Integrating Financial Capability Into Public Policy

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2013
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www.usfinancialcapability.org - clickable map

- 55 percent living paycheck-to-paycheck
- 60 percent do not have a rainy day fund to cover three months of unanticipated financial emergencies.
- On average 3/5 financial literacy questions correctly
Key Issues

- Innate Numeracy & IQ
- Education Level
- Access to institutions, products and information

Domains:

- Current income and consumption levels
- Intertemporal planning and choices
- Risk awareness and management
- Skills: Coordination and paying attention
Why Bother?

- Long-term shift of personal financial decision making to the level of individual
- Accelerated use of technology in financial transactions
- Democratization of access to credit
- Special issues for low-income, people w/ disabilities, seniors
- Lack of experience in financial markets and financial decision-making

Regulations, behavioral strategies (defaults, etc.) can alter behavior
How to foster dynamic adaptation?
Everyone’s Goal = financial security

Choices = tradeoffs
- Savings may not be goal; paying bills, debts, paying for ‘needs’
  
  e.g. Emergency savings = cash in pinch or spending on ‘social mobility’
Fast Friendly Service

$50. to $500.

Payday Loans

No Credit Checks

Same day service
Compared to What?

<table>
<thead>
<tr>
<th></th>
<th>FEE</th>
<th>APR^1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overdraft Protection &amp; Non Sufficient Funds (NSF) Fee</td>
<td>$28.95</td>
<td>621.57%</td>
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<tr>
<td>Overdraft Protection Fee</td>
<td>$27.00</td>
<td>579.71%</td>
</tr>
<tr>
<td>Credit Card Late Fee: 1st Time Late</td>
<td>$25.00</td>
<td>536.76%</td>
</tr>
<tr>
<td>Credit Card Late Fee: 2nd Time Late</td>
<td>$35.00</td>
<td>751.48%</td>
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<tr>
<td>Utility Late/Reconnect Fee</td>
<td>$46.00</td>
<td>987.65%</td>
</tr>
<tr>
<td>Payday Loan</td>
<td>$15.00</td>
<td>322.06%</td>
</tr>
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Empirical/Field Evidence

- Literature still young
- Evidence of effects of financial literacy education are weak at best

Problems...
- Selection problem dominates
- Highly Heterogeneous Programs
- If RCT is the gold standard, not meeting it
- Also lack of standard measures

1 http://ssc.wisc.edu/~jmcollin/JCA_published.pdf
Complications

- Who participates and why? Who does not?
- Time for program and time for impacts to take effects
- Have reliable and valid measures
- Keeping ‘subjects’ - attrition & incentives
- Variation in effects by client type (heterogeneous effects)
- **Fidelity** to program model—staff are consistent in who gets program and what participants are exposed do
- Comparison or contrast group hard to find
- Often ‘true’ effects of a single program are small and noisily measured = larger unknowns or error; Null finding is common
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A Few Examples

- Schools
- Job Training
- Housing
- Retirement
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Mandating Financial Education in Schools

- Little (or mixed) evidence
- Economics education
- Targeting by school/district
- Movements in testing; integration

Banking in Schools

- Study in process
Field Experiment

Financial Capability for Youth

Eau Claire, Wisconsin
• 2011-2012
• 2012-2013

Amarillo, Texas
• 2012-2013

Looking Ahead
Estimated Effects: Bank in School

% Banked

Baseline  Follow-up

No Bank (658)  Bank in School (706)
Estimated Effects: Deposits

Net Deposits by Week - Eau Claire
3-week moving average ($)

Education

Estimated Effects

Deposits

Net Deposits by Week - Eau Claire
3-week moving average ($)

Education
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Assessing Financial Capability Outcomes (AFCO)

- What does community-based Credit Counseling do for low-income employees?
- Focus on credit report outcomes
Counseling Integrated into Job Training

