



Welcome to

Behavioral Economics and Financial Decision-Making

Corporation for
NATIONAL &
COMMUNITY
SERVICE 



Dial:

Passcode:

Today's Team



Andy King
Corporation For
National &
Community Service



Dr. Nilton Porto
University of Rhode
Island

Guest Speaker



Rory Price
Southwestern
Vermont Health Care
VISTA

Session Goals

By the end of the webinar, you will be able to:

- Look at financial decision making through the lens of behavioral economics and explain how financial scarcity can inhibit our ability to make informed decisions.
- Describe concepts that impact people in poverty related to financial literacy and can result in being underbanked or unbanked
- Identify concrete solutions and types of programming that address these behavioral obstacles and that aid people in poverty with financial decision-making.
- Brainstorm how the insights from these strategies can be applied to support the constituents with whom you work

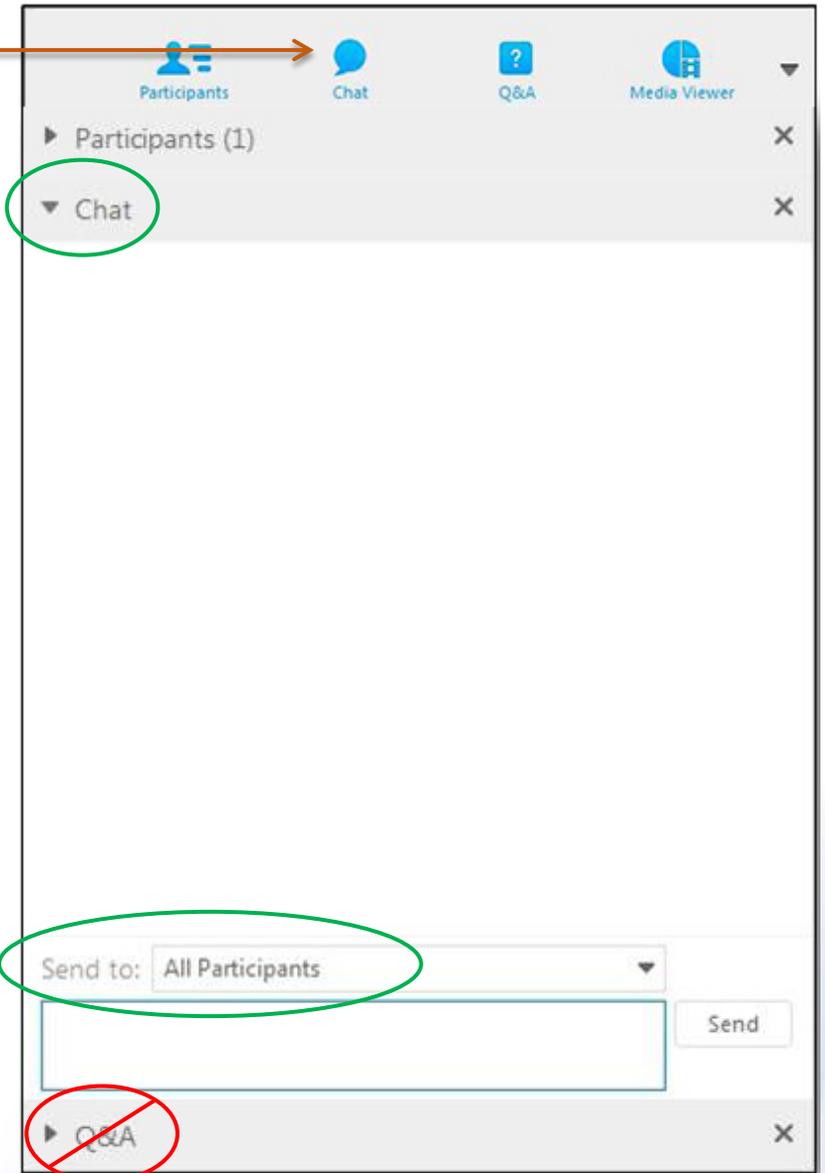
Today's Agenda

- What is Behavioral Economics (BE)?
- Decision making biases
- BE Strategies/Affecting behaviors
- Scarcity's impact on decision-making
- Behavioral Economics and Poverty
- Applying this to your VISTA service

Financial Decisions

- Thinking back to the decision you mentioned in the pre webinar chat, what strategies did you use to make that decision?

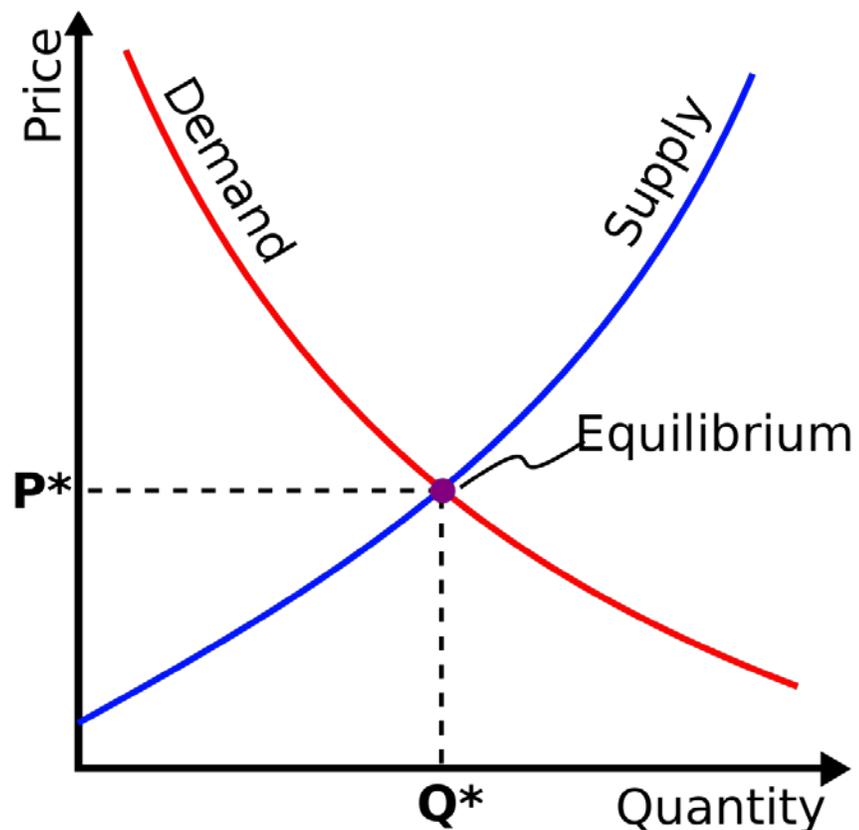
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Standard Economic Model (assumptions)

- People have known preferences → **Full Internal Knowledge**
- People act with full information → **Full External Knowledge**
- People act rationally to maximize utility → **Find Best Option**

Standard Model



- Assumptions help to develop clean mathematical models to explain behavior
- Assumptions **often** correspond to actual behavior

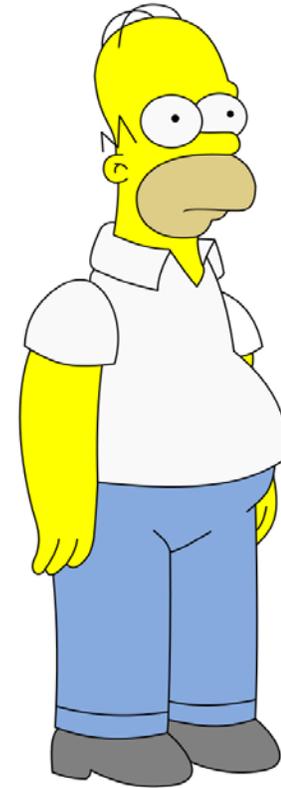
From assumptions... the rational Homo Economicus is born

- Carefully weighs costs and benefits
- Able to process all information
- Plan for a lifetime
- Able to exercise self-control
- Kind of selfish



Sometimes we are less than rational...

