

PROJECT EVALUATION: Commitment Savings



Fighting Poverty
with Innovation,
Evidence and Action

United States



Saving money can be difficult, and growing evidence suggests that self-control issues may contribute to undersaving. IPA partnered with Neighborhood Trust Financial Partners in New York City to conduct a randomized evaluation of a simple commitment savings product, as well as its performance relative to more conventional financial counseling. The study finds strong demand for the product among low-income households, and account holders successfully used the product to accumulate savings.

Project Overview

RESEARCHERS:

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PARTNERS:

Neighborhood Trust Financial
Partners & Neighborhood Trust
Federal Credit Union

LOCATION:

Upper Manhattan, New York City

SAMPLE:

1167 members of Neighborhood Trust
Federal Credit Union

TIMELINE:

2009 - 2012

THEMES:

Savings, Product Design, Financial
Literacy, Commitment Devices

POLICY GOALS:

Explore the use of behavioral
approaches to increase savings

POLICY IMPLICATIONS:

We find strong demand for
commitment savings products, and
credit union members used the
product successfully to accumulate
savings.

POLICY ISSUE

Managing finances can be difficult for any household, rich or poor, but low-income households face particular challenges, often lacking the resources to rebound from a bad financial decision or unforeseen adversity. There are many arguments for building and maintaining regular savings habits, from preparing for emergencies (and even anticipated expenses such as holidays) in the short run, to preparing for retirement in the long run. However, household savings rates in the United States are widely considered to be inadequate, especially among

*“43% of all American
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asset poor”*

low- and middle-income households.

According to CFED's 2012 Assets & Opportunity Scorecard, 43% of all American households are liquid asset poor.¹ Liquid asset poverty is defined as a household without sufficient liquid assets, such as cash or bank accounts, to subsist at the poverty

level for three months in the absence of income. Indebted households are at particular risk; as they struggle to cope with the day to day pressures of servicing their debts, they are unable to plan for the long-term.

New research on commitment savings products, however, suggests that financial products themselves may have a role to play in helping low-income households achieve their savings goals. Commitment savings products are designed to help individuals overcome competing influences for their money like social pressures, bad habits or even lack of self control. Informal financial practices from the developing world have informed the development of formal commitment devices in savings products. For example, Rotating Savings and Credit Associations (ROSCAs) are informal savings groups wherein members meet regularly and



contribute an equal amount of money to the group at each meeting. Each member receives the lump sum of collected funds once, and meetings continue until each member has received the large sum once. ROSCAs are common throughout Africa, Latin America and Asia, and create social obligations among the members to continue saving throughout the lifecycle of the ROSCA.

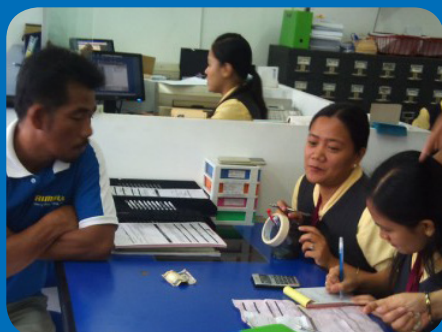
In some cases, low-income households demonstrate a willingness to pay for restricted access to their savings. In Ghana, for example, traditional Susu collectors collect small deposits from customers on a daily basis, charging a commission on deposits or a fee for fund

withdrawals. These practices not only demonstrate that low-income families have the desire to save, but also that they are willing to place voluntary obligations on themselves or incur costs in order to meet their savings goals.

In the United States, some evidence for the role of commitment in increased savings comes from tests of workplace savings programs, where a combination of defaults and sticky choices for contributions to retirement accounts has led to marked savings increases.³ However, not all employers offer opportunities to build savings for retirement through a 401(k) or other investment program. Blue-collar, hourly or seasonal workers in particular may lack access to employer-based savings programs.

LESSONS FROM THE PHILIPPINES

In 2005, IPA investigators Nava Ashraf, Dean Karlan and Wesley Yin designed the first formal commitment savings product in collaboration with Green Bank of Caraga in the Philippines.² The SEED (Save, Earn, Enjoy



Deposits) account provided individuals with the opportunity to voluntarily commit to restricting access to their savings. The terms of each commitment are customized, and individuals select either a savings goal date or amount. Individuals made continuous payments throughout their commitment period, and were restricted from withdrawing funds until they reached their self-specified goal. Aside from this commitment feature, the SEED account was identical to Green Bank's normal savings account.