Table 6. Changes in POP Population over the 12-Month Study

<table>
<thead>
<tr>
<th></th>
<th>Baseline</th>
<th>6 Months</th>
<th>12 Months</th>
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</thead>
<tbody>
<tr>
<td>Credit Score</td>
<td>558</td>
<td>561</td>
<td>570</td>
</tr>
<tr>
<td>Banked</td>
<td>34%</td>
<td>59%</td>
<td>54%</td>
</tr>
<tr>
<td>Uses alternative finance</td>
<td>74%</td>
<td>70%</td>
<td>64%</td>
</tr>
<tr>
<td>Employed full time</td>
<td>100%</td>
<td>6.9%</td>
<td>12.1%</td>
</tr>
<tr>
<td>Employed part time</td>
<td>0%</td>
<td>11.5%</td>
<td>23.1%</td>
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Estimated Effects

![Bar graph showing Percentage of Debt Past Due over time (Initial, 6 mo, 12 mo) with comparison between Control and Treatment groups.]}
Counseling seems to have impact on behavior

- Increase in credit scores (modest)
- Reduction in revolving debt
- Fewer accounts in collections
- Counseling may discourage take up of bank accounts and direct deposit
Integration Lessons

- Integrating Access—communication, incentives, hassles
- Successful Account Management is Challenging
- ChexSystems - limits banking
- If you build it . . . they may not come
- Financial Fragility Limits the Interventions
Mortgage Default Counseling

- 5 + million households at risk of foreclosure
- Policy Response: Making Home Affordable Program (MHA)
  - Some portion (perhaps a majority) of borrowers fail to make reciprocal contact with lender/servicer
- Policy Response: National Foreclosure Mitigation Counseling (NFMC) Program

(JPAM, 2011; JCA, 2012; JPAM, 2013)
Disclosures

- Warnings Disclosures for Mortgages (JCA R&R)
  - YOU MAY LOSE YOUR HOME AND ANY MONEY YOU HAVE IN IT
    - Dread Risk - dimension of risk assessment that dominates (vs. unknown)
    - Signatures may focus attention—signaling
  - About 20 percent increase in borrowers agreeing to high cost loan offers due to stronger state disclosure policies
Other Policies—Not Disclosures or Education

- **Mortgage Mediation (EJ forthcoming)**
  - Increased modifications and more favorable terms
- **Moratoria on Filings (JPubE review)**
  - Modifications more likely; no evidence of moral hazard
- **Servicer Reporting of Defaults and Modification Rates (JEBO R&R)**
  - Servicers less likely to let loans fall behind and not take action
- **Repayment Reminders (JPAM review)**
  - Reduced defaults by nearly 40% in first year
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• Challenging to forecast
• Employer-based options matter strongly
2 Retirement Education Studies

1. Getting started
2. Basics of personal finance
3. Basics of investing
4. Retirement planning
5. Retirement saving strategies

Each about 60 minutes to get through online, including review quizzes (mastery model)

→ Cost about $22 per employee ($30k for 1500 employees)
Introduction to Building an Emergency Fund

Life throws lots of surprises at you, many of them financial: the refrigerator dies, the radiator on the car goes out, we get a surprise tax bill, or a job is terminated. If you lack an emergency fund there are other options, including credit cards, payday loans, pawnshop loans or loans from family members or friends. Each of these options have their own problems: high interest rates, making them difficult to pay back, as well as potential conflict with people close to you.

It's at that point, when you hit a financial bottom, when you realize the importance of setting aside a certain amount of cash for unforeseen occurrences. Doing so can buy you peace of mind while sacrificing spending for the short term. Ideally, you want to have this cash saved up sooner rather than later so that you don't suffer a major inconvenience when something does go wrong.
What Investments Are Suited for Automatic Savings and Investment Plans? (Quiz)

Savings accounts can be ideal candidates for automatic investing plans ________.

- Only for the short term
- Only for the long term
- Incorrect.
- For either the short term or the long term

The correct answer is: For either the short term or the long term. They are ideal for the risk averse, over either the short term or the long term.
Summary of Budgeting

Everyone has a budget—it’s just not always a written one. When you write down a budget, you have moved up to cash-flow management. This allows you to get a better grasp of your finances and helps you identify areas in which you can economize. If you use the principle of “pay yourself first,” you will avoid the debt trap that can ruin a budget with excess interest. A sound budget is key to successful investing.

