

# Behavioral Economics: Insights for the Unbanked and the Underbanked

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## **Standard Economics**

- Assumes rational choices based on stable preferences, and complete knowledge to maximize satisfaction

## **Behavioral Economics**

- Uses concepts from psychology to investigate how social, cognitive, and emotional factors affect our choices

# Why Study Behavior?

- Describe what people *actually* do, and why
- Recommend what individuals *ought* to do
- Recommend what society *ought* to do

# Standard Model...

## how things ought to be

- We are able to carefully weight costs and benefits
- We are able to consider all relevant information
- We plan for the lifetime
- We are kind of selfish



# Behavior Economics... what people actually do

- We fail to consider costs and benefits
- We can't process all information available
- We are present-oriented
- We kind of care about others... we make comparisons



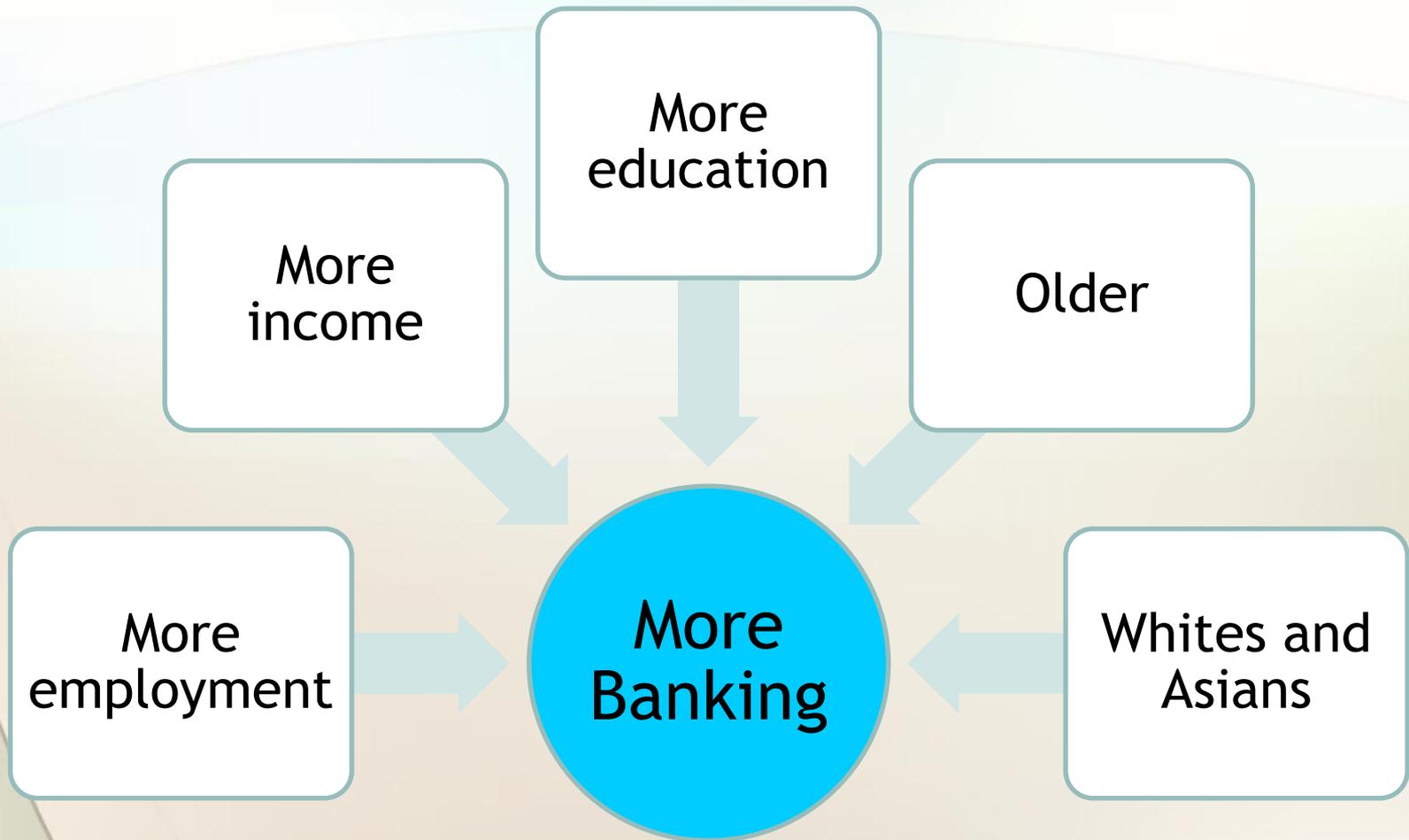


**The BIG Reveal:  
People are not always Rational!**

**First Research Question:**

**Is the economic choice of being  
unbanked or underbanked a  
rational one?**