Ashraf, Karlan and Yin conducted a field experiment to test the effectiveness of the SEED account with a sample of 1,777 randomly selected Green Bank clients. Individuals who were offered the SEED account, as well as individuals randomly assigned to a control group (which received the traditional savings account), were surveyed once at baseline and then again one year later in order to measure changes in savings, attitudes and household economic decisions. Researchers found an 81% increase in savings among those clients who had opened a SEED account after one year compared to the control group. These results suggest that formal commitment savings accounts have an important role to play in the accumulation of assets among the world's poor.

For more information about IPA's study with Green Bank of Caraga, go to www.poverty-action.org/provenimpact/commitmentsavings

THEORETICAL FOUNDATIONS

What explains low levels of household saving? Part of the story may be explained by low levels of financial literacy, or the inability to make sound financial decisions or plan for future financial needs. Studies of retirement savings in the U.S. suggest that financial education in the workplace and match incentives can significantly increase savings.

Another potential factor contributing to low savings rates is behavioral. Consumers the world over have been shown to be more impatient in the near-term than in the long-term and thus have a propensity to make purchases that are later regretted. In a series of lab experiments, Bone, Hey and Suckling find that a majority of people do not plan ahead and that the opportunity to gain experience does not make them more likely to plan.⁴ Interestingly, they find more evidence of planning when people are forced to pre-commit to a decision. The potential benefits of pre-commitment go beyond the creation of a plan of action. The novelty of a commitment device is that people may benefit from voluntarily imposing additional costs on themselves to give themselves added incentives for goal attainment. Research



suggests that commitment devices might be a good mechanism for mitigating tendencies for poor planning and procrastination.

SUGGESTED INTERVENTIONS

Standard approaches to helping consumers make better financial decisions focus on financial education, which can be costly to implement and difficult to scale. Given existing evidence from the developing world suggesting that savings products with commitment features may be effective at promoting savings, is it possible that a commitment savings product alone could produce comparable or better results than a financial education intervention in a U.S. context? To answer this question, Innovations for Poverty Action partnered with Neighborhood Trust Financial Partners (formerly Credit Where Credit is Due) and its financial institution partner, Neighborhood Trust Federal Credit Union. Neighborhood Trust Financial Partners (NTFP) is a nonprofit organization serving the Washington Heights neighborhood of Upper Manhattan in New York City, home to the largest concentration of immigrants from the Dominican Republic in the United States,⁵ and a median household income of \$31,000.⁶ The poverty rate in the Washington Heights and Inwood neighborhoods is 31%, as compared to New York City’s overall rate of 21%.⁷ Neighborhood Trust promotes financial mobility and wealth creation by offering financial education programs in tandem with gateway financial products from its financial institution partner, Neighborhood Trust Federal Credit Union. Neighborhood Trust Federal Credit Union is a community development credit union with over \$8 million in assets and nearly 4,000 members.

“Could a commitment savings product alone produce comparable or better results than a financial education intervention?”

For the purposes of this study, IPA and Neighborhood Trust developed a commitment savings product specifically targeted to low- to medium-income households in New York City in order to test the impact of the commitment feature on savings behaviors. This product was then compared to NTFP’s existing financial counseling services.

Super Saver CD – The Super Saver CD (SSCD) is a balance-building Certificate of Deposit whereby the client makes an initial commitment to save a goal amount (up to \$10,000) within a customizable maturity term (up to 18 months), by making weekly or monthly deposits towards

that goal. Clients have the option of opening 3, 6, 12 or 18 month CDs, and can start with a low initial deposit of \$15, eliminating the large minimum balance that can make traditional CD products inaccessible to low-income savers. As with a traditional CD, once funds are deposited into the SSCD they cannot be withdrawn by the owner without closing the CD and forfeiting accumulated interest and the initial \$15 deposit. SSCDs that reach maturity but fail to meet their stated savings goal forfeit earned interest. Upon opening a SSCD, clients are shown a payment schedule with dates and required savings amounts; they can choose to set up automated transfers to the CD from their regular savings account or make manual deposits at the credit union.

One-on-One Financial Counseling – Neighborhood Trust’s trained financial advisors work one-on-one with clients to alleviate financial crisis and establish the building blocks of financial security. Hour-long sessions focus on goal-setting, budgeting and financial discipline, debt management and saving. As part of this intervention, clients receive a comprehensive financial diagnostic, a copy of their credit report, and an



individualized budget that includes regular savings behaviors. Counseling sessions are offered free of charge and clients are able to return for free follow-up sessions if necessary.