- We fail to consider costs and benefits
- We can't process all information available
- We are present-oriented
- We kind of care about others... we also make comparisons



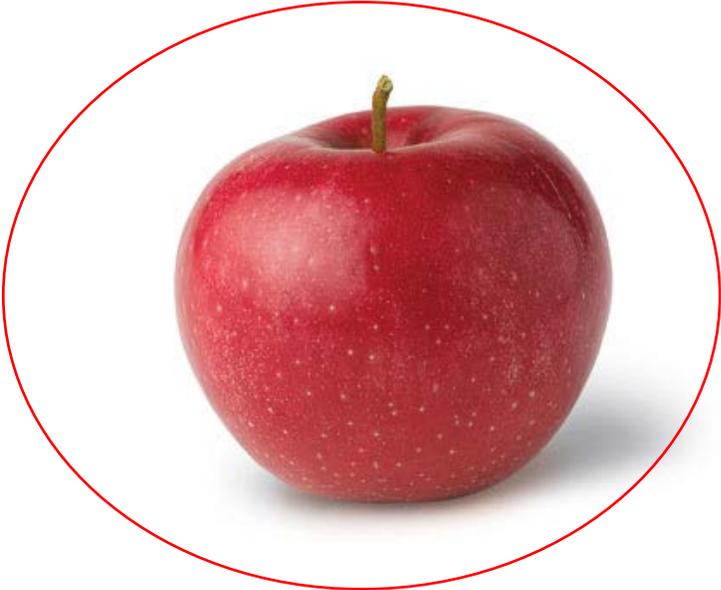
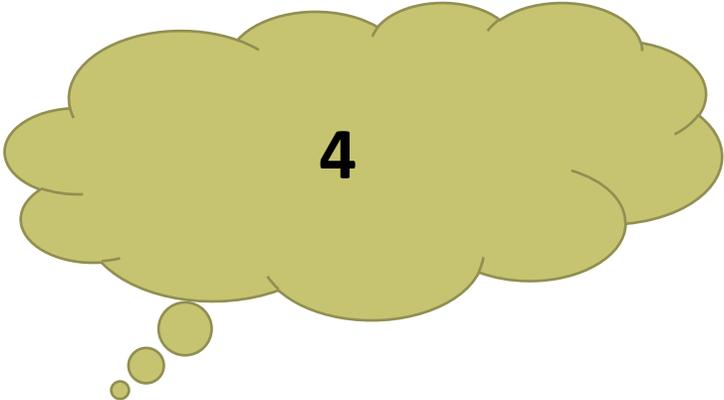
Behavioral Economics

- Uses concepts from psychology to investigate how social, cognitive, and emotional factors affect our choices
- In other words, try to explain deviations from the standard model

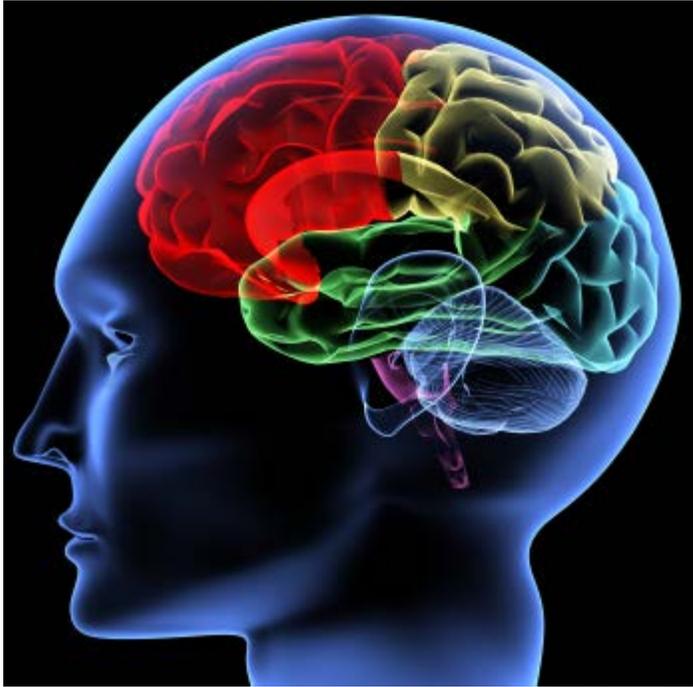
Why Does Behavioral Economics Matter?



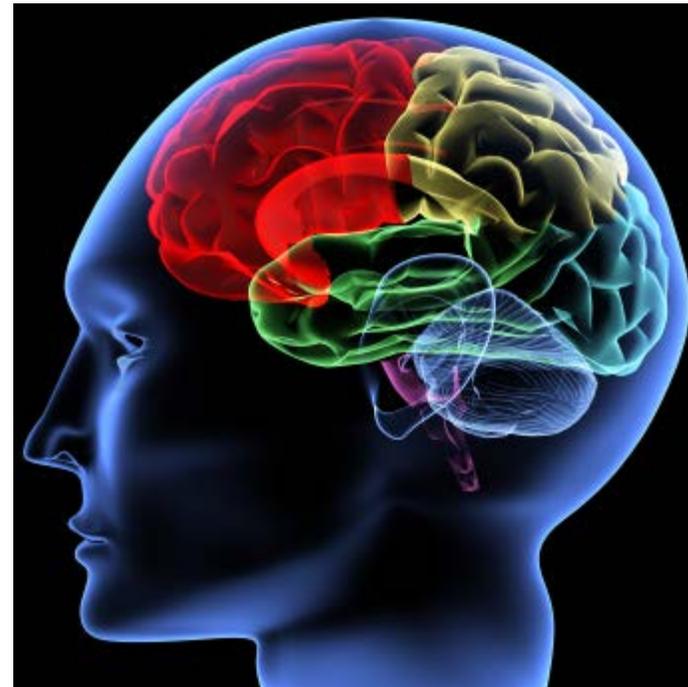
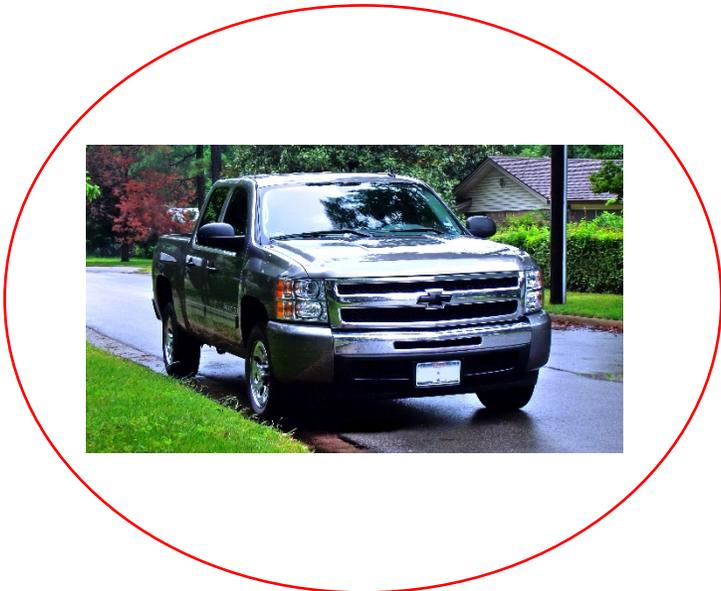
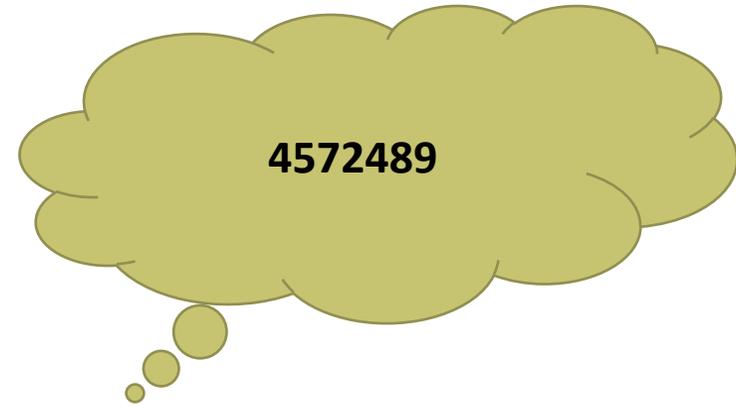
Choosing a snack?



