

Discussion of
Can Human Capital Explain Income-based Disparities in
Financial Services

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Preamble

- ▶ **Starting point:** consumers in lower-income and high-minority areas experience worse outcomes along the quality dimension (Begley and Purnanandam 2021, JFE)
- ▶ **Relevance:** understanding demand and supply factors that influence the quality of financial services is important to guide policymakers
- ▶ **Objective:** analyze supply factors
 - ▶ financial firms' internal labor allocation
- ▶ **Results:**
 - ▶ Human capital is a major factor affecting the provision of financial services
 - ▶ Financial firms allocate worse-performing loan officers in lower income areas
 - ▶ **Conclusion:** internal labor allocation contributed to disparities of treatment across areas with different income levels

Discussion

- ▶ Empirical setting and endogeneity
- ▶ The role of mortgage loan officers
- ▶ Measuring quality of financial services

Comment 1: empirical setting

- Challenge: *'isolate variation in supply that is orthogonal to demand'*

$$\text{PerfMLO}_{izt} = \underbrace{\beta_1}_{>} \text{PerfMLO}_{izt-1} + \epsilon_{izt}$$

$$\text{FirmAllocMLO}_{izt} = \underbrace{\beta_2}_{>} \text{Income}_{zt} + \epsilon_{izt}$$

$$\text{FinServQual}_{ist} = \underbrace{\beta_3}_{>} \text{QualityMLO}_{ist} + \epsilon_{ist}$$

- Supply factors might still be function of the consumer demand
- For example, complexity of products or evaluation of borrower worthiness
- To evaluate the impact of supply factors, one should keep the demand factors fixed

Comment 2: role of mortgage loan officers?

- ▶ Job responsibility: best mortgage for a client and best lenders, then write an application for the client
- ▶ Getting a license that costs \approx \$600:
 - ▶ state-specific fee (30\$), federal fee (\$60), background check (\$46), test fee (\$110), credit report (\$15), 20-hour course (\$350)
- ▶ Intermediary (commission) or working directly for a lenders
- ▶ Can you distinguish between self-employed and employees?
 - ▶ Self-employed mortgage loan officers might be a better option for lower-income individuals
 - ▶ They maximize the probability for an individual to be granted a loan
 - ▶ Your empirical exercise might be capturing only part of the story (segmentation)

Comment 2: competition and incentives of MLO?

- ▶ License is not (too) expensive but it does create entry barriers
 - ▶ %35 of Americans have less than \$1,000 readily available
- ▶ Competition in the market for MLOs
 - ▶ More skilled MLOs get to choose their location
 - ▶ Less skilled MLOs have no choice
- ▶ Consistently, statistics show the move up variable has a very small average (≈ 0.006), while the move down variable is much larger (≈ 0.07)
- ▶ It could either be firms' allocation is close to optimal since the beginning or firms are forced to place less skilled MLOs in lower income areas
 - ▶ Different stories with different policy implications

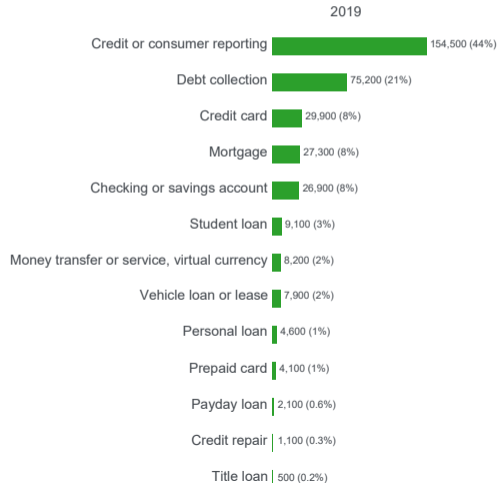
Comment 2: competition and incentives of MLOs

- ▶ Moreover, I would like to know more about the incentives scheme of MLOs
- ▶ Provision of lower quality services could be a symptoms of the wage structure
- ▶ Behr, Drexler, Gropp , and Guettler (2019) show that loan officers' main activities (loan prospecting, screening, and monitoring) are sensitive to the compensation structure
- ▶ Incentives might be differ across income areas. Do you have information about MLOs' contracts? Are they standard?
- ▶ Even if they are standards, MLOs' gains might be a function of the loan size: likely the average loan is larger in higher-income areas
- ▶ These are stories driven by labor market frictions and incentives rather than firms' endogenous internal labor allocation

Comments 3: measuring of quality financial services

- As in Begley and Purnanandam (2021), mortgage complains collected by the Consumer Financial Protection Bureau to capture quality of financial services

FIGURE 2: COMPLAINT VOLUME BY FINANCIAL PRODUCT OR SERVICE



Comments 3: Measuring the quality financial services

| Financial Product or Service | Closed with monetary relief | Closed with non-monetary relief | Closed with explanation | Administrative response | Company reviewing | Company did not provide a timely response |
|---|-----------------------------|---------------------------------|-------------------------|-------------------------|-------------------|---|
| All | 4% | 14% | 73% | 3% | 5% | 1% |
| Credit or consumer reporting | <1% | 20% | 69% | 3% | 7% | <1% |
| Debt collection | <1% | 10% | 81% | 1% | 3% | 4% |
| Credit card | 16% | 10% | 68% | 2% | 4% | <1% |
| Mortgage | 3% | 3% | 86% | 3% | 4% | 1% |
| Checking or savings account | 18% | 3% | 68% | 3% | 5% | 2% |
| Student loan | 2% | 7% | 85% | 1% | 2% | 3% |
| Money transfer or service, virtual currency | 9% | 6% | 76% | 2% | 4% | 2% |
| Vehicle loan or lease | 4% | 6% | 83% | <1% | 4% | 2% |
| Personal loan | 5% | 5% | 75% | 4% | 4% | 6% |
| Prepaid card | 17% | 3% | 68% | 1% | 8% | 2% |
| Payday loan | 1% | 1% | 83% | 5% | 3% | 7% |
| Credit repair | 11% | 6% | 68% | 2% | 6% | 8% |
| Title loan | 3% | 11% | 74% | 1% | 4% | 7% |

- ▶ 86% of complains are resolved with an explanation
- ▶ Does the result survive when using all complaints as measure of quality?

Final remarks

- ▶ Important topic, very cool data, and well-written paper
- ▶ The motivation and findings might be more connected: can we use your findings to guide policy interventions?
- ▶ It would be nice to narrow down the economic mechanism determining the labor allocation to learn about the source of the problem generating (or contributing) to disparities in quality of financial services

Thank You!

References

- ▶ Behr, P., Drexler, A., Gropp, R., & Guettler, A. (2020). Financial Incentives and Loan Officer Behavior: Multitasking and Allocation of Effort under an Incomplete Contract. *Journal of Financial and Quantitative Analysis*, 55(4), 1243-1267.