

# INNOVATIONS IN PAYING DOWN DEBT: LESSONS FROM BORROW LESS TOMORROW

# Housekeeping

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- Q&A session at the end of the presentations
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- You can submit questions at anytime during the webinar

# Speakers

- **Genevieve Melford**, Director of Research, CFED and Moderator
- **Jonathan Zinman**, Associate Professor of Economics, Dartmouth College and Academic Director, U.S. Household Finance Initiative, IPA
- **Christopher Trepel**, Senior Vice President, Corporate Affairs and Chief Scientific Officer, Encore Capital Group
- **Brian Enneking**, Vice President, Consumer Marketing, Encore Capital Group

**BORROW LESS  
TOMORROW**  
BEHAVIORAL APPROACHES TO  
DEBT REDUCTION

(FROM IPA'S  
U.S. HOUSEHOLD FINANCE  
INITIATIVE)

Dean Karlan, Yale University, IPA

Jonathan Zinman, Dartmouth College, IPA

# Problem: Household Debt Management

- Low household savings rate (sometimes)
- High debt loads/reliance in emergencies
- Highest, safest return for many households: pay down expensive debt
- But... getting/staying out of debt is hard, psychologically, cognitively, etc.
  - Consumers may need help
  - Yet many face limited, unattractive options in market for debt management services

# Potential Solution:

## Borrow Less Tomorrow (BoLT)

- Design Strategy:
  - Use “behavioral” insights to develop a new product that helps people reduce/manage debt
  - Save More Tomorrow™ as a guide
    - SMaRT: 401k enrollments
    - Important institutional/market differences between retirement saving and debt reduction
- “Kitchen sink”/“behavioral engineering” approach
  - Design product to counter multiple potential biases:
    - In price perceptions, attention, preferences
  - Product/choice architecture approach
  - (Ideally/eventually complemented with robust advice market)

# BoLT Features



- **Motivate:** Help consumers identify whether they should borrow less
- **Plan:** Help consumers make a concrete plan to borrow less
- **Commit:** Offer client option(s) to incentivize sticking to the plan
  - Current options include peer supporters/referees
  - “Harder” commitment options to be added soon
- **Communicate:** Send feedback/reminders to stay on track

# Pilot Testing So Far



- Small-sample concept test: Jan 2010- April 2011
  - Convenience sample: tax preparation clients, Community Action Project (CAP), in Tulsa
- Pilot addresses two threshold questions
  - ▣ Will borrowers use BoLT if offered simple, free version?
  - ▣ Potential for cost-effective operation/administration?
- Also trying to build large enough sample to test BoLT's effectiveness
  - ▣ Field experiment built into pilot delivery

# Operations/Field Experiment Flow for Pilot Testing

- Person enters tax prep site
- Offered survey, consent form for soft pulls of credit report
- Randomly assigned to Treatment (some version of BoLT) or Control (no BoLT, or BoLT later)
- BoLT group:
  - ▣ Counselor works with client to identify whether suitable debt
    - “High touch” is not necessarily essential component of BoLT
  - ▣ Uses repayment calculator to come up with a plan
  - ▣ Offers opportunity to enlist peer support
    - Peer supporters contacted
  - ▣ Later:
    - Regular reminders to make payments
    - Client notification and peer notification if fall off-track

# Pilot Sample Characteristics: Year 1

- N =505 with auto loan or credit card debt
- From baseline credit report:
  - ▣ Credit score: mean 603, standard deviation (95)
  - ▣ Credit card balances: mean \$2,408, SD (\$5,103)
  - ▣ Auto loan balance: mean \$5649, SD (7626)
- From baseline survey:
  - ▣ 70% at least some college
  - ▣ >20% report using “fringe” loan product in last 2 years
  - ▣ High prevalence of various financial distress proxies
  - ▣ But... 57% say financial situation  $\geq$  “OK”