STUDY METHODOLOGY

Innovations for Poverty Action implemented a randomized evaluation with the following objectives:

1. Mobilize savings in a formal financial institution and improve financial portfolios among study participants
2. Evaluate the effectiveness of financial education and commitment contracts to encourage sound financial behavior
3. Contribute to academic and policy literature on behavioral finance and financial product design for low-income American families

Fieldwork took place at Neighborhood Trust Federal Credit Union between March 2010 and May 2011. The study population is made up of 1,167 individual members who visited the credit union during this timeframe. Credit union members were approached by IPA staff in the lobby as they waited in line at the teller window or waited for a loan officer, and were invited to take a 10-minute survey about their financial well-being. At that point they also authorized IPA to conduct soft pulls of their credit report for research purposes. All participants were offered a \$10.50 subway pass as an incentive to participate in the study.

The baseline survey collected demographic information, a descriptive portrait of the financial situation, financial attitudes, and financial literacy levels of individuals in the sample. Members who consented to participate were administered a baseline survey electronically on a computer kiosk in a secluded corner of the credit union lobby in either English or Spanish. All Neighborhood Trust Federal Credit Union members over the age of 18 were eligible to take the survey. At the conclusion of the survey, members were randomly assigned to one of three treatment groups:

1. Super Saver CD offer
2. Financial counseling offer
3. Control – no offer

Members randomly assigned to the Super Saver CD group were then given the opportunity to open the product on the spot with a surveyor, who shared written marketing materials, explained product features, and provided an application form. While members were encouraged to open an account with a member services representative at the time of taking the survey, they were also able to return to the credit union and open the product at a later date. IPA staff conducted follow-up marketing calls to members of this treatment group, in addition to mailing additional marketing materials to members' homes, in an effort to promote the product.

Members who were placed in the counseling group were given the opportunity to sign up for a free counseling session at the conclusion of the survey. Appointments with a counselor were scheduled by the surveyor in person, and the member was called by phone to confirm the appointment.

STUDY POPULATION CHARACTERISTICS

- 63% of the respondents were female
- Average age is 49 years old
- 74% chose to take the survey in Spanish
- 86% earned less than \$40,000 per year; 55% earned less than \$20,000 per year
- 75% had less than a college degree; 24% had not completed high school
- 36% described their overall financial situations as "bad" or "very bad"
- 19% were unable to pay their rent, mortgage or utility bills in the past year
- 41% were dissuaded from applying for credit in the past year due to their financial situation
- In the past year, 14% had to skip meals or reduce the size of meals because there was not enough money for food
- 80% agreed with the statement: "I often find that I regret spending money. I wish that when I had cash, I was better disciplined and saved my money rather than spent it"