# Evidence from 2013 FDIC National Survey of Unbanked and Underbanked



# Unbanked Adults Demographics

Unbanked Adults	
<b><i>Overall – US adult population</i></b>	<b>7.6%</b>
African-American	32%
Hispanic	24%
Native American/Alaska Native	29%
Single female parent household	20%
Single male parent household	15%
Household income less than \$30,000	20%
Less than a high school diploma	25%

Source: FDIC 2009 Survey of Unbanked and Underbanked Households

2013 FDIC National Survey of Unbanked and Underbanked

## Reasons for Being Unbanked

- Not enough money
- Don't like dealing with or don't trust banks
- Account fees are too high/unpredictable  
(previous banked households more likely to pick this one)
- ID/Credit/Bank history problems
- Privacy
- Banks do not offer needed products or services  
(only 1.2% picked this as the main reason... payday lending)

# Why do we care about the unbanked/underbanked?

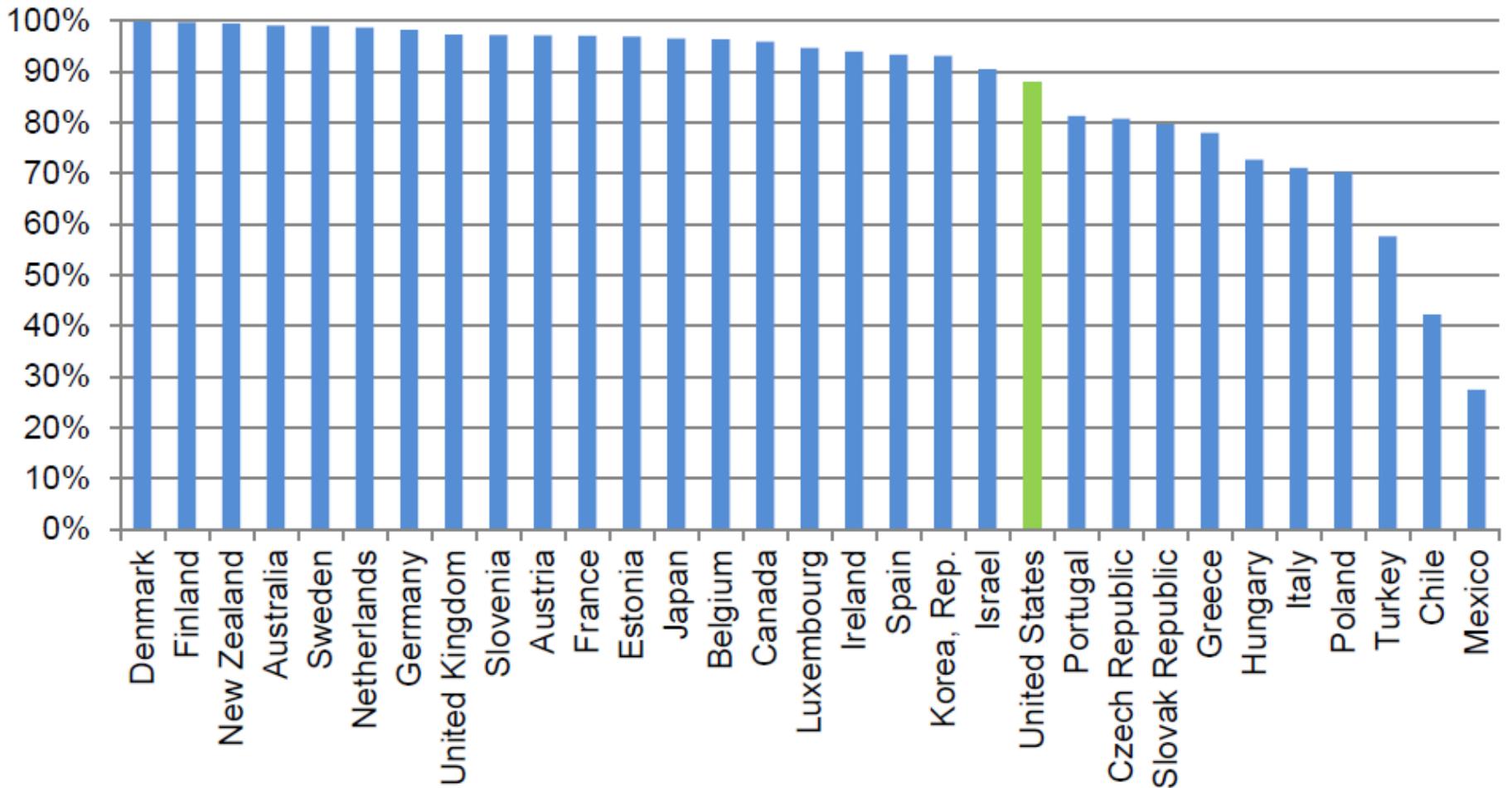
- Banked households have more assets
- More small business owners amongst banked households
- Externalities:
  - Employers: payroll
  - Retailers: more access to credit, payment methods
- For banks/credit unions, more business

