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Book Reviews

Editor's Note: Guidelines for Selecting Books to Review

Occasionally, we receive questions regarding the selection of books reviewed in the *Journal of Economic Literature*. A statement of our guidelines for book selection might therefore be useful.

The general purpose of our book reviews is to help keep members of the American Economic Association informed of significant English-language publications in economics research. We also review significant books in related social sciences that might be of special interest to economists. On occasion, we review books that are written for the public at large if these books speak to issues that are of interest to economists. Finally, we review some reports or publications that have significant policy impact. Annotations are published for all books received. However, we receive many more books than we are able to review so choices must be made in selecting books for review.

We try to identify for review scholarly, well-researched books that embody serious and original research on a particular topic. We do not review textbooks. Other things being equal, we avoid volumes of collected papers such as festschriften and conference volumes. Often such volumes pose difficult problems for the reviewer who may find herself having to describe and evaluate many different contributions. Among such volumes, we prefer those on a single, well-defined theme that a typical reviewer may develop in his review.

We avoid volumes that collect previously published papers unless there is some material value added from bringing the papers together. Also, we refrain from reviewing second or revised editions unless the revisions of the original edition are really substantial.

Our policy is not to accept offers to review (and unsolicited reviews of) particular books. Coauthorship of reviews is not forbidden but it is unusual and we ask our invited reviewers to discuss with us first any changes in the authorship or assigned length of a review.

D Microeconomics

No Slack: The Financial Lives of Low-Income Americans. By Michael S. Barr. Washington, D.C.: Brookings Institution Press, 2012. Pp. ix, 294. $34.95. ISBN 978–0–8157–2233–5.
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No Slack: The Financial Lives of Low-Income Americans is a collection of articles based primarily on analyses of data from a survey of low and moderate-income consumers in the Detroit metropolitan area conducted in 2005 and 2006. The extensive scope of the data permits a thorough analysis of the financial behavior of low and moderate-income consumers across a broad set of financial services. Some of the articles are revisions of papers that appeared in other publications, and most were written with coauthors. The book is written to appeal to a broad audience that includes academics, practitioners, and policymakers.

The Chapters

The first chapter provides an introduction.

Chapters 2 and 3 examine use of transaction services and short-term credit by low and moderate-income consumers. Transaction services involve how income is received, checks are cashed, and bills are paid. Short-term credit includes mainstream products (credit cards and small closed-end loans, for example), alternative financial products (pawnshop, payday, tax refund anticipation loans), and related products (rent to own, layaway, and check overdrafts). The analyses compare use of different services by consumers with bank accounts (banked consumers) with that of consumers without bank accounts (unbanked consumers). Chapter 2 also examines saving behavior of banked and unbanked consumers.

An important contribution in chapter 3 is the estimation of annual expenditures for transaction services and short-term credit. The authors estimated actual use over a year based on the survey data. This approach differs from the usual approach of previous research of constructing a hypothetical annual cost of using a nonbank provider. The survey collected from respondents what services respondents used, the type of service provider, the frequency of use over a time interval, and the price they paid for the services. The time interval was chosen to facilitate accurate reporting and varied by type of service (a month for cashing checks and a year for refund anticipation loans, for example). Respondent reported prices were checked against prices charged by financial service providers in the area. The resulting survey based estimates of expenditures for transaction and credit services are far lower than estimates based on hypothetical costs. The findings corroborate evidence suggesting that consumers find ways of avoiding high price providers (Dunham 2001; Berry 2004). Unbanked consumers may cash paychecks for no fee at a supermarket or at the issuing bank rather than use a check casher, for example.

Government agencies have looked to payment cards (account-based debit, prepaid debit, and payroll cards) as a mechanism for delivering transaction services at a lower cost to the government and unbanked consumers. Chapter 4 reviews federal and state initiatives for delivering transaction services using payment cards and discusses the successes and limitations of these initiatives. The chapter also presents an empirical analysis to survey respondents' preferences for different payment card features. The preferences are derived from the respondents' choices of different hypothetical payment cards. The results may provide guidance for designing payment card products for the low and moderate income market segment.

Chapter 5 investigates the effect of geographic proximity of suppliers on bank account ownership. The findings indicate that close proximity to a bank was not related to greater bank account ownership. The findings also suggest that bank accounts and alternative financial products are substitutes but that alternative financial services are inferior substitutes, which are used less frequently as income rises.

Chapter 6 contains additional analysis of short-term credit use, focusing more narrowly than chapter 2 on alternative credit and related products. Both users and nonusers of alternative products often experienced financial difficulties in the past year, but users were more likely than nonusers to have experienced difficulties. Notable is that users of these alternative credit and related products were not the least educated consumers (most had more than a high school diploma). Users were active borrowers, and those users with credit cards often revolved card balances and missed card payments. Nearly half applied for credit from mainstream lenders in the previous three years and were turned down. Thus, it would seem that users of alternative products lacked mainstream choices, not basic financial ability. The analysis does not provide much insight on the extent to which the difficulties that led consumers to use alternative products was the result of intended risk bearing, self-control problems, or just bad luck.