# Pilot Threshold Question 1: Demand?



- Are borrowers interested in using BoLT? Yes!
- 38% take-up rate among CAP's tax prep clients with a credit card or auto loan at baseline
  - This is without doing any pre-screening or target marketing for high-interest debt
- Among BoLT takers, 48% enlist peer support

# Question 1b, Demand Analysis: Description of BoLT plans

- 58% of takers use for a credit card
  - Estimated mean interest rate: 18%
  - Estimated principal amount: \$4,000
  - Mean plan to accelerate repayment: \$23/month
  - Median payoff time with vs. without BoLT: 17 vs. 35 months
- 42% of takers use for auto loan
  - Estimated mean interest rate: 12%
  - Estimated principal amount: \$10,000
  - Mean plan to accelerate repayment: \$41/month
  - Median payoff time with vs. without BoLT: 32 vs. 45 months

# Pilot Threshold Question 2: Delivery?

- Can BoLT be marketed cost-effectively?
  - ▣ Probably yes. More speculation on this later.
- Feasible to monitor whether someone is on track with paydown schedule?
  - Yes, using credit report soft pulls (with client consent obtained up front)
    - Finding cost efficiencies key to scale-up
- Peer supporters actually reachable when a BoLT client falls off track?
  - Yes, though there is some room for improvement; e.g., give a “heads-up” to peers up front
- Text message reminders deliverable? Yes.

# Beyond Threshold Questions: Is BoLT Effective?

Why is random assignment important for answering this?

- After 6 months, 29% of BoLT users were on schedule
- 59% of BoLT users stayed on schedule for  $\geq 1$  month
- Are these proportions low or high? Unknown!
  - Depends on the counterfactual... what would balances look like in absence of BoLT?
  - If difficult to pay down expensive debt then counterfactual = continued high balances
    - Analogy to smoking: most attempts to quit fail
  - So... we implement BoLT as part of field test that builds in counterfactual (by creating a valid Control Group)

# Measuring Effectiveness: Some Outcomes of Interest

- Outcome measurement from follow-up soft pulls of credit report. So can measure:
  - ▣ Credit score
  - ▣ Balances
    - \*1/0 plausible-sized reduction in balances\*
- In other settings might be able to do some short follow-up surveys by web or phone
  - ▣ Measure self-assessed financial condition, etc.

# BoLT Effectiveness on Year 1 sample: 12-month treatment effects

- OLS-estimated effects of BoLT offer on:
  - ▣ 5%, 10% reduction in card debt:  $-0.05(0.04)$ ,  $-0.04(0.04)$
  - ▣ 5%, 10% reduction in car debt:  $0.03(0.05)$ ,  $0.03(0.04)$
- Propensity score matching (person-level) estimates:
  - ▣ 5%, 10% reduction in card debt:  $0.00(0.05)$ ,  $0.00(0.05)$
  - ▣ 5%, 10% reduction in car debt:  $0.14(0.06)$ ,  $0.15(0.06)$

# BoLT Effectiveness on Year 1 sample: Preliminary thoughts on interpretation



Why might this version of BoLT work for car, not card?

- Most people have many cards, one car loan
  - ▣ If this what's going on, suggests important going forward to offer BoLT across multiple cards/loans
- Managing card(s) requires more sustained attention
  - ▣ Would more frequent feedback?
  - ▣ More binding commitments?

# Going Forward: Design Permutations

Much more development and testing worth doing!

- Consumer **motivation** through direct marketing
- Expand and improve set of potential **plans**. Examples:
  - Plans over aggregated balances (e.g., across all cards)
  - Plans to restrict new borrowing (e.g., no new trades)
  - Extend to products not covered in traditional bureaus?
  - Improve repayment planning using algorithm-based advice to **set default options**
- Expand set of potential **commitments**. Examples:
  - Performance bonds
  - “Cut me offs”
  - Link peer support to social networking
- Refine **communication** strategy
  - Content, timing, frequency, duration, channel, client customization

# Going Forward: Business Model

- Identify revenue models
  - Subscription (as part of a larger bundle?)
  - Cross-sell/bundling
- Reach scale with partners who have comparative advantage in delivery
  - Bureaus/credit report monitoring services
  - Credit counseling agencies\*
    - 3 projects ongoing
  - Online financial management aggregators/advisors\*
    - One failed pilot with HelloWallet (back to drawing board)
  - Payments platforms
    - Mobile wallets
    - Bill payers
  - Debt buyers/collectors: back-end for clients who repay\*
    - In development with Encore...



