buy more than what is necessary (3, pp. 189–199).

A lot of consumers often buy products they did not intend to buy before entering the shop. It is buying on impulse, often as a result of sudden, uncontrollable impulse. It is an irrational behaviour. However, it should be noted that buying on impulse occurs with various intensity and not always it is an unplanned purchase although the purchased product is not on the shopping list.

The behaviours of households on the market influence the condition of their finance. A household buying products can save its money or spend more than it earns. By analyzing expenses a rational consumer can prevent excessive and unnecessary slimming of his or her wallet. There are a lot of possibilities of rationalizing expenses and lowering their values through it. Thus, for example, it is worth buying groceries in super- or hypermarkets where they are cheaper than in traditional grocery stores. Savings that can be made monthly by buying in big markets are considerable. Big savings can be also made by buying products on the street markets or on the market-places where they can be bought at a lower price than in a store.

#### 4. Settlement of liabilities

Households pay for the purchased goods in different ways—in cash, by payment card, by cheque. Some prefer to pay in cash, others by payment card. Households also make payments by transfer. In particular, it concerns regular payments, such as: the rent, utilities or insurance premiums. Consumers make those payments in the bank in person. They may also be made by transfer as a standing order or direct debit.

A modern form are more and more frequent electronic banking transactions made from home by means of a computer.

Consumers settle a lot of payments in cash.<sup>1</sup> It is a traditional method of paying bills and a form of direct payment. It means settlement of the amount due directly at the counter or at the cash desk.

As a rule, consumers pay small amounts in cash. A consumer usually pays for products of low price, fulfilling the basic needs, being the object of everyday shopping.

Paying in cash has its advantages and disadvantages. Consumers carrying cash with them incur the risk of having it stolen. By paying in cash consumers 'rationalize' their expenses, reducing them to the sum they have on them. Some consumers use it to control expenses, carrying only a limited amount of money, which does not let them spend more. It is an expression of self-control.

One of the methods of payment is paying by cheque. This way of paying is more comfortable for a consumer than paying in cash, particularly in case of unexpected expenses. By a cheque we understand a written order of definite paying out of some monetary amount, given to the bank by the owner of the bank account (Cheque Law Act, Journal of Laws of 1936, no. 37, item 283 with later amendments). Cheques have both pros and cons. For the consumer, an unquestionable advantage of a cheque is the easiness of performing non-cash operations, and his responsibility is limited in case of the theft of the cheque. Its disadvantage is the easiness with which a cheque can be forged.

As legal tender, cheques have found broad application mainly in the English-speaking countries. In Poland they did not enjoy particular popularity.

A lot of consumers make payments by payments cards. They can be considered an equivalent of cash. Their advantages make them enjoy more and more popularity, enabling to make payments and use cash.

A payment card is a card 'identifying the issuer and the authorized owner, entitling to pay out cash or make payment' (The Banking Law Act of 29 August 1997, consolidated text Journal of Laws 2012, item 1376, Art. 4, section 4). It enables to withdraw cash from a cash machine or make non-cash payments for goods and services.

The owner of a payment card does not have to carry cash because by means of it he can settle various liabilities. One can pay with it practically in all sale and service establishments: in a shop, at a chemist's, in a petrol station, on the motorway or in household appliances repair services.

Payment cards in Poland are a relatively new tool. The first payment cards appeared in our country by the end of 1960s. The development of payment cards in Poland took place in 1990s. However, significant growth could be observed only after 1994 (see Figure 1). The dynamic development of the payment card market contributed to the fact that cards have become in Poland the most frequently used form of non-cash monetary settlements applied in retail payments (4, p. 6).

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<sup>1</sup> Cash consists of paper banknotes and metal coins.

