Lessons from Behavioral Economics and a Credit Repair Program in Boston

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(Based on joint work with P&CA Department and City of Boston)
Savings and Borrowing: The Issue

Revolving Credit Per Capita and Personal Savings Rate

Source: Haver Analytics
Board of Governors of the Federal Reserve System. "Consumer Credit." G.19 (421)
The Credit Repair Program

• Credit repair program
  – Offer counseling ‘light’: credit report (including FICO) and how to read it
  – Referral to professional counselors

• In 2006 in 1 VITA site with 155 clients
• In 2007 in 2 VITA sites with ~700 clients
• To be continued in 2008 with ??? clients
Two questions for credit repair:

• Why do people get into debt? Behavioral economics explanation
• Who selects into counseling programs?
Behavioral Economics of Asset Building

• Saving and borrowing is an *intertemporal* decision
  ➢ How do people think about the future?
  ➢ How do they delay instantaneous gratification?

• As some of us know from introspection, delaying instantaneous gratification is not that easy (e.g. planning vs. eating of unhealthy food)
• This is human – and not conditional on income!
Research Project in VITA sites

• Asset building of LMI individuals
  – Why do people get into credit problems?
  – How should public policies be tailored?

• Measuring who appears time inconsistent (i.e. violates plan when future becomes present) and whether it affects asset building
Self-Control and Debt

Notes: Debt Level = Outstanding Balance on Revolving Accounts on Credit Report (in Dollars). N = 556. Difference is statistically significant on the 1 percent level.

Source:
Self-selection into programs

- Who is getting help OR who is becoming financially literate?
- Remember, we offer free credit scores to individuals

- Only 55% take the offer!
- Do they differ?
Selection of More Patient People into Educational Programs

Notes: Discount factors measured in choice experiments. N = 778. Difference is statistically significant on the 1 percent level.

Discount factor = "How much is a $ in a month worth to you today?"

Get informed  Don't get informed

0.7  0.75  0.8  0.85
Selection is an big issue!

• In particular, people who get scores are much more patient

• Implications:
  – Evaluation studies are biased
  – We do reach only fraction of people
  – We might miss those who need it most!
Conclusions

• Successful credit repair program in Boston
• Key learning from research to improve program:
  – Take behavioral factors more seriously
  – Minimize selection effects
  – Maximize impact on behavior