Practical Ideas You Can Start with Today

- Determine your current cash flow. [Use this calculator.]
- Determine your projected cash flow. [Use this calculator.]
- Make a budget that balances your cash inflows and expenses.
- Pay yourself first by withholding a chosen amount from each paycheck and putting it into savings. [Use this calculator to estimate how your savings could grow.]
Findings for Public Employees

- Low take up rate: 23% of responders in treatment sample started course
- Self-assessed knowledge increased
- Knowledge test scores also increased
  - Effect sizes small—roughly 1/6th of the standard deviation
    - Using Bloom estimator perhaps as much as 2/3rds of std. dev.
- No observed effects on behaviors...but employees had fully-funded defined benefit pension
Findings for Private Employees

- Credit Unions employees in Wisconsin
- Could complete the modules at work–offered incentives to do so
- Randomized wait-list control design (by credit union)
  - Can compare “Fall Cohort” CUs to “Spring Cohort” CUs
Change in Self Reported Behaviors

- Opened an IRA: 8%
- Established a budget: 6%
- Drafted a written financial plan: 5%
- Set aside 3 months’ expenses: 5%
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‘Housing Choice Vouchers’
- Verify income, assets, etc. annually
- Family Self-Sufficiency (FSS) program allows families to earn income without losing vouchers

Required to complete classroom financial education course
- 181 FSS clients needed to complete financial education by the end of 2007
- 144 consented to participate in study
- 73 treatment / 71 control
Baseline Characteristics of Treatment and Control Groups

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<thead>
<tr>
<th></th>
<th>Control</th>
<th>Treated</th>
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</thead>
<tbody>
<tr>
<td>Savings</td>
<td>718</td>
<td>627</td>
</tr>
<tr>
<td>Net Wealth</td>
<td>-11,909</td>
<td>-12,599</td>
</tr>
<tr>
<td>Tenant Rent</td>
<td>359</td>
<td>427</td>
</tr>
<tr>
<td>FICO Score</td>
<td>566</td>
<td>577</td>
</tr>
<tr>
<td>White</td>
<td>0.27</td>
<td>0.32</td>
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<tr>
<td>Observations</td>
<td>144</td>
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More Information Can Encourage Debt Use

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Financial Capability

Integrating Financial Capability into Policy

Schools and Education Systems

Job Training

Housing

Retirement

Looking Ahead

Pre-post Debt Levels: Financial Education v. Controls

Dollar Debt from Credit Report

Control

Treatment

Pre

Post

0

5,000

10,000

15,000
But Not Worse Debt Use?

Pre-post FICO: Financial Education v. Controls

Credit Report Scores

Pre Post

Control Treatment

Looking Ahead
Findings

- Rising debt
  - Surprising? Very low income women in high cost housing market who likely have liquidity constraints and restrictions on savings will borrow

- What if financial education raises confidence and lowers information barriers to accessing credit?

- What if these barriers are welfare enhancing constraints? Opening the door to self control failures?
  - May suggest re-focus on product access, use and control
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Keeping Up in Modern Consumer Financial Market

- Accelerated use of technology
- Prepaid debit cards
- Electronic payments
- SmartPhone Wallet
- Instant liquidity
Student Loans: Need for Education/Counseling

- Loan amounts and types
- Major and time to degree
- Post-graduation - payment options - low take up and wide confusion

Dept of Education online ‘counseling’ could be enhanced...
Aging Demographics: Loss in Cognitive Functioning

Ability to make financial decisions?

- 30% of people in their 80s show cognitive impairment
- 20% of people in 80s show evidence of dementia

That’s 50%. 50-50 chance you will lose cognitive acumen.


http://dash.harvard.edu/handle/1/4554335
What About Behavioral Nudges?

Defaults
- Procrastination / Impatience

Inattention
- Reminders

Following the Crowd
- Social comparisons

- Pro: Can be very powerful
- Con: Indiscriminate

Still need to have the ability to make decisions
Emerging Strategies

- Peers, Couples, Generational
- Focus on Goals
- Translating into impacts on ‘future self’
- Leverage Peers (and peer networks)

**Examples:**

- Financial Coaching
- Emergency Savings
Be Realistic: Financial Interventions Have Limits

Limits of technical sciences...

Monitoring, Nutrition, Food Access, Counseling
Contact

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Looking Ahead

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