Chapter 7 looks at home ownership and mortgage borrowing among low and moderate income consumers. Much of the discussion concerns differences in mortgage outcomes by borrower race and mortgage origination channel. The discussion of reasons for the observed differences is speculative due to an inability to account for effects of omitted variables and joint causation of loan terms (see Yezer 2010) using the survey data.

Many low and moderate consumers owe debts and have little discretionary income or liquid assets. When adverse events occur, these consumers often experience financial difficulties. Bankruptcy is one way to obtain relief from financial difficulties. Chapter 8 provides evidence suggesting that many more consumers might benefit from bankruptcy than actually file for it. Both those who might benefit from bankruptcy and those who would not frequently experienced adverse events. The findings in this chapter further suggest that neither financial calculation nor adversity can fully explain bankruptcy-filing decisions.

Chapter 9 discusses low and moderate income consumers' use of tax withholding to save. Survey responses indicated that by far most consumers filing a tax return received refunds, which were about $2,000 on average. This outcome was probably intentional as over half of respondents indicated that they preferred to overwithhold and receive a refund. A considerable proportion of banked consumers and more than half of unbanked consumers obtained refund anticipation loans (RALs) to obtain funds from their refunds faster (at a relatively high cost of about $90 to obtain funds from a $2,000 refund ten to fourteen days sooner), usually because they wanted to pay their bills sooner. Regardless of whether they received a RAL or not, about half of consumers receiving a refund said that they saved at least some of their refund. That such a large share of consumers precommit to overwithhold despite having little or no slack in their monthly budget suggests that tax withholding is an important tool to enforce saving for many low and moderate income consumers.

Chapter 10 further explores the use of tax withholding to enforce saving. The authors argue that low and moderate income consumers' asset allocation choices between liquid and illiquid assets may help reveal self-control problems that make saving difficult. Consumers that hold mostly illiquid assets to prevent them from withdrawing savings may also overwithhold to enforce saving. Results of analysis indicated that consumers with mostly illiquid assets were more likely than other consumers to prefer to overwithhold. However, the impatience to spend that caused consumers with mostly illiquid assets to precommit apparently was not so strong that they immediately spent their tax refunds. These consumers were less likely than other consumers to obtain RALs to hasten receipt of refunds or spend all of their refunds once they received them. These findings suggest behavior that is purposive, even if it is not optimal behavior in conventional economic models.

Chapter 11 presents a program of regulatory reform based largely on hypotheses from behavioral economics. The chapter argues that consumers do not collect full information or carefully evaluate alternatives before making choices. Rather consumer decision making is influenced by cognitive limitations and biases and is prone to error. More options create complexity, which may cause consumers passively to choose a default option or postpone making a decision; inflexible mental accounting produces intertemporal choices, such as simultaneously keeping funds in a savings account and borrowing on a credit card (lending at low rates and borrowing at high rates), that may not be in consumers' interest); and cognitive limitations cause consumers to collect insufficient information, which they may not completely understand and process fully.

This chapter then proposes a *behaviorally informed* regulatory framework that considers whether market incentives of firms are aligned with the interest of consumers in reducing the effects of cognitive limitations. For example, many consumers do not understand basic financial mathematics. For savings accounts, financial firms' incentives for disclosure of interest rates are aligned with consumer interests: Financial firms have an incentive to disclose an effective rate, which reflects the compounding of interest. In contrast, for credit, incentives are not aligned: financial firms have an incentive to hide costs, such as disclosing an interest rate that does not reflect the reduction in principal on installment loans or charging separate dollar fees for some costs rather than including them in the interest rate. The case for regulation is stronger when incentives are not aligned. In such situations, the authors of this chapter argue for regulation that both changes rules and changes financial firms' incentives. Existing regulations provide examples of both. Truth in Lending, for instance, changed rules for credit products by defining how the interest rate is calculated and what costs are included and changed incentives by creating costly remedies for wrongful disclosure.

The last part of chapter 11 discusses how a behaviorally informed framework might apply to recent proposals for changing mortgage and credit card regulations. Some proposals would entail rules such as requiring default options, developing default options that depend on borrower circumstances, and providing disclosures that influence decisions in a preferred way. Other proposals would alter incentives by regulating some forms of lender or broker compensation or creating additional lender liability when nonstandard products are used.

Finally, chapter 12 briefly discusses regulatory initiatives since the financial crisis.

