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US Household Finance Initiative



Dartmouth

Household Debt is Where the Money Is: Product Solutions, Marketing Challenges

Jonathan Zinman
Dartmouth College and
IPA's U.S. Household Finance Initiative

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What's This Talk About?

- Huge opportunity to add value by helping people manage their borrowing decisions
 - Focus on *loan shopping*
- Huge challenge is pricing and marketing
 - Product development relatively easy to solve
 - Selling value proposition is not so easy to solve
 - Business model tied up in this
 - Roadmap for figuring this out





Debt is Where the Money Is

- For most Americans
- \$13 trillion on household balance sheets
 - Many more people participate in debt market(s) than in, e.g., stock market
- Borrowing costs $>$ asset yields
 - Higher stakes



Household Mismanage the Liability Side of Their Balance Sheets



- (Or at least evidence suggests that they do)
- Sources of “decision inefficiency”
 - Overspending
 - Undershopping
 - Upfront contract choice (e.g., overpaying)
 - Failure to refinance
 - (Misallocation/workouts)
- Money on table => Money to be made





Is There Really Money to Be Made?

- Focus just on overpaying. Take a household that:
 - Has \$10k in credit card debt and pays +500bp
 - Has \$20k in auto loans and pays +100bp
 - Has \$200k in mortgage and pays +100bp
- **This household is paying \$2,700 in excess interest *per year***
- Potential to add even more value by:
 - Helping consumers reduce principal balances: capture spread between APR and risk-free rate
 - Helping choose other contract terms (fixed vs. variable, downpayment vs. APR, maturity, etc.)

What Do Consumers Need?

(Product Development: 30,000-foot view)



Personal loan shoppers (focus today)

- Existing market lacks clarity, credibility

Previous BeFi talks:

Debt management tools on spending margin

- For durables (how much car? house? college?)
- For discretionary (managing cards)

Debt management tools for debt reduction

- **Borrow Less Tomorrow:** SMarT with bigger bang for buck

On-ramps from borrowing to saving

- Auto-convert loan payments to savings once loan is paid off

Where do Consumers Go Wrong? (Product Design and Marketing)

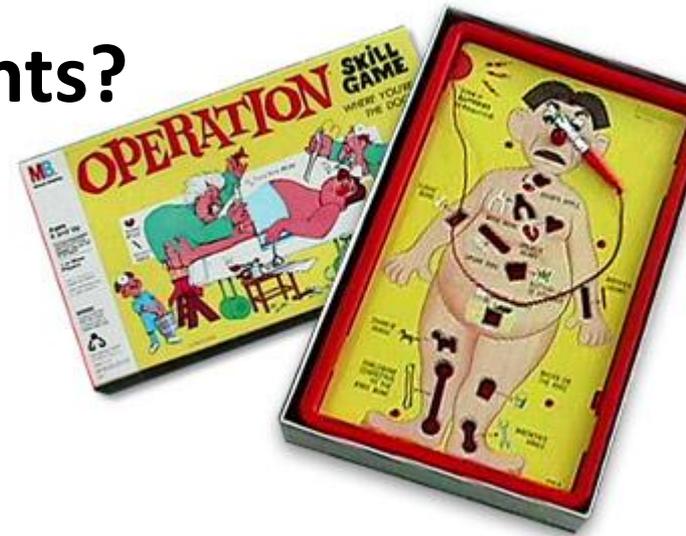


What leads to undershopping, overspending?

- Behavioral factors: self-control costs, limited attention, price misperceptions
- Confusion (financial illiteracy/innumeracy)
- Disutility from personal financial management (distaste, time costs)

How to solve for these pain points?

R&D





R&D for Personal Loan Shopping

- Building a product that salves/solves
 - Personalized, simple, timely
- *Get people to pay for it
 - Kickback model dominates, so differentiate
 - Wouldn't transparent pricing be better?
 - Branding
 - Regulatory constraints/threat
 - Signaling value proposition
- So how do we get there?
 - Issue for value-added services more generally

Beta-/AB-Testing for Value-Added Business Models



- Let's say we have an shopping app/platform that can save someone \$2,000 per year. How to sell it?
 - Informative appeals
 - How to frame cost savings?
 - How to signal quality/credibility?
 - Emotional appeals
 - How to capture attention?
 - How to counter procrastination?
- Behavioral evidence suggests that:
 - Both informative and emotional *can* be effective
 - Context and customer-particulars matter
 - => **Optimizing content requires experimentation**

Beta-/AB-Testing for Value-Added Business Models



- How to price it? No way people will pay?
 - But people *do* pay out of pocket for credit report management, identity theft protection, tax prep, etc.
- Potential retail pricing solutions
 - Upfront lump-sum
 - Natural for cash-out refinancing?
 - Otherwise paid by credit card?
 - Monthly subscription
 - Teaser?
 - Periodic “debt under management” fees
- Behavioral evidence suggests
 - Willingness-to-pay depends a lot on framing, timing
 - => **Optimizing framing content* pricing requires experimentation**



What Was This Talk About?

- Huge opportunity to add value by helping people manage their borrowing decisions
 - Focus on *loan shopping*
- Huge challenge is pricing and marketing
 - Transparent pricing as an opportunity
 - Consumers will pay out-of-pocket with right framing, timing
 - Behavioral research offers insights, but no prescriptions
 - Getting this right requires systematic testing