

Consumer Debt and Poverty: the Default Risk Gap

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RESUMEN

This paper examines the disparity in default risk between vulnerable and non-vulnerable populations in consumer lending. We merge an exhaustive registry of loans granted in the financial system with microdata on vulnerable individuals applying for social programs. We estimate the sources of this disparity and how loan and individual characteristics influence the probability of default. We find that vulnerable individuals have a higher risk than non-vulnerable individuals. However, this difference is reduced when individual debt characteristics, particularly the interest rate, are considered. Specifically, interest rates explain at least 30 percent of the risk gap. We also find that the default probabilities faced by lending firms are higher than those faced by banks, but we show that this effect is partly due to interest rate divergences. Our study underscores the importance of considering individual characteristics, loan characteristics, and interest rates when assessing default risk. While recognizing their limitations, these results suggest the need for policy interventions to promote financial inclusion, fair interest rate practices, and financial education, especially for vulnerable populations.

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