Federal Reserve Forum on Consumer Research & Testing: Tools for Evidence-based Policymaking in Financial Services, November 9, 2010
Panel One: Exploring the root disciplines for studying consumer behavior

Margaret Sherraden:
Good morning. It's great to be here. Thanks again to Jeanne and Ellen and Anna, others who put this together. Looking forward to -- already learned a lot and looking forward to hearing more from others of you in the room today. So I'm going to be taking the sort of applied sociological perspective, a bit different than the former three panelists, but I think fits well. And I think the order we're doing it is right. We did have a conversation prior for planning this and thought this might be the best way to do it. And I've been, you know, thinking about Jeanne's request that we do that 35,000-foot-high view of sociology, which is a bit of a challenge because there's a lot to cover and I don't have anyone else on the panel to help me do this part of it. So I'm going to run through some of the stuff that -- that we actually do use a lot of the behavioral economic ideas in our work, and I'll run through that. The kids you see on the slide are kids who participated in a college savings program. Most of the research we do is on saving in low income and financially vulnerable households. So I'm going to talk about sociological understanding of consumer issues very briefly. And if there are any sociologists in the room, please forgive me, talk about a definition that we use of financial capability, which is a little different; some of the constraints people face; the role of institutions, how we might leverage some of that to provide greater opportunity to people; and then some of the research implications.

So the sociological understanding, we begin with the idea that it's not just about behavior of individuals. It's also actions, which may not be even intended. And that understanding the social and economic cultural context shapes and influences people's financial capability. And that behavioral economics brings to this that very important, as John mentioned early, choice architecture that channels consumer behavior. But we also need to think about the role of institutions. So, you know, the great works of sociology that talk about household decision-making, about affluence and consumer culture, how people organize themselves in ways that imbue money with certain kinds of meaning. I'm not going to talk directly about -- about those traditions, so, you know, people like Thorstein Veblen and others who -- who gave us the sort of basics in sociology, I just don't have time to cover today. But I guess the point that I would like to make is that the decisions that people are making or the actions that people take are socially embedded. And they're socially embedded in a variety of social, economic, and cultural institutions. So the key questions I'm going to be looking at are, one, how these social institutions ease or constrain individual behavior and action and how do features of financial services influence consumer participation.

So to get this started, we've done quite a lot of research on matched savings accounts, individual development accounts with low income people. We don't -- we don't really actually talk about them as consumers necessarily. They're consumers and a lot of other things as well. So in this study that we wrote about in our book, *Striving to Save*, where we did a fairly rigorous design of -- it was part of an experimental design, in-depth interviews with both controls and treatments who were in a matched savings account program and Ann was somebody who stood out -- and I'm going to talk about two people that sort of fall at different ends of the continuum. Ann stays connected to financial services. And what was interesting about Ann was she was sort of your classic screw-up. You know, this was a kid who didn't grow up wealthy at all, lower middle class. But his or her family was secure in the sense that her father had a job; he had access to financial services; he had a retirement account; a number of things through that employment situation that made the family life a lot more financially stable. As a child, her parents told her to save. And I have to say that, across the board, successful, unsuccessful savers, everybody said -- almost everybody said, that they got the message as very young children that they should save. There were a lot of other things that happened, too, which made it difficult. But they did. Early on, Ann made poor financial decisions. In her words, she said, I blew a lot of money, I didn't save, I lived paycheck to paycheck. She almost flunked out of school and didn't make it back. But her family bailed her out. They were there through that period. You know, many of us -- probably some of us in this room have had to bail out our kids. And she actually learned how to effectively -- if she fell flat, got back up several times and managed to effectively manage her finances and saved effectively in the program.

Theresa cannot get connected to financial services. She grew up working poor as a child. She was taught to pay yourself first. That's what her parents told her. But she had a number of circumstances that made it a lot more difficult than Ann. She didn't have a family who could help bail her out, for one. She got married. Her ex-husband made all the financial decisions. She left the marriage without any assets, not knowing really what kinds of things to do. She can't open a checking account because of past financial mismanagement. She had credit card debt. But she said to us, I know where every dime of my money goes, my money is valuable to me. But no insurance, and illness has led to serious financial trouble. And one of her comments was, “Everybody has a dream -- she talked about this a lot-- Everybody has a dream, but the system makes it very, very difficult for lower income people to achieve what they've set out to do”.

So a picture of opportunity constrained. You know, we all know these stories. We've certainly seen a lot of this in the last couple years. I don't know; many of you are college professors. I know that my students are really hurting right now being kicked out of homes, having to drop out of school, any number of things like that. We know that the data also show us that, in terms of social stratification and sociology, we talk about different strata in the social world; that racial and ethnic minorities, single women are far more likely to be unbanked or underbanked in terms of the FDIC study. The high costs of alternative financial services, rates of foreclosure are higher; increases in income and asset inequality, especially for minority groups; and this financial wealth gap that's widening, and Tom Shapiro and colleagues work increasing four times between 1984 and 2007, with one-quarter of African Americans owning no assets at all.

