RESEARCH RAP

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DEBT COLLECTION AGENCIES AND THE SUPPLY OF CONSUMER CREDIT

The activities of third-party debt collectors affect millions of borrowers. However, relatively little is known about their impact on consumer credit. To study this issue, the author investigates whether state debt collection laws affect the ability of third-party debt collectors to recover delinquent debts and if this, in turn, affects the amount of credit being provided. This paper constructs, from state statutes and session laws, a state-level index of debt collection restrictions and uses changes in this index over time to estimate the impact of debt collection laws on revolving credit. Stricter debt collection regulations appear to reduce the number of third-party debt collectors and to lower recovery rates on delinquent credit card loans. This, in turn, leads to fewer openings of credit cards.

Working Paper 15–23. Supersedes Working Paper 13–38/R. Viktar Fedaseyeu, Bocconi University, Federal Reserve Bank of Philadelphia Visiting Scholar.

FORECLOSURE DELAY AND CONSUMER CREDIT PERFORMANCE

The deep housing market recession from 2008 through 2010 was characterized by a steep rise in the number of foreclosures and lengthening foreclosure timelines. The average length of time from the onset of delinquency through the end of the foreclosure process also expanded significantly, averaging up to three years in some states. Most individuals undergoing foreclosure were experiencing serious financial stress. However, the extended foreclosure timelines enabled mortgage defaulters to live in their homes without making mortgage payments until the end of the foreclosure process, thus providing temporary income and liquidity benefits from lower housing costs. This paper investigates the impact of extended foreclosure timelines on borrower performance with credit card debt. The authors' results indicate that a longer period of nonpayment of mortgage expenses results in higher cure rates on delinquent credit cards and reduced credit card balances. Foreclosure process delays may have mitigated the impact of the economic downturn on credit card default.

Working Paper 15–24. Supersedes Working Paper 14–8. Paul S. Calem, Federal Reserve Bank of Philadelphia; Julapa Jagtiani, Federal Reserve Bank of Philadelphia; William W. Lang, Federal Reserve Bank of Philadelphia.

VALUING "FREE" MEDIA ACROSS COUNTRIES IN GDP

"Free" consumer entertainment and information from the Internet, largely supported by advertising revenues, has had a major impact on consumer behavior. Some economists believe that measured gross domestic product (GDP) growth since 2000 is too low because it excludes online entertainment. Similar large effects on consumers occurred with the arrival of free radio and television entertainment. The authors provide an experimental methodology that uses previously established GDP measurement procedures to value advertising-supported entertainment around the world.

Working Paper 15–25. Leonard Nakamura, Federal Reserve Bank of Philadelphia; Rachel Soloveichik, U.S. Bureau of Economic Analysis.

THE IMPACT OF STUDENT LOAN DEBT ON SMALL BUSINESS FORMATION

Small businesses are the backbone of the U.S. economy and account for approximately one-half of the private-sector economy and 99% of all businesses. To start a small business, individuals need access to capital. Given the importance of an entrepreneur's personal debt capacity in financing a startup business, student loan debt, which is difficult to discharge via bankruptcy, can have lasting effects and may have an impact on the ability of future small business owners to raise capital. This study examines the impact of

the growth in student debt on net small business formation. The authors find a significant and economically meaningful negative correlation between changes in student loan debt and net business formation for the smallest group of small businesses, those employing one to four employees. This is important since these small businesses depend heavily on personal debt to finance new business formation. Based on the authors' model, an increase of one standard deviation in student debt reduced the number of businesses with one to four employees by 14% on average between 2000 and 2010. The effect on larger firm formation decreased with firm size, which the authors interpret to mean that these firms have greater access to outside capital.

Working Paper 15–26. Brent W. Ambrose, Pennsylvania State University, Federal Reserve Bank of Philadelphia; Larry Cordell, Federal Reserve Bank of Philadelphia; Shuwei Ma, Federal Reserve Bank of Philadelphia.

INTERACTIONS BETWEEN JOB SEARCH AND HOUSING DECISIONS: A STRUCTURAL ESTIMATION

In this paper, the authors investigate to what extent shocks in housing and financial markets account for wage and employment variations in a frictional labor market. To explain these interactions, the authors use a model of job search with accumulation of wealth as liquid funds and residential real estate, in which house prices are randomly persistent. First, the authors show that reservation wages and unemployment are increasing in total wealth. And, second, they show that reservation wages and unemployment are also responsive to the composition of wealth. Specifically, when house prices are expected to rise, holding a larger share of wealth as residential real estate tends to increase reservation wages, which deteriorates employment transitions and increases unemployment. The authors estimate their model structurally using National Longitudinal Survey of Youth data from 1978 to 2005, and they find that more relaxed house financing conditions, in particular lower down payment requirements, decrease employment rates by 5 percentage points in the short run and by 2 percentage points in the long run. The authors also find that worse labor market conditions immediately increase homeownership rates by up to 5 percentage points, whereas in the long run homeownership decreases by 8 percentage points.

Working Paper 15–27. Sílvio Rendon, Federal Reserve Bank of Philadelphia; Núria Quella-Isla, Barnard College, Columbia University.

THE IMPACT OF THE HOME VALUATION CODE OF CONDUCT ON APPRAISAL AND MORTGAGE OUTCOMES

The accuracy of appraisals came into scrutiny during the housing crisis, and a set of policies and regulations was adopted to address the conflict-of-interest issues in the appraisal practices. In response to an investigation by the New York State Attorney General's office, the Home Valuation Code of Conduct (HVCC) was agreed to by Fannie Mae, Freddie Mac, and the Federal Housing Finance Agency. Using unique data sets that contain both approved and non-approved mortgage applications, this study provides an empirical examination of the impact of the HVCC on appraisal and mortgage outcomes. The results suggest that the HVCC has led to a reduction in the probability of inflated valuations, although valuations remained inflated on average, and induced a significant increase in the incidence of low appraisals. The well-intentioned HVCC rule made it more difficult to obtain mortgages to purchase homes during the housing price crash, possibly exacerbating the fall in prices.

Working Paper 15–28. Supersedes Working Paper 14–23. Lei Ding, Federal Reserve Bank of Philadelphia; Leonard Nakamura, Federal Reserve Bank of Philadelphia.

DECLINING LABOR TURNOVER AND TURBULENCE

The purpose of this paper is to identify possible sources of the secular decline in the job separation rate over the past four decades. The author uses a simple labor matching model with two types of workers, experienced and inexperienced, where the former type faces a risk of skill loss during unemployment. When the skill loss occurs, the worker is required to restart his career and thus suffers a drop in his wage. The author shows that a higher risk of skill loss results in a lower separation rate. The key mechanism is that the experienced workers accept lower wages in exchange for keeping their jobs.

Working Paper 15–29. Supersedes Working Paper 11–44\R. Shigeru Fujita, Federal Reserve Bank of Philadelphia.