Discussion
Accounting for the Rise in Consumer Bankruptcy

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Recent Developments in Consumer Credit and Payment
2005
OUTLINE

1. Methodology
2. Model
3. Implementation
4. Findings
5. Summary
METHODOLOGY
Theory as a Measurement Tool

- Model Specification
- Model Calibration
- Counterfactuals
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MODEL
Key Elements

- Life-Cycle Model
- Uninsured Shocks to Earnings and Expenses
- Market For Consumer Loans With Option to Default
- Main Costs of Default:
  - Proportional Wage Garnishment ($\gamma$)
  - Fixed Psychic Cost ($\chi$)
- Competitive Risk-Based Pricing of Consumer Loans

$$q^b(d', z, j) = \frac{(1 - \theta(d', z, j))d'}{1 + r} + \frac{\theta(d', z, j)y}{1 + r}$$
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IMPLEMENTATION
A Concern

- **Model**: Garnishment Under Bankruptcy is 28%
  - **Data**: 0%
- Missing Important Costs of Bankruptcy
- Debtors Have Non-Exempt Assets
  - Net Liabilities = 0.7 < 9.0 = Gross Liabilities
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Findings

Insensitivity of Filings

- Insensitivity to $\uparrow$ Earnings and Expense Risks
- Insensitivity to $\downarrow$ Trans. Costs
- Why?
  - Borrower Response to Risk-Based Pricing
    \[ \phi = \int \theta(x, z, \eta, j) d \mu(x, z, \eta, j) \]
  - Large and Exogenous $\gamma$
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SUMMARY

- ↓ Trans. Costs and ↑ Risk Not Important For ↑ Filings

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