How Consumers Use Plastic — and Why

BY MATTHEW CONNER

"Credit Card Debt and Payment Use." Charles Sprenger and Joanna Stavins, Federal Reserve Bank of Boston Working Paper 08-2, May 2008.

Nearly half of credit card holders in the United States can be referred to as "revolvers" — those who regularly carry balances on their cards. Those who pay off their balance every month can be called "convenience users" of credit cards because they use the cards as an easy form of payment technology. The authors of this study examine the differences in the use of payment technologies between these two groups of people.

Using data from the Survey of Consumer Payment Preferences for more than 1,800 individuals who use both debit and credit cards, the authors examine the four different ways these people can pay for goods: credit cards, debit cards, checks, and cash. They report significant evidence that individuals regularly carrying revolving debt are more likely to substitute the use of a debit card for that of a credit card. In other words, these individuals use credit cards for a significantly lower percentage of their total payments than do convenience users of credit cards. However, there is no significant difference in the use of cash and checks between the two groups.

From the same survey, the authors infer that revolvers use debit cards more often not because they perceive it as an easier form of payment at the check-out. Instead, they are more likely to use debit cards because they see them as a good way to control their spending.

"Are Children 'Normal?'" Dan Black, Natalia Kolesnikova, Seth G. Sanders, and Lowell J. Taylor, Federal Reserve Bank of St. Louis Working Paper 2008-040C, October 2008.

In 1960, Gary Becker first posed the question: Does the demand for children follow the pattern of a "normal" good? In consumer theory, increases in income induce greater consumption of "normal goods." So, to restate Becker's question: As the incomes of married households rise, will that lead to an increase in fertility?

The authors of this paper evaluated this question using data from the 1990 census. They discovered that fertility and household income are inversely related for non-Hispanic white married women. This suggests that children are not "normal goods." However, when the amount of education the women have is held constant — that is, when you compare a college graduate to another college graduate — a positive correlation between the husband's income and fertility appears. From this brief cross-sectional examination, the authors conclude that in the United States, fertility exhibits the characteristics of a normal good if the women being compared have similar human capital.

In order to more fully answer the paper's motivating question, the authors turn to a natural experiment: They examine the effect of a large increase in coal prices in Appalachian coal-mining counties during the energy shock of the 1970s. The large increase in the price of coal had its largest positive impact on the income of men because mining mostly employs males. Fertility data for the same period shows an increase in births in high-coal counties relative to non-coal counties during the coal price boom. Thus, children do indeed appear to be "normal."

"The Role of Lenders in the Home Price Boom." Richard J. Rosen, Federal Reserve Bank of Chicago Working Paper 2008-16, November 2008.

Home prices rose at a steady rate of approximately 1 percent annually from 1983 to 1996. After that, prices started to increase at the much faster pace of 2.8 percent from 1997 to 2001 and an even sharper 7.6 percent from 2001 to 2005. In this paper, Rosen examines the effect that competition among lenders had on this price boom.

The two main types of mortgage lenders are depository institutions (like banks) and mortgage brokers. Comparing home price data collected from the S&P/Case-Shiller Home Price Index, Rosen discovers that the rate of home price increases began to rise when the share of mortgages in an area were issued by banks instead of mortgage brokers. Rosen notes that this phenomenon might be explained by the nature of the institutions. Banks naturally have higher overhead than the mortgage brokers, but the banks can capitalize on their reputation and the fact that they often have pre-existing relationships with potential borrowers who hold other accounts with the bank (checking, saving, etc). Thus, banks can offer lower interest rates to these customers and increase their market share.

When national housing markets get hot, however, mortgage brokers chip away at the market share of the banks. The increase in mortgage securitization allows mortgage brokers to compete with banks because it allows them to make loans without raising much capital. Yet that is also true of banks. So, to compete in an environment of high rates of growth in housing prices, banks seem to become more risky in their lending compared to earlier periods. Between 2002 and 2005, for instance, Rosen notes that the average ratio of the loan amount to the borrower's income increased substantially. **RF**