FINDINGS

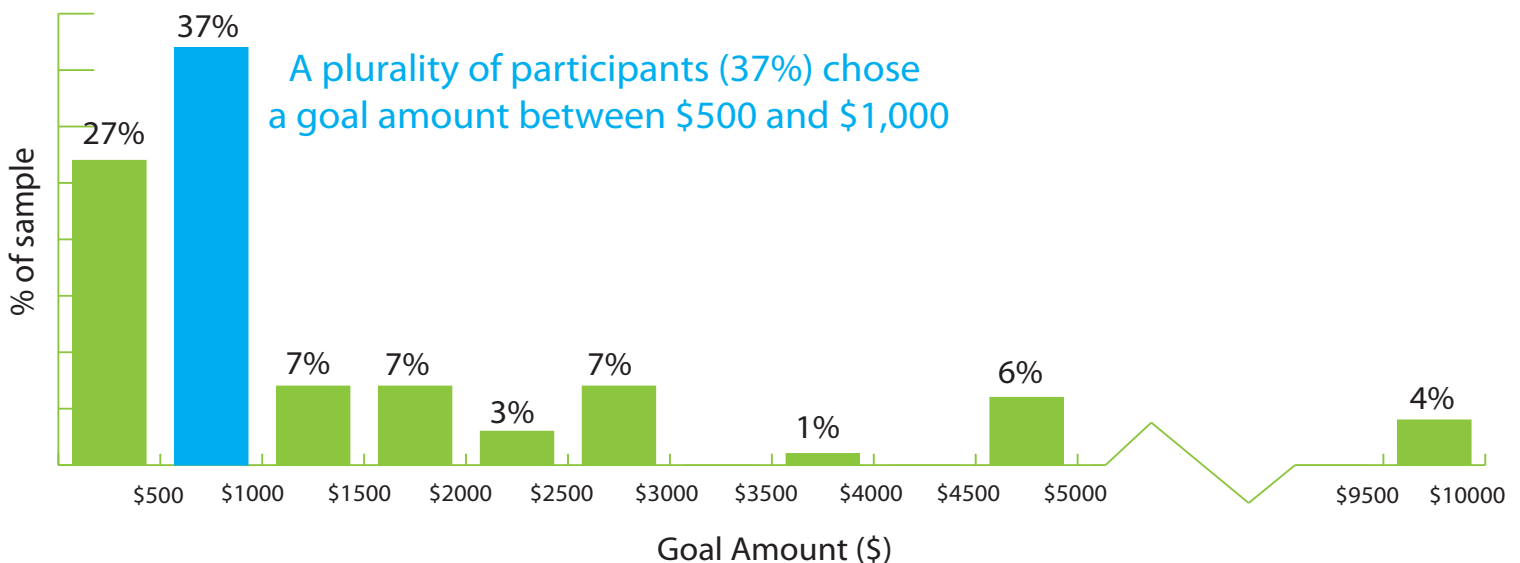
Demand

Among the key results of this research is that demand for the SSCD product is high. Twenty one percent of those randomly offered the product opened an account. Analysis of the 381 individuals assigned to the CD treatment group shows that the gender and incomes of respondents was significantly correlated with take-up. Women were significantly more likely to take up the SSCD than men. Though we cannot exactly determine why this correlation exists, it may be due to surveyor effects or a desire on the part of women to maintain control over household resources.

Individuals with incomes less than \$20,000 were 26% more likely to take up a SSCD account as compared to individuals with incomes greater than \$60,000. Respondents with incomes in the range of \$40,000 to \$60,000 were about as likely to open a CD account as those with incomes higher than \$60,000. In short, lower income respondents were more likely to open a CD account. This could perhaps be explained by the relatively small penalty (\$15 and accumulated interest) for early withdrawal, which may not be economically meaningful for high income individuals looking for commitment savings products. The maximum contribution for the SSCD, at \$10,000, may also be a factor.

The education and age of respondents was not significantly associated with CD take-up. Nor was the language that respondents took the survey in. Surprisingly, given that the SSCD is differentiated from other CD products by its commitment features, the measures of behavioral biases relevant to financial behavior such as self-control problems, time-inconsistency, exponential growth, and limited attention are not significantly correlated with SSCD take-up.

Survey questions that sought to capture qualitative differences in household situation do not significantly predict take-up. Nor is baseline ownership of financial products such as checking accounts, savings accounts, credit cards, CDs, and various types of loans a significant predictor of take-up.



United States

Overall, 15.9% of counseling-group respondents took up a counseling offer, defined by whether they came to a counseling appointment, out of a total treatment-group sample of 397 individuals. None of the baseline variables was predictive of take-up, other than how respondents characterized their own financial situation. As might be expected, respondents who viewed their financial situation as “ok” or better were less likely to take up an offer of counseling than those who described their financial situation as “bad” or “very bad”.

Product Usage

Individuals who took up a Super Saver CD offer used the product in quite different ways. Nearly half of the treatment-group take-ups chose SSCDs with 18-month maturity terms, while about 30% chose 6-month CDs, and about 20% chose 12-month CDs. Similarly there was a wide range in individuals’ chosen goal amounts: the 10th percentile goal amount was \$300, the median was \$1000, and the 90th percentile was \$4000.