Choosing a snack?



Retirement Savings



A Behavioral-Economics View of Poverty

Bertrand, Mullainathan, and Shafir 2004

- The poor suffer the same types of biases as anybody else
- However, poor individuals have a very narrow margin so mistakes are very costly
- Poor financial decisions might be due to scarcity – being in a constant state of cognitive load.

Decision Making Biases

- Framing
- Overconfidence
- Representativeness Heuristics
(mental shortcuts)
- Numeracy
- Present Bias



Framing

- How a choice is presented affects our decision making
- Losses loom twice as large as gains

Which steak is more appealing?



Levin & Gaeth, 1988

Framing of Price Reduction

- High-priced product: people prefer dollar discount
- Low-priced product: people prefer a percentage discount

Chen, Monroe, & Lou, 1998



Overconfidence

1. Overestimation of one's knowledge/ability (*I think I know a lot*)
 2. Overplacement of one's performance compared to others (*I am better than*)
 3. Calibration of subjective probabilities (*I am sure I got this right*)
- Due to overconfidence, people trade stocks too often, diminishing the returns on their investments (Barber & Odean, 2001)
 - People that are overconfident on their financial knowledge are the most likely to seek debt counseling advice, perhaps a sign of making bad choices (Porto & Xiao, forthcoming)



Representativeness heuristics



- Tendency to form judgement based on stereotypes
- We are too quick to detect patterns in data that are in fact random
- And we are overly optimistic about past winners and overly pessimistic about past losers

- Examples: lottery, casino

Numeracy



- People have a hard time figuring out probabilities, compounding interest, and the nominal versus real interest
- So we use fuzzy math when trying to make choices involving interest rates and future values

Present Bias

- Overvalue the present reward over long term rewards

Which would you prefer?

- a) \$100 today
- b) \$150 in a year

Which would you prefer?

- a) \$100 in one year
- b) \$150 in two years

We can't resist the \$100 today but usually okay to wait two years for \$150



- Refund anticipation loan

Who are the Unbanked?

Source: 2013 FDIC National Survey of Unbanked and Underbanked

	Unbanked
Overall – US households	7.6%
African-American	32%
Hispanic	24%
Native American/Alaska Native	29%
Single female parent household	20%
Single male parent household	15%
Household income less than \$30,000	20%
Less than a high school diploma	25%

Reasons Not to Have a Bank Account*

- Not enough money
- Don't like dealing with or don't trust banks
- Account fees are too high/unpredictable
(previous banked households more likely to pick this reason)
- ID/Credit/Bank history problems
- Privacy
- Banks do not offer needed products or services
(only 1.2% picked this as the main reason...
payday lending)



* Source: 2013 FDIC National Survey of Unbanked and Underbanked

Why do we care about the unbanked/ underbanked?

- Banked households have more assets
- More small business owners amongst banked households
- The unbanked pay high costs to manage their money
 - Cashing checks or paying bills
 - No access to formal savings – informal savings earning very little

Guest Speaker



Rory Price
Southwestern
Vermont Health Care
VISTA

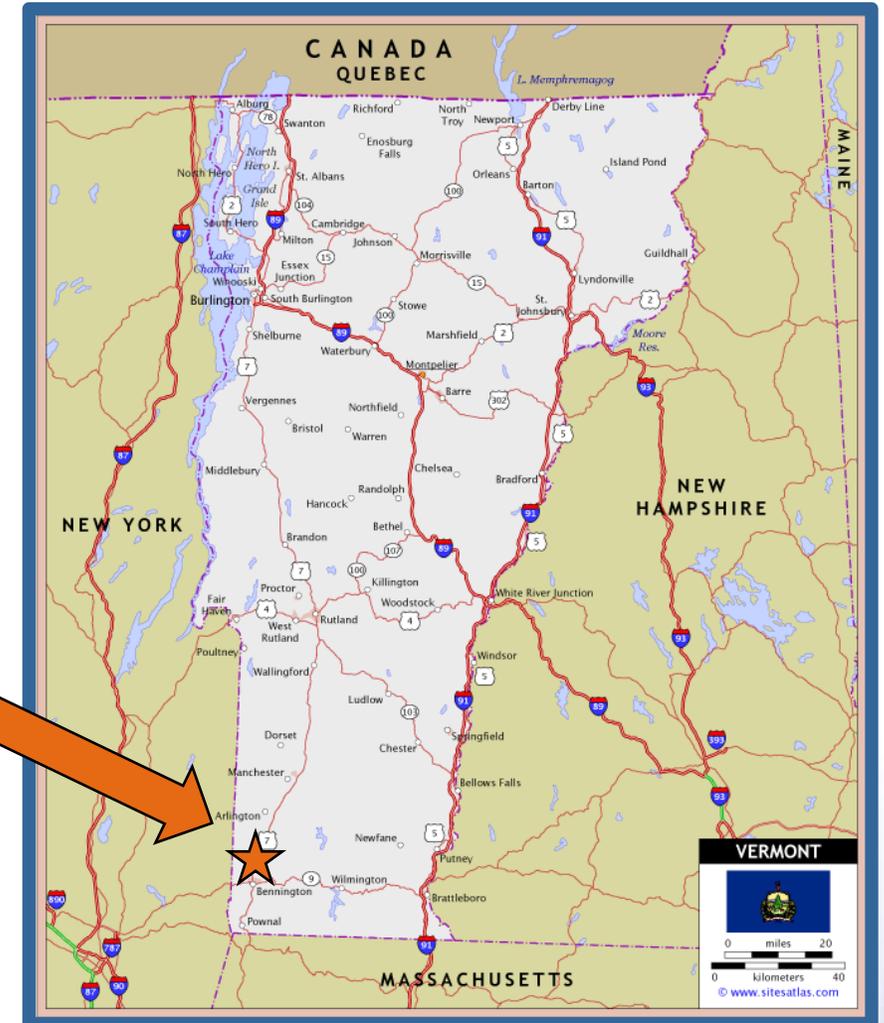
Southwestern Vermont

HEALTH CARE



The Town of Bennington:

- 9,074 people
- 21% of persons live at or below federal poverty level
- 60% of adults are overweight or obese
- 6.5% of adults are diabetic



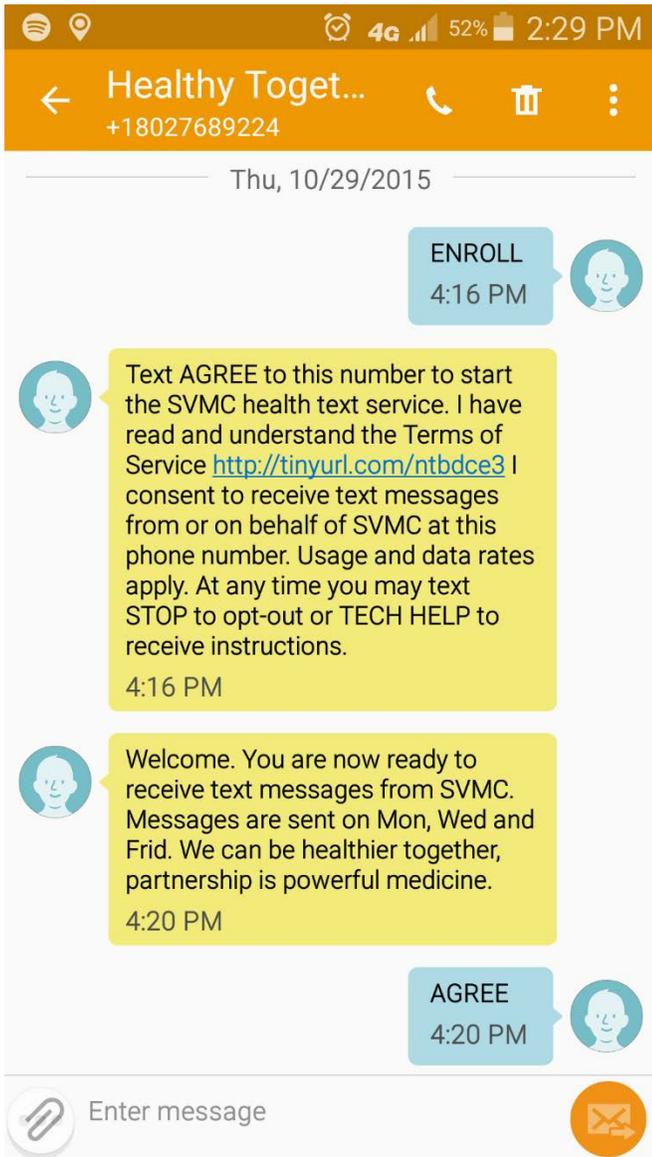
Health Tip Message Service



Healthy Together

A health tip message service brought to you
by Southwestern Vermont Health Care

- Messages originally created for individuals living with diabetes
- Easy way to reach people anytime, anywhere
 - Chronic conditions like diabetes affect people 24/7, not just when they are at the doctor



Logistics

- Enrollment is easy, open to the public
 - Simple opt-out process
- Numbers remain confidential
- Not an interactive service

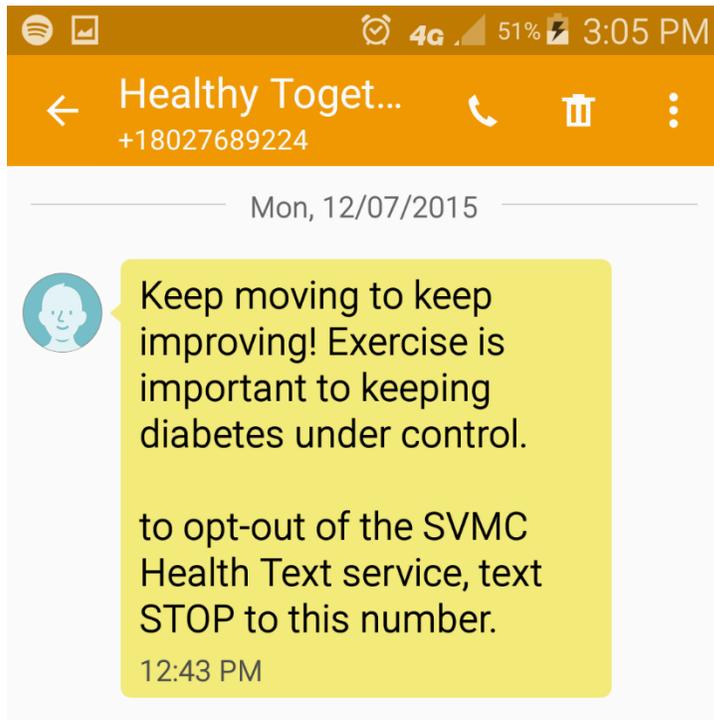
Nudges



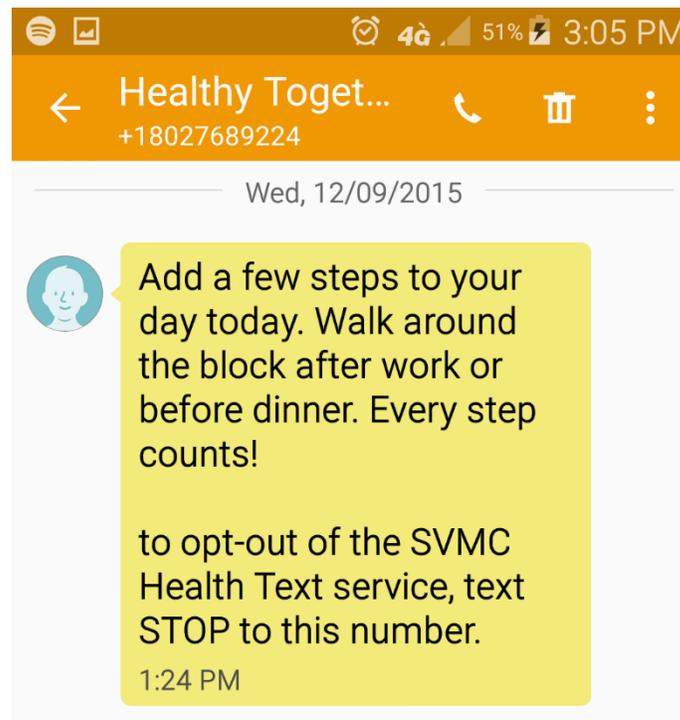
- 3 texts per week
 - **Monday**- Introduction of theme
 - **Wednesday**- Gentle directive/suggestion
 - **Friday**- Advice to sustain behavior

One Step at a time: The Effects of an Early Literacy Text Messaging Program for Parents of Preschoolers
[http://cepa.stanford.edu/sites/default/files/York%20%26%20Loeb%20\(October%202014\).pdf](http://cepa.stanford.edu/sites/default/files/York%20%26%20Loeb%20(October%202014).pdf)