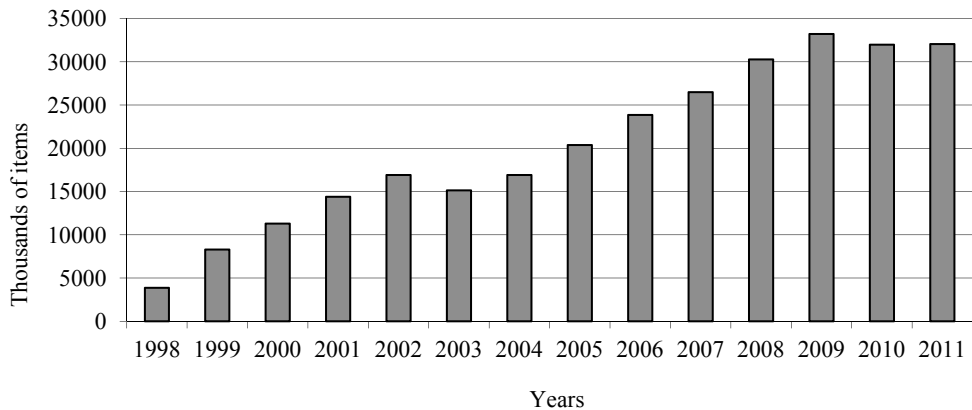


Figure 1. The number of the issued payment cards in the years 1998–2011

Source: Author's own study on the basis of the materials of the National Bank of Poland (<http://www.nbp.pl>).

Payment cards have become in Poland almost a common form of payment without which it is difficult to imagine the majority of transactions. At present, banks offer varied payment cards to customers. Depending on the adopted criterion of division, we can classify them differently. One of more often used criterions of the payment card division is the way of settling transactions. When using this criterion, we can distinguish the following cards: credit, debit, charge, prepaid (also called the electronic purses) cards (5, p. 21; 6, p. 22; 7, p. 21).

## 5. Savings

Apart from settling current fixed liabilities, managing finance in households also includes creating and retaining savings.

A possibility to save appears only when the funds of a household are big enough that after fulfilling the basic needs, the financial surplus is left. The skill of managing money in such a way that the income is always bigger than the expenses is a source of achieving wealth and prosperity in life. Such managing money is a source of savings.

To achieve success and happiness, financial security is necessary. The appropriate level of savings can ensure it. In order to achieve it, first of all one should (8, p. 145):

- define the aims we want to achieve;
- change the way of thinking from the consumption to the pro-saving one;
- define the optimum level of income and expenses;
- change buying mechanisms and habits, not to buy on impulse;

- limit buying on credit for the benefit of buying financed from the interest-bearing savings;
- earn on savings, investing them reasonably.

Saving is understood as a consumer's refraining from ongoing consumption for the benefit of its increase in the future (9, p. 14). In other words, saving is keeping a given part of one's income for the future.

Saving may be of a voluntary or a compulsory character. Voluntary saving means conscious, free from external pressures resignation of a consumer from spending some of his or her income on the ongoing consumption purposes. On the other hand, compulsory saving is saving in which a consumer, forced by law, resigns from spending some of his or her income on consumption. Compulsory saving includes, for example, paying pension contributions and life insurance premiums. The latter often occurs on the basis of employee collective agreements.

Voluntary saving includes all kinds of savings about which a household decides freely whether to save money or not. An example of accumulating savings and their free disposal is a savings account in a bank.

Voluntary saving includes: residual saving, precautionary saving and special purpose saving.

Residual saving, also called unintended saving, occurs when the expenses of a household (by the end of the month) do not exceed its current income.

Precautionary saving is the accumulation of funds for the occurrence of unexpected events. Creating and retaining this kind of savings requires discipline from the household so that they were not spent on consumption.

Special purpose saving is putting aside money for planned transactions, e.g. the purchase of durable goods, a foreign trip, a holiday or an overhaul of the flat.

The aims of saving of the Polish households are shown in Table 1. What results from the data presented in the Table is that the Poles primarily save for unexpected fortuitous events, this aim was shown by about 70% households in the years 2000–2011. The second reason in the hierarchy of importance was the financial securing of the old age period. Significant aims of saving in households were in that period as follows: treatment, reserves for consumer spending, as well as the renovation of the flat or the house. The hierarchy of the aims of saving of the Polish households presented in Table 1 clearly shows the prevalence of precautionary motives.

