STUDY SUMMARY

Can Prize-Linked Incentives Promote Debt Reduction?

Large debt burdens are a significant threat to financial stability for many households. Innovations for Poverty Action is working with researchers to evaluate whether prize-linked incentives can help borrowers reduce their debt burdens more effectively. A randomly selected group of borrowers on debt repayment plans were offered entry into a program that turns on-time debt repayments into entries in a lottery. Researchers are studying whether prize-linked incentives influence debt reduction, delinquency and default, programmatic retention, and whether the program can be financially self-sustaining.

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COUNTRY
United States

PARTNER

PROGRAM AREA
US Finance

TOPICS
Behavioral Design, Financial Capability

TIMELINE
2015-2018

Policy Issue

As of January 2015, Americans held approximately $887 billion dollars in outstanding credit card debt. High levels of debt can be financially problematic for consumers, particularly unpaid balances, which compound, growing as they remain unpaid. One approach to help people repay debt is Debt Management Plans (DMPs), in which providers negotiate a repayment plan with creditors on the borrowers' behalf based on their monthly budget. However even with a DMP, those in debt may face repayment obstacles including income constraints, unexpected financial setbacks, and common behavioral tendencies to put off difficult tasks, even when in one's own long-term best interest.

Prize-linked programs are becoming an increasingly popular approach to try to incentivize people to engage in positive financial behaviors. Designed similarly to a lottery, participants in a prize-linked program are offered a chance to win a prize every time they engage in a specific financial behavior. While prize-linked programs are popular in many countries, they are usually implemented to try to promote savings, and there have been few randomized evaluations investigating whether prize-linked incentives can promote positive financial behavior. In the United Kingdom, for example, data suggests that consumers prefer prize-linked savings products, but there is no evidence that they promote behavioral changes. While there is reason to think that prize-linked incentives might help consumers improve their financial behavior, whether they actually do is still unknown, particularly in regards to debt reduction.

Evaluation Context

Innovations for Poverty Action is working with a non-profit debt management provider who serves clients with outstanding debt in all 50 US states. The DMP consolidates non-Mortgage, non-Student, and non-Auto debt. Their average client is approximately 40 years old, earns $40,000 per year and owes approximately $17,500 in unsecured debt. A typical DMP plan lasts three to five years, but only approximately a third of clients successfully complete the program.

Details of the Intervention

Innovations for Poverty Action is working with researchers to test whether prize-linked incentives improve debt reduction, decrease defaults and delinquencies, improve programmatic retention, and whether these incentives can be offered in a financially self-sustaining fashion.

IPA and the debt management provider randomly offered selected existing clients and newly enrolled clients a chance to participate in a prize-linked debt repayment program. With each on-time monthly debt payment in 2016, participants were entered into a monthly drawing to receive $500 to be applied to the balance of their DMP. Each successful monthly payment also granted the participant one entry into the end of the year grand prize drawing; $10,000 to be applied to the balance of their DMP. Clients received monthly emails about the winners of sweepstakes drawings.
The researchers are measuring the effects of the program on timely DMP repayment, balances on other outstanding debts, bankruptcy, and other indicators of financial health.

Results and Policy Lessons

Project ongoing, results forthcoming.

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