# FIELD TESTING BOLT WITHIN CONSUMER FINANCE

A partnership between IPA and Encore's  
Consumer Credit Research Institute (CCRI)

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January 17, 2012

PROPRIETARY

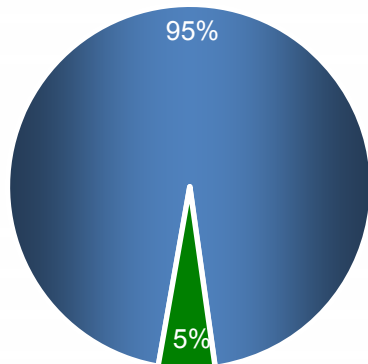


# ENCORE CAPITAL GROUP IS THE COUNTRY'S LARGEST DEBT BUYING AND RECOVERY FIRM, BY REVENUE

## Revenue Composition

As of March 31, 2011

### Debt Purchasing & Collections



- Purchase and collection of charged-off unsecured consumer receivables (primarily credit card)
- Robust business model emphasizing consumer intelligence and operational specialization
- Acquired ~34 million consumer accounts since inception

### Bankruptcy Servicing

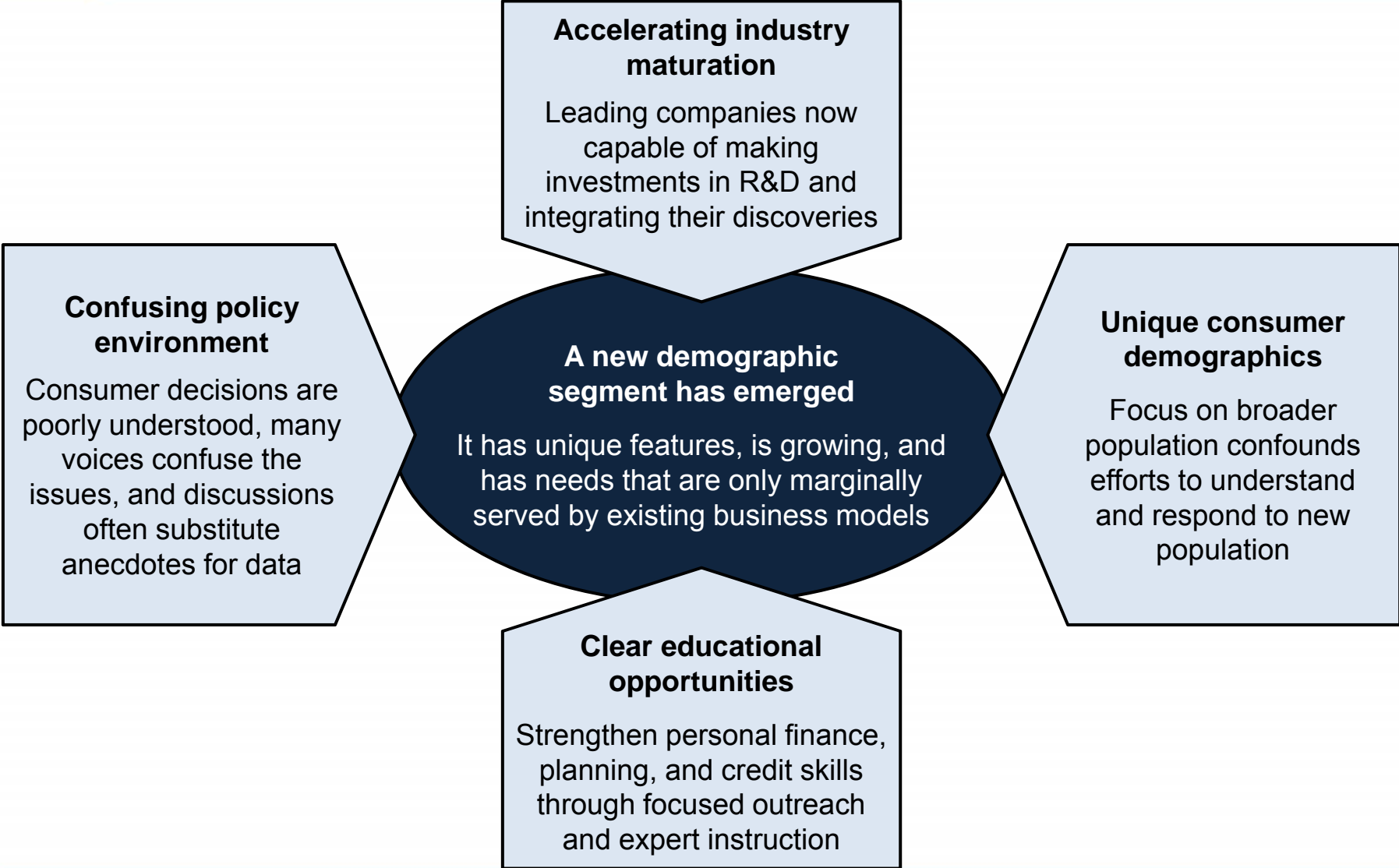
- Process secured consumer bankruptcy accounts for leading auto lenders and other financial institutions
- Proprietary software dedicated to bankruptcy servicing
- Operational platform that integrates lenders, trustees, and consumers