Table 1

The aims of saving in the Polish households in the years 2000–2011 (in %)

The aims of saving	2000	2003	2005	2007	2009	2011	Average 2000–2011
Reserve for fortuitous situations	75.6	72.1	70.6	65.8	61.1	61.5	67.6
For the old age	–	43.6	44.9	39.9	36.1	36.5	40.0
Medical treatment	44.7	39.6	42.1	34.5	29.2	25.0	35.1

The aims of saving	2000	2003	2005	2007	2009	2011	Average 2000–2011
Reserve for consumer spending	40.2	34.8	31.0	35.1	30.5	33.2	34.0
Renovation of the house, the flat	37.6	39.1	35.8	32.8	28.4	25.0	32.7
For children's future	35.0	31.2	30.9	28.7	25.0	23.2	28.7
Relaxation	30.6	29.3	31.3	29.5	26.4	23.5	28.3
Purchase of durable goods	34.5	27.9	29.6	29.5	25.6	22.7	28.1
For other purposes	20.4	18.4	19.3	17.8	17.0	14.0	17.7
For fixed payments	20.2	20.8	18.5	15.5	14.1	12.0	16.5
Without any purpose	11.3	9.9	12.2	8.7	11.4	10.1	10.5
Purchase of a flat, house	11.8	12.1	10.5	8.7	8.7	6.4	9.5

Source: 10, p. 41.

Voluntary saving is conditioned by the expectations concerning income and the economic prospect. Households whose income increased in the previous year and which expect its increase in the following year do not save much. On the other hand, households whose income stays on the same level or decreased in the previous year, and they do not expect its increase in the following period, save a lot. In other words, when households have positive expectations concerning their income, they save little. If, on the other hand, they have negative expectations, they save a lot.

Expectations concerning income influence both the way of saving and the quantity of the saved amounts. Positive expectations of households concerning income make them save less, and borrow more. In case of negative expectations, households save more and borrow less.

Negative expectations of households with regard to income usually contribute to their striving for accumulating precautionary savings for the event of unexpected events, and ensuring financial stability in the future. As a rule, they are also afraid of doing big shopping, especially on credit.

Saving is influenced not only by expectations concerning income but also the interest rate of the deposit and inflation. The latter give consumers an answer to the question about the sense of saving. A positive answer inclines to save. However, when the interest rate is low and the inflation is high, saving is not reasonable.

Inflation is basically a phenomenon constantly accompanying economy. For example, in Poland in the years 2001–2012 it shaped from 0.7 to 4.3%. In 2012, inflation in Poland was 3.7% (11, p. 23). This is the value by which the value of our money dropped during that year.

Therefore, a household wishing to secure its money against the loss of its value looks for tools which will enable to at least considerably reduce this phenomenon, if not eliminate it. One of such instruments are deposits, on the condition that they bear appropriate interest. Thus, for example, in case of the inflation of 3.5%, the safety of



savings is guaranteed by the interest rate of the deposit above 4.33% annually (12, p. 91). Such an interest rate on savings, however, does not ensure obtaining profit on the capital. Therefore, they do not incline households to save.

It should be noted, that the proneness of the Polish households to save is low. It is proven both by the data from the National Bank of Poland and the findings of the research conducted in Poland by various research institutions. They inform that in the years 1995–2012, as many as 70–80% of the Poles declared having no savings at all. The research also proves that the scarce group of the saving Poles is distinctly dominated by people who had the lowest savings, that is at the level of income from the last 3 months. The percentage of people with savings at this level among the total number of the saving people fluctuated in the years 1995–2012 from 63–73% (10, pp. 27–29).

## 6. Investment

Saving consists in putting aside money for a purpose. If a household has saved much enough to cover necessary later expenses, it considers a possibility to invest their money. Investing is disposing savings for future benefits.

When investing, a household makes a decision about depositing funds in various kinds of ventures expressing in (8, p. 178):

- winning tangible assets by means of a purchase (real estate, companies, etc.);
- generating tangible assets by oneself (building a house);
- purchasing or creating new non-usable assets (works of art, precious metals, precious ores);
- purchasing securities (e.g. shares, government bonds, treasury bonds).