**Some** Households might be better off **not** being banked

**Most** Households might be better off **being banked**

We just don't know **the split**

## Account at a formal financial institution (% age 15+)



Source: 2013 A Cross-Country Analysis of Unbanked Within the OECD

# Unbanked/Underbanked: Possible Issues

## Bounded Rationality

- Processing information is costly
- Our perception is biased: overconfidence, use of rules of thumb, status quo bias

## Bounded Willpower (self-control)

- We put off doing things we don't like...
- We don't do what is good for us
- Procrastinate even the good stuff

## Bounded Selfishness

- We care about others feelings and opinions
- We display altruism/warm glow, use clues from others

# Strategies: Bounded Rationality

- Relevant information: brief and easy to understand (graphics and pictures work!)
- Benefits of banking/costs of AFS
- When there is ambiguity, people clink to the *status quo*

## *Conflict and the status quo*

### **Proliferation of Choice**

Shoppers in upscale grocery store encounter tasting booths for jams:

**6 jams:** (40% stopped); **30%** bought

vs.

**24 jams:** (60% stopped); **3%** bought

(Iyenger & Lepper, 2000; B. Schwarz, 2000)



401(k) options: For every 10-option increase, individuals' participation probability declines by ~ 2%

(Iyengar & Jiang, 2005)

# Strategies: Bounded Willpower

- Easy to open account: smartphones  
{can we scan ID barcodes?}
- Commitment Devices: free checking if transfer  $X$  every month to a savings
- “Now” Incentives: immediate gratification

# Tying Odysseus to the Mast

- People demand commitment devices to help them save
- They prefer limited access to their money - a locked piggy bank, banker has the key



# Strategies: Bounded Selfishness

- Social media/social feedback
- Use of peer groups
- “Family” options
- Nudge people towards the desirable behavior/social norm
  - Instead of 7.7% of people are unbanked
  - **92.3% of American households are banked!**



**Thank You!**

If you have any questions, contact me at:  
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