## Global Capabilities


- Debt Purchasing & Collections
- Bankruptcy Servicing



# WE HAVE BUILT A CENTER OF EXCELLENCE DEDICATED TO UNDERSTANDING FINANCIALLY DISTRESSED CONSUMERS



# THE INSTITUTE IS FOCUSED ON THREE INTERRELATED AREAS OF INTEREST TO POLICY MAKERS AND THE PUBLIC

 <p>CONSUMER CREDIT RESEARCH INSTITUTE</p> <p>&lt; <a href="http://www.encoreccri.org">www.encoreccri.org</a> &gt;</p>	<p><b>Promote financial literacy</b></p> <hr/> <p>Create and manage a tailored suite of programs that provide <b>significant, measurable benefit to consumers</b></p>
<p><b>Improve business model performance</b></p> <hr/> <p><b>Integrate experimental psychology and behavioral finance</b> into marketing and operational practices</p>	<p><b>Enhance consumer intelligence</b></p> <hr/> <p><b>Conduct research to understand financially distressed consumers'</b> choice, consumptive, and financial behaviors</p>

# BORROW LESS TOMORROW OFFERS A UNIQUE OPPORTUNITY TO EXPLORE REPAYMENT OPTIONS, ATTITUDES, AND BEHAVIORS

Understand  
consumer  
behavior

- What do consumers consider when taking on, and repaying, debt?
- How do consumers psychologically connect to financial obligations?