Thus, we can distinguish tangible and financial investment. In case of tangible investment, the object of the investment is of material character and a household, as an investor, expects that the value of the object of the investment will increase in time. In case of financial investment, the object of the investment is of immaterial character. Tangible investment are the flows of goods as a result of the exchange of funds into material goods in order to achieve additional income in the following periods. Financial investment is a transfer of funds (the flow of capital).

When investing, a household takes a risk to achieve bigger profitability than in case of savings. The risk consists in losing a part of the entirety of the invested funds. The risk a household takes by investing is bigger or smaller. It depends on the kind of an investment project. The most risky are, among others, shares, investment funds, forward transactions and certificates of deposit. Less risky are bonds, deposits, real estate and precious metals.

To diminish risk, households should not invest all the possessed money in one financial instrument but the forms of investing capital should be diversified into shares, investment funds, bonds, deposits, and similar financial instruments.

Table 2

The value of financial assets of households in Poland in the years 2001–2010  
as of the end of the year in billions PLN

Specification	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Total	335.2	365.9	400.4	434.7	509.2	624.0	738.9	738.1	854.4	966.1
Bank deposits	219.4	213.0	209.8	207.4	218.4	232.1	267.5	336.6	387.9	425.9
Funds accumulated in OFE (Open-End Pension Fund)	19.5	31.5	44.8	62.6	86.1	114.2	139.7	138.0	178.6	221.3
Investment funds	10.1	20.5	30.4	34.4	58.0	92.4	109.4	50.9	62.4	75.5
Unit-linked insurance plan and premiums	20.8	25.6	30.0	35.2	41.8	51.8	62.8	67.9	68.4	74.1
Shares listed at the Stock Exchange	9.7	8.0	11.2	18.7	26.0	44.9	61.3	28.0	41.9	51.1
Treasury securities	16.1	20.5	19.2	20.4	16.8	12.5	10.3	13.3	12.8	10.1
Non-treasury securities	–	–	–	–	–	–	3.7	3.0	2.6	1.9
Deposits in SKOK (Loan and Savings Cooperative Society)	1.7	2.2	3.2	3.9	5.1	5.6	6.7	8.9	11.1	13.0
Cash in circulation (without bank counters)	38.2	42.1	49.2	50.9	57.0	67.4	76.8	90.8	89.7	92.7

Source: 10, p. 34.

The value of financial assets of households in Poland is presented in Table 2. What results from the data presented in this Table is that the total savings of the Polish households increased in the years 2001–2010 almost three times. The data show that households basically accumulate funds on bank deposits or in cash. The savings are mainly a reserve for unexpected fortuitous events and the security for the old age.

In the strategy of households referring to savings, the option of investing funds in safe financial products, namely bank products, prevails—in the form of a personal account, a fixed-term deposit and a savings account. However, investing in real estate, investment funds, investment deposits is not very popular, with the relatively frequent keeping cash at home (13).

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## Zarządzanie finansami w gospodarstwach domowych

**Streszczenie:** Głównym celem gospodarstwa domowego jest zaspokojenie potrzeb i aspiracji jego członków. Aby to osiągnąć, musi ono prowadzić odpowiednią politykę w zakresie finansów. Wskutek ograniczeń budżetowych konsumenci stają przed koniecznością rozpatrywania wielu spraw finansowych i podejmowania odpowiednich decyzji.

Przedmiotem artykułu są finanse gospodarstw domowych. Omówiono w nim proces podejmowania decyzji finansowych w gospodarstwie domowym oraz zarządzanie środkami finansowymi w gospodarstwie. Ukazano warunki gromadzenia oszczędności i ich utrzymania, zwrócono uwagę na różny ich charakter, przedstawiono cele oszczędzania polskich gospodarstw domowych. W artykule omówiono także warunki przekształcania się oszczędności w inwestycje oraz ryzyko z tym związane. Ukazano też wielkość i strukturę aktywów finansowych polskich gospodarstw domowych.

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**Słowa kluczowe:** zarządzanie, środki finansowe, decyzje finansowe, regulowanie zobowiązań, oszczędności, inwestycje

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