Assessment

Most low and moderate income consumers have some savings, own checking or savings accounts, borrow from mainstream financial institutions. However, many also use alternative financial service providers—such as check cashers, pawnshops, and payday lenders—at a high cost relative to the size of transactions. The use of alternative financial service providers has been attributed to a variety of factors including limited access to mainstream products, low asset holdings, low levels of discretionary income to service debt, impatience, lack of knowledge, and cognitive limitations. The empirical analyses in *No Slack* provide insights on the financial behavior of these consumers and are an important contribution. The analyses indicate that low and moderate income consumers are indeed vulnerable and their small resources limit their access to financial services and afford them little opportunity for financial improvement. However, the analyses also provide new evidence suggesting that many low and moderate income consumers' behavior is thoughtful and purposive—they are often able to limit their use of high cost financial services, are aware of the benefits of saving and the consequences of late payments, and find ways to save even when they have an inclination for current consumption, for example. Well-designed regulation may indeed help such consumers' financial decisions.

A few considerations may temper enthusiasm for the reform agenda proposed in the book. First, many of the policy recommendations in the book are based on cognitive errors and biases from the behavioral economics literature. These cognitive errors and biases often are not precisely defined, neither the antecedent conditions that elicit (or suppress) them nor the cognitive processes that produce them are well specified, and the empirical evidence of errors and biases in consumers' decisions is far from robust (Gigerenzer 1996). That the cognitive errors and biases from the behavioral literature exist is well established. That they seriously impair actual financial behavior of most consumers or that the recommended regulations would remedy them is not established, however. Several studies provide evidence suggesting that consumers—including users of alternative financial services—reasonably manage their finances (see Mann 2013, Bertrand and Morse 2011, Stango and Zinman 2011, Agarwal et al. 2006, and chapter 3 in this book, for example). Such evidence weakens the case for regulations that limit choices.

In addition, designing effective regulations is difficult. Both behaviorally informed default options or disclosures intended to influence consumers to make the right choice and substantive restrictions that limit choices require that regulators know the right choice. That right choice is not always obvious and may not be the same for different consumers. Moreover, the right choice may depend on unknowable future circumstances (Durkin 2008), such as a mortgage borrower's expected tenure or a credit card borrower's future payment pattern. A presumed advantage of disclosure regulations is that policymakers do not need to know the right choice. However, even disclosure regulations may cause harm when not informed (see Lacko and Pappalardo 2007, for example). At this time, the available empirical evidence is far too limited for policymakers to know the right financial choices for most consumers.

Finally, providing "reasonably priced" accounts is a challenge. Because of the limited resources of these consumers, the size of transactions tends to be small. Much of the cost of providing small loans or low balance accounts arises because the loan or account exists. As a consequence, small loans and low balance accounts are relatively costly to produce. For a for-profit firm to provide the product, interest or fees revenue must also be relatively high. This problem has been recognized for a long time (for example, see Robinson and Nugent 1935, and National Commission on Consumer Finance 1972). More recently, the Federal Deposit

Insurance Corporation's Small-Dollar Loan Pilot project found that the interest and fees on small-dollar loan products are not always sufficient to achieve robust short-term profitability (Burhouse, Miller, and Sampson 2009; Miller et al. 2010). Charitable and subsidized provision of such financial services are alternatives to the market, but these alternatives have not been sufficient in the past.

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E Macroeconomics and Monetary Economics

Japan's Great Stagnation: Forging Ahead, Falling Behind. By W. R. Garside. Cheltenham, U.K. and Northampton, Mass.: Elgar, 2012. Pp. viii, 219. $110.00. ISBN 978–0–85793–821–3.

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Japan's rapid economic growth from the 1950s to the 1970s once marveled the world. After the collapse of the asset prices boom in the early 1990s, the Japanese economy stopped growing. After more than twenty years, Japan still continues to stagnate. It is very important to understand why a once high-growth economy entered a long period of stagnation and seems unable to recover. When other advanced economies, including the United States and European countries, have been struggling to recover from the global economic crisis, which started with a collapse of asset prices boom similar to the one in Japan, understanding what happened to Japan and why Japan cannot recover is an urgent task.

This book, by W. R. Garside, is an attempt to do that. The book rejects approaches based on the "de-historicized economic rationality" (1) that point out some ex post misguided policies by the Japanese government that delayed Japan's adjustment to the changing global environment and prolonged its stagnation. Instead, the book advocates "an holistic approach" (2) that provides a nuanced view on how the political and economic institutions that worked so well in the rapid economic growth period evolved during the post-catch-up phase in the globalizing world and prevented (so far) Japan from restoring the growth.

The book starts out with a brief survey of the political economic system of Japan during the rapid economic growth period. The main idea is the "developmental state" proposed first by Chalmers Johnson, but the book widely surveys the literature. The book then describes how