Welcome to
Behavioral Economics and Financial Decision-Making
Today’s Team

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Guest Speaker

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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?
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 Matters?
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

- Refund anticipation loan

We can’t resist the $100 today but usually okay to wait two years for $150
## Who are the Unbanked?

**Source:** 2013 FDIC National Survey of Unbanked and Underbanked

<table>
<thead>
<tr>
<th>Category</th>
<th>Unbanked</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Overall – US households</strong></td>
<td>7.6%</td>
</tr>
<tr>
<td>African-American</td>
<td>32%</td>
</tr>
<tr>
<td>Hispanic</td>
<td>24%</td>
</tr>
<tr>
<td>Native American/Alaska Native</td>
<td>29%</td>
</tr>
<tr>
<td>Single female parent household</td>
<td>20%</td>
</tr>
<tr>
<td>Single male parent household</td>
<td>15%</td>
</tr>
<tr>
<td>Household income less than $30,000</td>
<td>20%</td>
</tr>
<tr>
<td>Less than a high school diploma</td>
<td>25%</td>
</tr>
</tbody>
</table>
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
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

- 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*

Monday

Keep moving to keep improving! Exercise is important to keeping diabetes under control.

to opt-out of the SVMC Health Text service, text STOP to this number.

12:43 PM

Wednesday

Add a few steps to your day today. Walk around the block after work or before dinner. Every step counts!

to opt-out of the SVMC Health Text service, text STOP to this number.

1:24 PM

Friday

Take a step in the right direction: increase your walking distance a little each day. Your body will thank you!

to opt-out of the SVMC Health Text service, text STOP to this number.

1:10 PM
Monday

Managing diabetes can be stressful, but you can do it! Your health care team, friends, and family all believe in you.

to opt-out of the SVMC Health Text service, text STOP to this number.

11:50 AM

Wednesday

Write down what is causing you the most stress today. Now, write one thing you can do to help it.

to opt-out of the SVMC Health Text service, text STOP to this number.

1:00 PM

Friday

A caring smile or thoughtful hug are the best gifts. Today we send you a digital hug. You are part of SVMC’s family. Joyous holidays.

to opt-out of the SVMC Health Text service, text STOP to this number.

5:53 PM
The Three Cs

1. Cost-effective
2. Customizable
3. Compassionate
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

Mandrian & Shea, 2001

Before | After
---|---
FEMALES | 36% | 86%
HISPANICS | 19% | 75%
UNDER $20K | 13% | 80%
Simplify

- Eliminate barrier and reduce hassles
- Bring the bank to the unbanked
BE approaches for Personal Finance

- Earn
- Save and Invest
- Protect
- Spend
- Borrow
Share an idea of how you could use Behavioral Economics solutions to help support your programs and constituents.
Resources

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