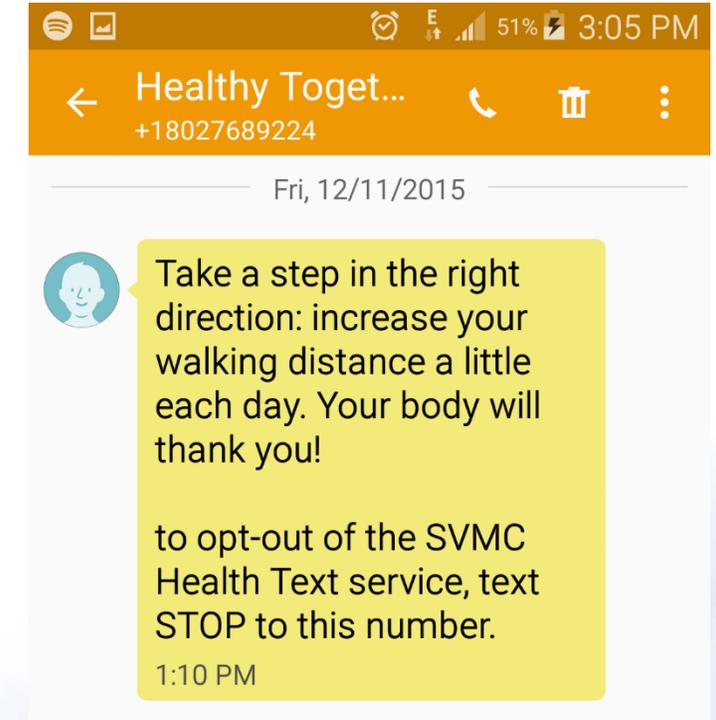
Monday



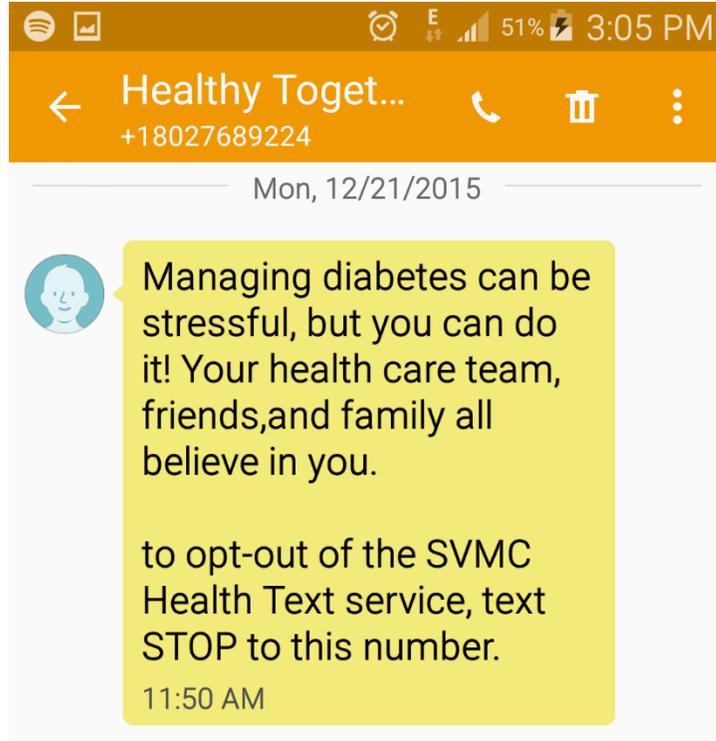
Wednesday



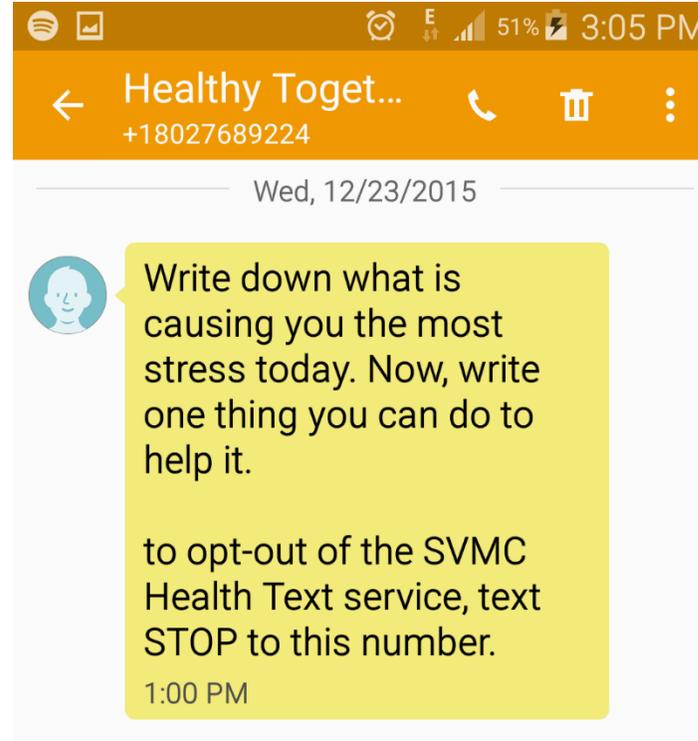
Friday



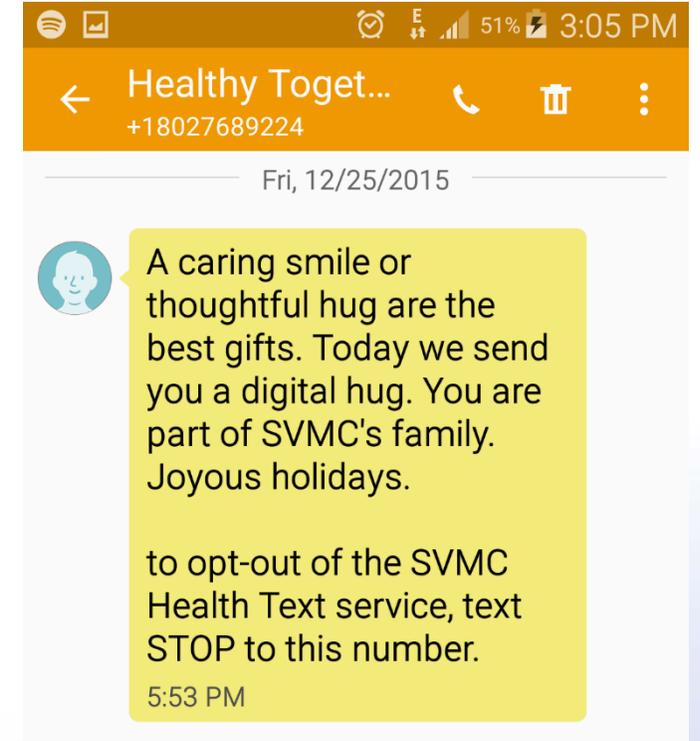
Monday



Wednesday



Friday

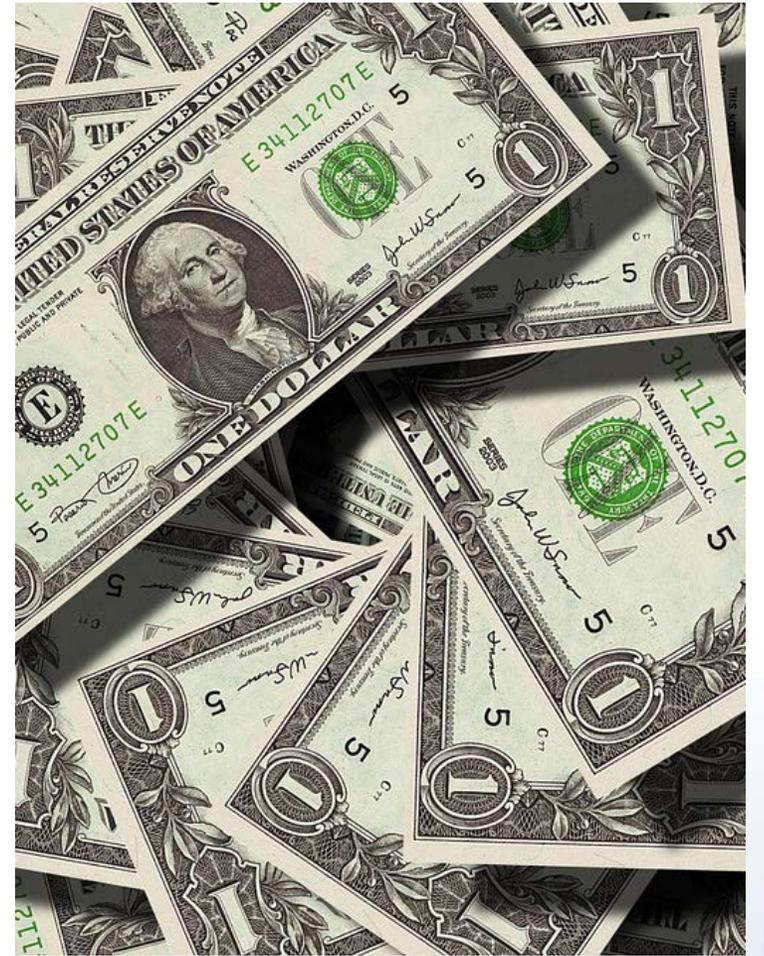


The Three Cs

1. **C**ost-effective
2. **C**ustomizable
3. **C**ompassionate

Cost-Effective

- Most people already have phones and unlimited texting
- Inexpensive for SVHC
- No cost associated with adhering to tips