And we know that assets are very closely tied to the future. And I think one of the things that would be interesting to talk about is if people -- and we found this certainly in our qualitative research -- if people can envision a future, they feel much more secure about it. And one of the things that we think assets does, actually, is it provides a lens for people to be able to see their future and that, without that, it's a month-to-month deal. So we look at capability a little bit differently than a lot of the financial capability discussion today. We look back at Amartya Sen and Martha Nussbaum's work on capability theory where Martha Nussbaum has said that internal capabilities, in other words, the kinds of things that people -- one could think about this as financial literacy in that world and external conditions, which I'm talking about as a sociologist, equals the combined capabilities. And this last part is from Nussbaum's work: Policies, laws, regulations, and practices can provide opportunities for all individuals to develop the full range of capabilities that lead to well being. So if we -- we sort of have translated this into financial capability, and we think about this as financial education. So one's understanding and knowledge and skills personally plus their financial participation will equal their financial capability. And this financial capability requires not only the ability to act within the individual, so the knowledge skills, confidence, motivation, but also the opportunity to act. And that is access to beneficial financial services and products. And this is probably where our understanding of the term "capability" differs a little bit, because we think sort of conceptually about this as one could think about economic socialization leading to and then financial education leading to financial literacy. So that's the top part of that -- of that schema. And the bottom part is sort of the financial products and services, which would include whether they're accessible, whether they're affordable, whether they're easy to use, whether they're safe and reliable leads to financial inclusion. And the two of those combined are one's financial capability. In this sense, then, it's a little bit like social psychology in that financial capability does not reside within the individual. It actually resides within the individual in their environment, which I think is a critical difference because it does suggest that one or the other is not going to work alone.

So financial socialization, just to break that model apart a little bit, modeling within the family, participation in family financial planning, lots of research has been done on this, financial education, both the formal and informal instruction. Also, you know, accumulating amount of research in that sphere. But financial actions are not just a matter of individual effort, informed decision, preferable choices, and good financial habits. We talked actually to a lot of people who are low income who do all of those and still have a great deal of difficulty managing and saving for the future. So, for example, when an employee has a retirement account at work, it seems like a choice to sign up unless they're in one of the opt-out programs that -- that we've been learning about in recent years. But when an employee has no retirement account, there is no opportunity for this choice. So middle range theory and empirical inquiry on social institutions suggest features of financial services and products that shape consumer behavior. So this is where we're sort of moving into a kind of conceptual model and perhaps some indications of where -- what directions we might go in terms of policy. So we think about these social institutions as having certain -- being made up of certain constructs. And I think we'll see reflections of what -- what Dan and John have just talked about and Susan, actually, coming back around to some of the work -- the empirical work that she presented, that it matters whether there's access: the ability and right to approach, enter, and use and communicate with an institution.

Many low income people will say, I don't feel comfortable walking into that place or it's not in my community or it cost too much to get there. Information, knowledge about the services; the incentives which have already been discussed, both positive and negative. We have a lot of disincentives for low income families to participate in banking services because of fees. Facilitation, mechanisms that make products and services easy to use, such as opt-out, direct deposit, that kind of thing. Expectations, and this is where the targeting, the idea of anchoring on an idea, on a goal will make a difference for people. And we certainly saw that in our low income families who were saving. Restrictions such as limitations on use and security obviously a big issue today about whether people's money is safe in the institution. So these are just some examples. But I think what's important about this is that these provide leverage points from a policy perspective about what we might do in terms of organizing financial products and services.

So for access, and Dan just gave us a few great examples in his talk, but starter account products; training and education, which would increase information; a match or a higher rate of return as an incentive; targets or goals, which sets an expectation; withdrawal penalties, examples of restriction; and consumer protections for security.

So here's just a couple of examples from the quantitative side of the research that we've done on savings for both expectations and information. This is part of the American Dream demonstration research that was done, The Experiment. And what they found was, in terms of expectations, a match cap is more effective than a match rate, which I think surprised me. And it's sort of why we came up with the idea of expectations as being so critical and in terms of encouraging more savings. So controlling for many other variables, a dollar increase in the match cap, that's how much would be matched by the program. So they save $750, that was their cap. That that match cap is associated with a 57 cent increase in monthly net IDA savings. Higher match rates, however, in some cases and maybe the data kind of look like it may be associated with lower savings among savers. And that's -- I mean, that's the dilemma, right, with these kinds of incentive programs. On information, up to a point, financial education encourages higher savings. So for every up to ten hours of education, there was -- there was a positive effect on savings. And then, after that, it really didn't make any difference, which actually is good news because financial education is expensive. So it's better that it just didn't keep going up, you know, to 50 hours.

So final words from Cynthia, another participant in this savings project, very articulate about where she wanted to go in life and was working hard to save and facing a lot of barriers. And she said -- she said, “We just need more keys, more information. We need more tools put in our hands. Don't just tell me, You need to save, or, Are you saving? Help me. Show me the arena. Give me access to the arena.” I think, you know, her comments really illustrate the -- the sort of sense that people feel that they don't have access to the way to get ahead.

Research implications, you know, these always come at the end of talks. But this is so critical, I think. We -- you know, we have a very parsimonious model in traditional economic thought, and it's very helpful. It's -- you know, it's provided a whole way of understanding human behavior in their economic lives. I think what we've been talking about here today is moving beyond that model, but we have not really come up with the kind of parsimonious way of thinking about human behavior that we have to do. So we really have to start building the blocks; taking each of these constructs; investigating these features, the combinations of features that will really make a difference in how people respond. Use both qualitative and quantitative data to do that, especially in controlled experimental conditions, testing that out. And assess not just the short-term actions but the long-term impacts on well being. So one of our concerns is not just did people sign up for a product or a service; not just did they participate over time; but what impact did that have on themselves, on their families, on their futures and the way they think about the future. And that all requires a great deal of work. I think it's very promising that we are, as Bob suggested, talking more across disciplines because I think that will really be required. I think there's a lot of fertile work to be done out there in that regard. And with that, thank you very much.