Encourage  
and support  
repayment

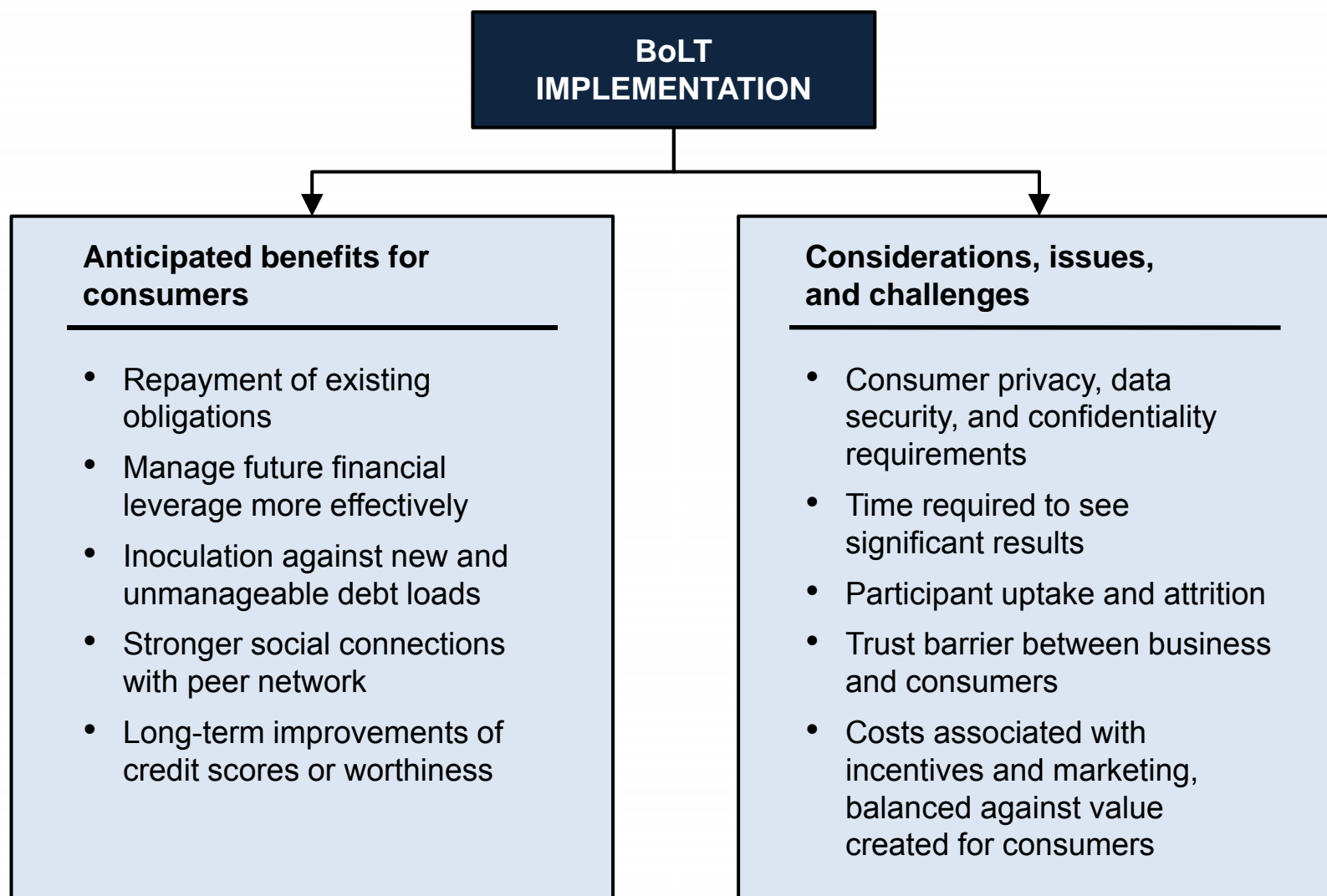
- Which tools and processes are most likely to result in repayment?
  - Likelihood
  - Velocity
- Which factors confound consumers' repayment desires and intentions?

Promote  
financial  
literacy

- Can we provide information and training that breaks the debt cycle?
  - Budgeting
  - Numeracy
  - Introspection

The BoLT approach allows us to address a series of questions that are central to the relationship between household balance sheet management, credit availability and use, and repayment behavior

# IMPLEMENTATION SHOULD LEAD TO SIGNIFICANT BENEFIT, THOUGH IMPORTANT QUESTIONS MUST BE ADDRESSED



# Q&A

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- ❑ Further questions? Email [Istebbins@cfed.org](mailto:Istebbins@cfed.org)