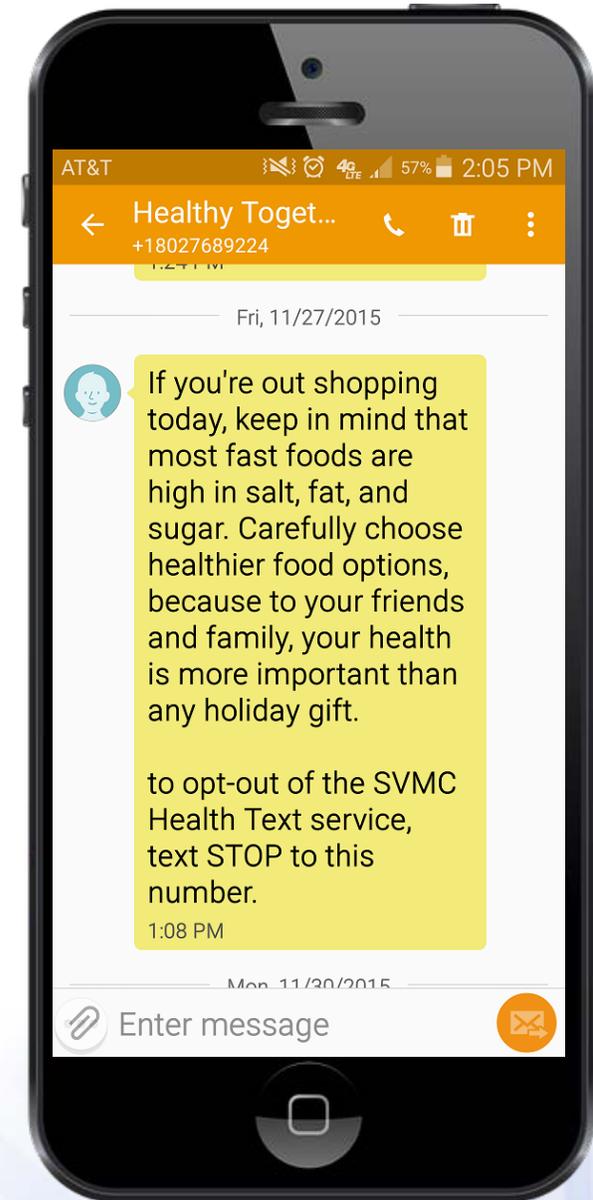


Customizable

- Messages are manually entered and can easily be changed
- Could expand to other chronic conditions
 - COPD, hypertension, depression
 - Financial literacy, increased vocabulary, etc.

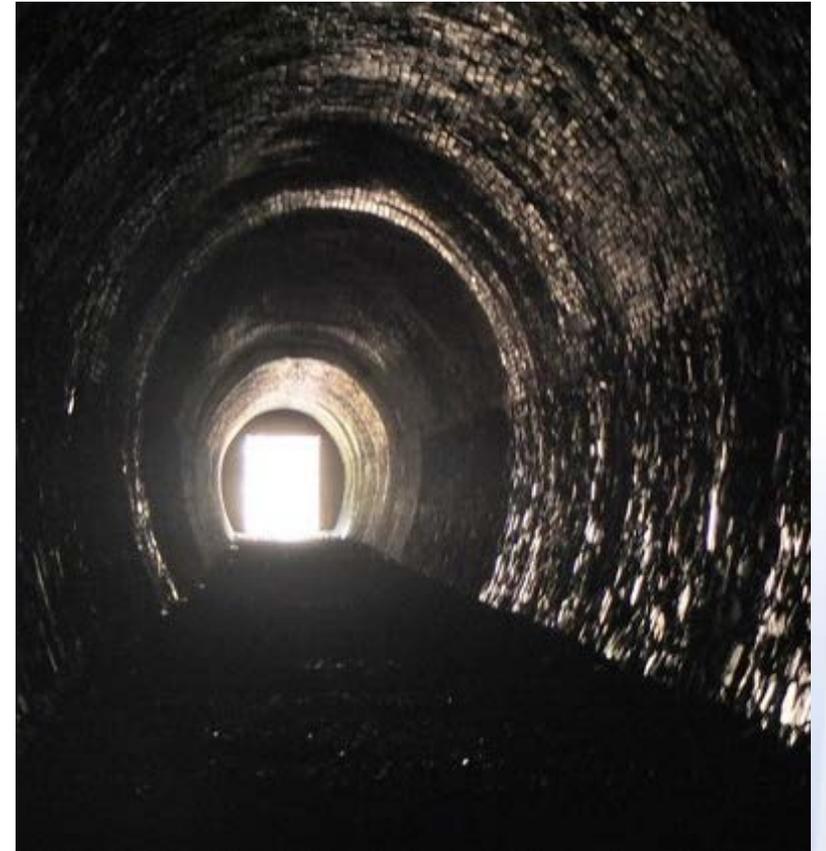
Compassion

- Most important aspect
- Positive pushes
 - Counterbalance negative feedback in daily life
 - Friendly, informal
 - Boost feelings of self-worth



Solutions:

- Commitment Device
- Choice architecture
 - Nudges
 - Defaults
 - Simplify

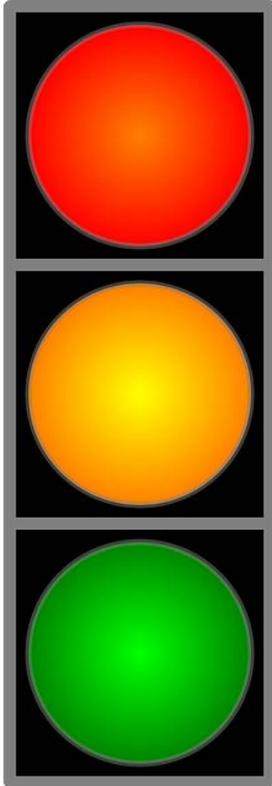


Commitment Devices



- Uses to avoid temptations and stay on the best course – to accomplish future goals
- Good technique against procrastination and self-control issues
- Only self-aware, sophisticated people will use it

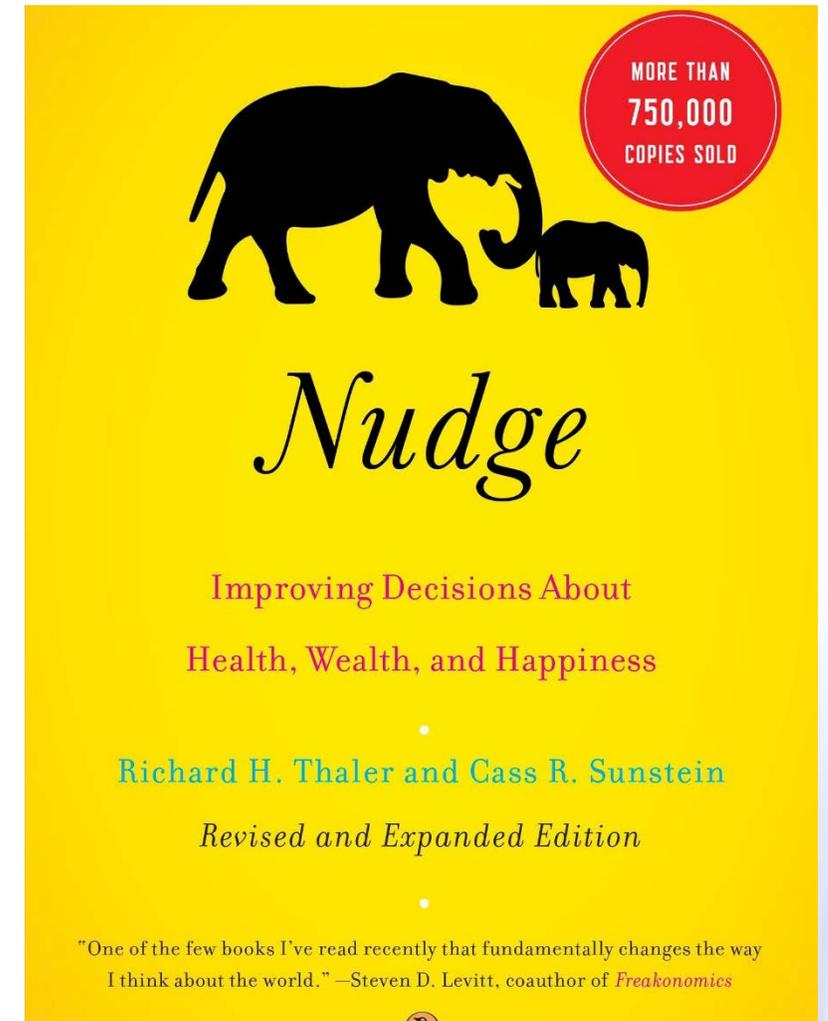
Choice Architecture



- Change how options are presented to help people make better choices
- Eating healthy and traffic light labels

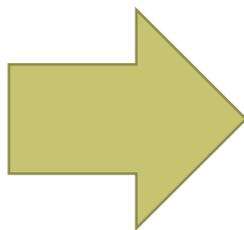
Nudges

- Use of positive reinforcement and indirect suggestion
- Not mandatory or hard to implement
- Example: text message



Default : 401(k) auto enrollment

- **Before:** new employees need to opt in into the program
- **After:** new employee need to opt out of the program (auto enrolled)

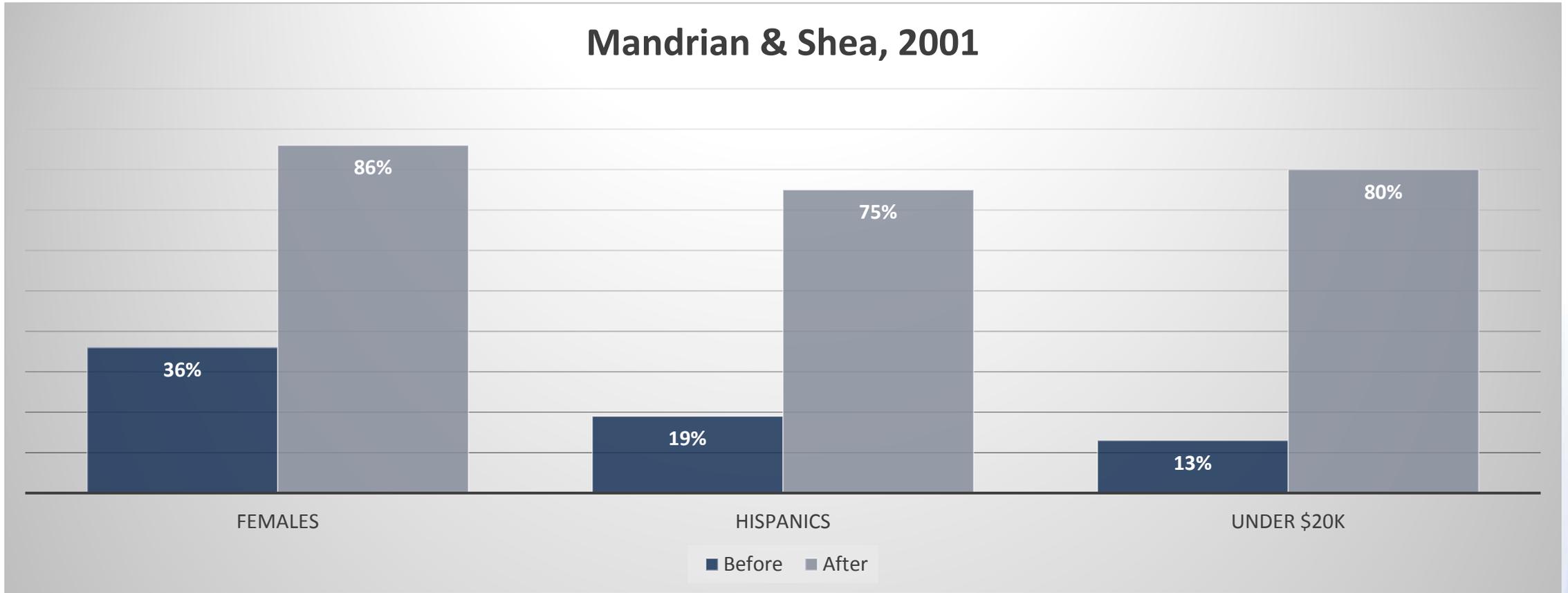


Savings increased! Why?