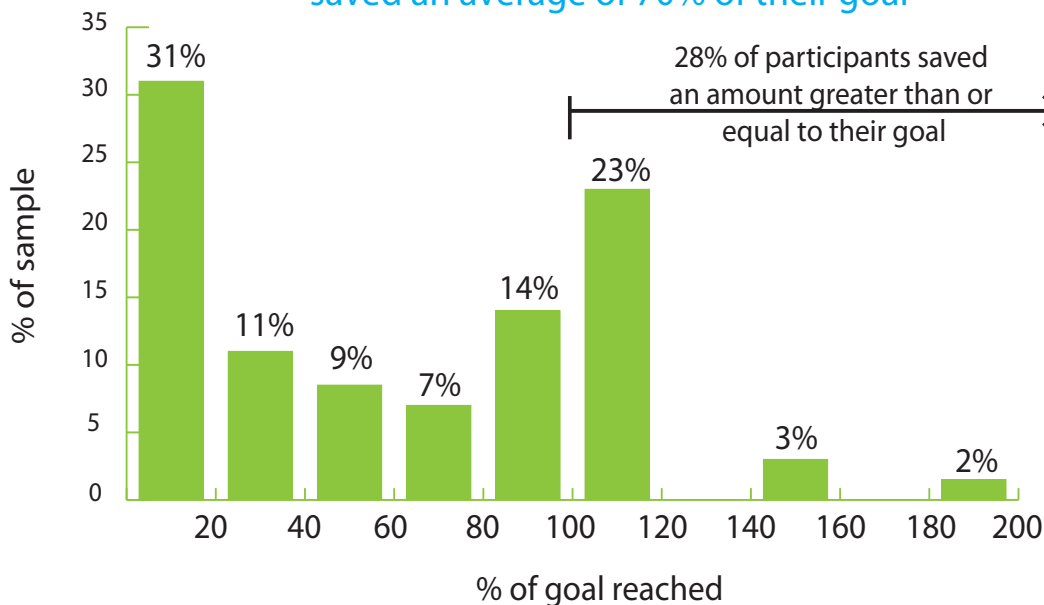
Among the 86% of treatment-group SSCDs that had matured (or had been closed before their maturity date by the owner) as of March 1, 2012, only 32.5% had met their savings goal. Nonetheless most individuals made substantial progress toward their goal, with the median SSCD accumulating 56.5% of its goal amount by closure or maturity. Even among the subset of SSCDs that did not reach their savings goal, the median SSCD accumulated 27.9% of its goal amount. Total balances at maturity or closure were also considerable: the average was \$910, and the median was \$417.

“Most individuals made substantial progress toward their goal, with the median Super Saver CD accumulating 56.5% of its goal”

Impact

A crucial question is whether savings accumulated in SSCD accounts were achieved at the expense of drawdowns in other asset accounts or an increase in debt. We focus on differences in quarterly balances data from the Credit Union between those who were offered the SSCD product (rather than those who took up the product) and the control and counseling groups. For each individual, the analysis horizon begins at the quarter before the respondent is surveyed, and proceeds for the four subsequent quarters.

Overall, those who opened a Super Saver CD account saved an average of 70% of their goal



We do not find significant evidence of either the SSCD product offer or the financial counseling treatment increasing savings balances, increasing net assets, or affecting borrowing behavior relative to the control group. Most of the results are in the expected direction, but they are too imprecisely estimated to make meaningful statistical inferences. This is due to the relatively small sample and high variance in balances across individuals and over time. Treatment non-compliance also reduced the precision of our estimates.

For a broader view of the financial complementarities and substitutions that might be implicated in an offer of an SSCD



product or counseling, individual's credit reports were also analyzed. These "soft pulls" do not affect an individual's credit history. The outcomes measured include: (i) an individual's credit score ("FICO score"), (ii) the number of active trade lines on an individual's credit report in the past year, (iii) an individual's total outstanding credit card debt, (iv) the log of an individual's total outstanding credit card debt, (v) an individual's credit utilization rate in the past year, (vi) the number of negative trade lines on an individual's credit report in the past year, which is a measure of mild delinquency, (vii) whether an individual has any delinquent or 90-day-late trade lines in the past year (severe delinquency), and (viii) the number of delinquent or 90-day-late trade lines in the past year. Here too, the results are imprecise and do not provide significant evidence for the hypothesis that either an offer of the SSCD product or counseling affected individual's credit report outcomes.

NEXT STEPS

While these results are encouraging, there is no significant evidence that the savings product or counseling offer increased the treatment group's savings relative to the control group, or affected the treatment group's credit behavior relative to controls. It is possible that this null result is due to small treatment effects – perhaps because of substitution between SSCD savings and other savings at the credit union. Our empirical analysis also faced several challenges that limit our ability to estimate treatment effects precisely, such as low statistical power, non-compliance with treatment assignment, and high variance in outcome variables such as savings behaviors. In spite of these challenges, this study lays the groundwork for future research in designing and testing commitment savings products and financial counseling.

More research, with larger treatment groups, is needed in order to obtain conclusive results. Adding hundreds of additional observations from a similar study, launched in Washington DC in May 2011, should allow us to fill the gaps in our learning and better understand the performance of this product in the long run.

Endnotes

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Acknowledgments

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