Psychological Factors

- Inertia
- Costly to contribute to 401(k): time and money
- Self-control issues prevented participation

Defaults: Participation Increased



Simplify

- Eliminate barrier and reduce hassles
- Bring the bank to the unbanked



BE approaches for Personal Finance

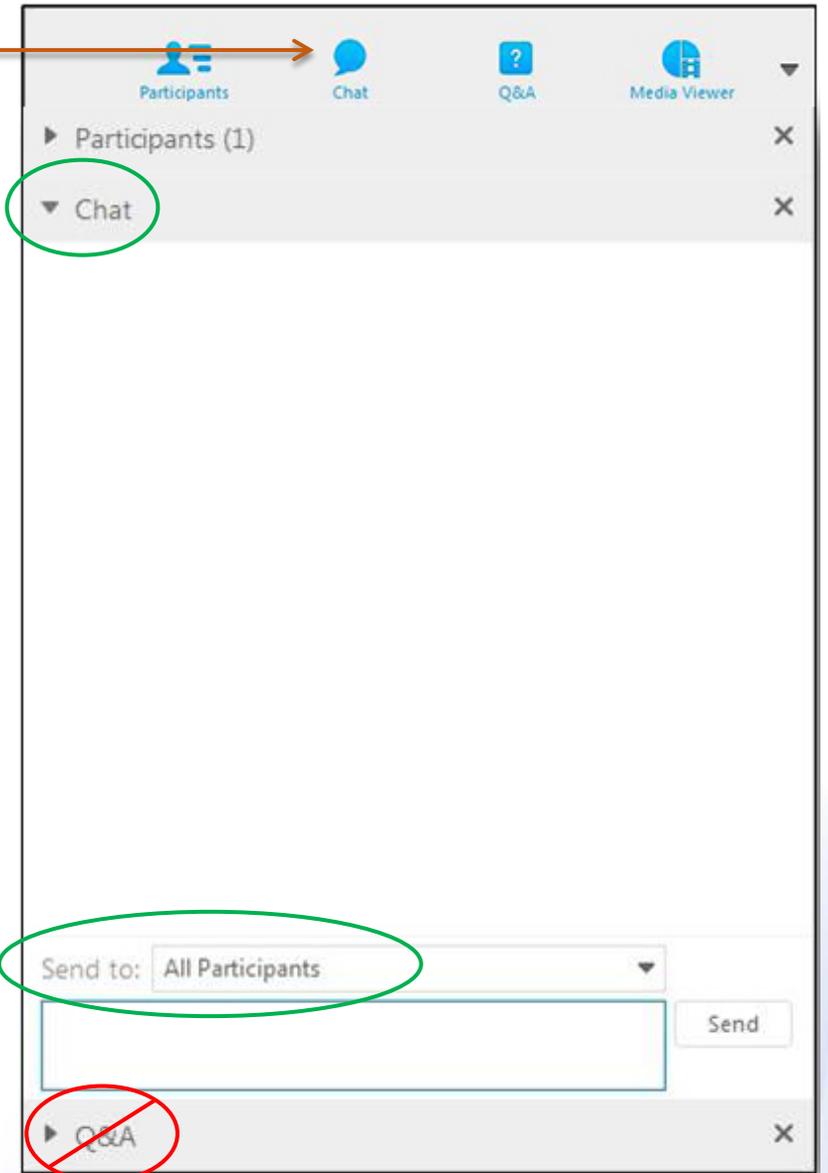
- Earn
- Save and Invest
- Protect
- Spend
- Borrow



VISTA in Action

- Share an idea of how you could use Behavioral Economics solutions to help support your programs and constituents.

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Resources

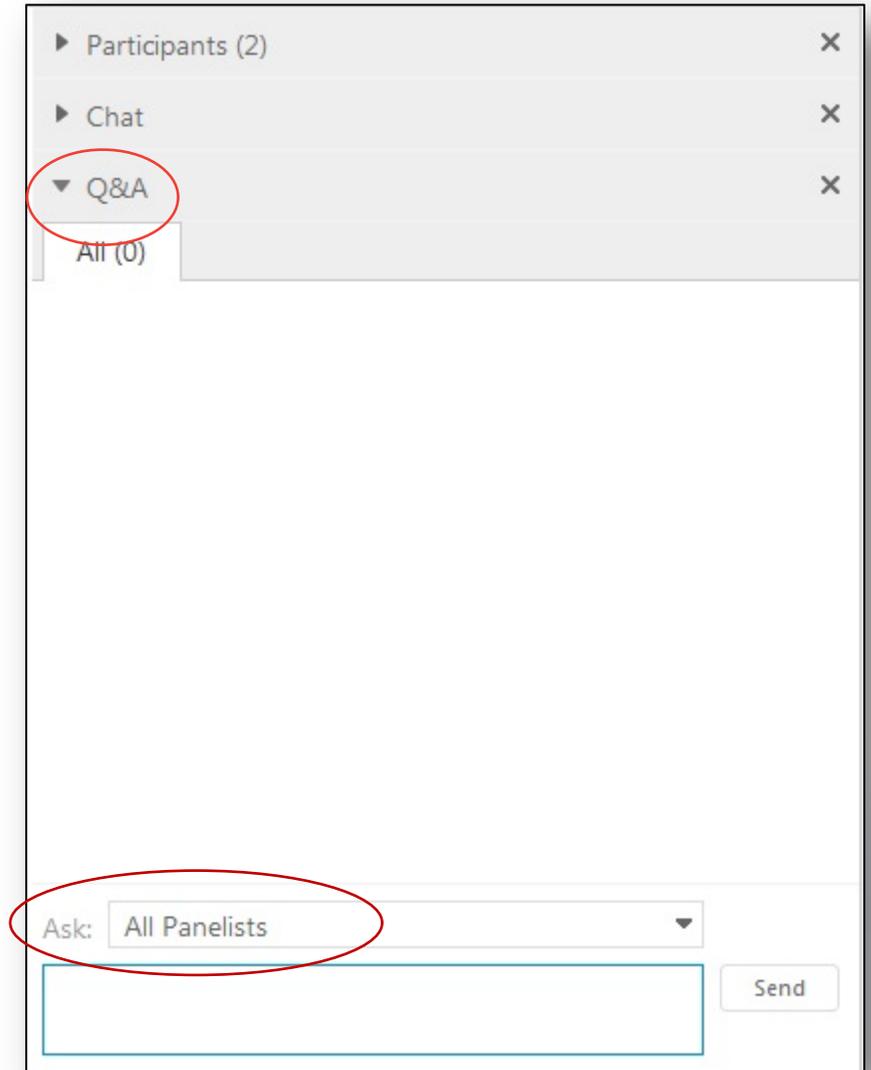
- Benefits.gov
- Second chance bank accounts
- VITA : Volunteer Income Tax Assistance
- Doorway to Dream (D2D) <http://www.d2dfund.org/>
- Bankrate.com

Evaluation

- Please take a few moments to share your feedback through the quick poll on the right side of the screen.
- How can we improve these sessions? What topics should we include in future webinars?
- Thank you very much for your time and participation!

Questions ?

- To ask a question verbally, call in using the number on this slide and press *1
- To ask a question electronically, use the Q&A feature located in the bottom right corner of the screen. Please ask “All Panelists”



Thank You for Your Participation!

If you have further questions or for more information, contact us: VISTAwebinars@cns.gov

Our next webinar:

Poverty and The U.S. Safety Net

February 24, 2016

2:00pm Eastern

Visit the Webinars for VISTAs page on the VISTA Campus for a complete schedule of VISTA webinars