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Making Savers Winners: An Overview of Prize-Linked Saving Products

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Background: Low savings from existing programs

- Private saving rates are low (close to zero) for a large segment of the U.S. population
 - ✓ About half of US population claim they can't get access to \$2000 in 30 days
- Policy initiatives aimed at increasing household saving rates typically focus on:
 - ✓ Changing choice architecture of saving decisions
 - ✓ Providing financial incentives
 - ✓ Embedding savings in a social network

...while gaming activities remain very popular

- Wide spread demand for low-probability, high-prize gambling products
 - ✓ In 2008, 42 states and D.C. offered state lotteries, bringing in roughly \$60 billion in sales
 - ✓ In 2008, households spent \$540 per year on lottery products (compared to \$444 per year on alcohol)
 - ✓ Lotteries are particularly popular among low income households

Goal of the Chapter

- Explore an alternate policy option:

Prize-Linked Savings (PLS) Accounts

Outline:

- ✓ What are PLS?
- ✓ Why might they be a popular savings vehicle?
- ✓ Historical and current use
- ✓ Issues that could prevent PLS widespread use in U.S.

What Are Prize Linked Saving (PLS) Products?

- Combine a lottery feature with an otherwise standard saving product
- Instead of a guaranteed return, offer a stochastic return
 - ✓ Small chance of winning a large prize
- Unlike a lottery, participant retains ownership of principal
- Can be constructed with the expected return equal to a traditional savings vehicles
 - ✓ Makes the product cost effective for those offering the product

Why Might PLS Be Popular?

- For Savers
 - ✓ Individuals may have preference for skewed returns
 - ✓ 100% chance of \$1 \leftrightarrow 0.0001% of \$1 million
 - ✓ A chance to “win big”
 - ✓ Individuals may get utility from lottery play
 - ✓ Potential behavioral reasons as well
- For issuers
 - ✓ Ease of marketing and production
 - ✓ Possible low cost customer acquisition

Historical PLS Offerings

- 1694 “Million Adventure”
 - ✓ Bonds offered within the U.K. to finance the debt of the Nine Years War
 - ✓ Offered bond holders a guaranteed nominal coupon payment, ~6.15% annual return
 - ✓ Offered bond holders a 2.5% chance of winning larger prizes
 - ✓ Tens of thousands of investors
- Prior to 1896, similar programs were found in Germany, Austria, Spain, Greece, Italy, Sweden, and Switzerland (Levy-Ullman 1896).

Current PLS Programs: UK Premium Bonds

- Started in 1956 to encourage saving after WWII
 - ✓ “Savings with a Thrill!”
 - ✓ “[Premium bonds] will appeal to those who are not attracted by the rewards of interest, but do respond to the incentives of fortune”
- Instead of interest, bonds entered into monthly drawings
- Investors allocated a series of “lottery” numbers, one for each pound invested
- Currently, the top prize includes £1 million (as well as lower tier prizes)
- Prize pool equal to 1 month’s interest on all eligible bonds

Current PLS Programs: UK Premium Bonds

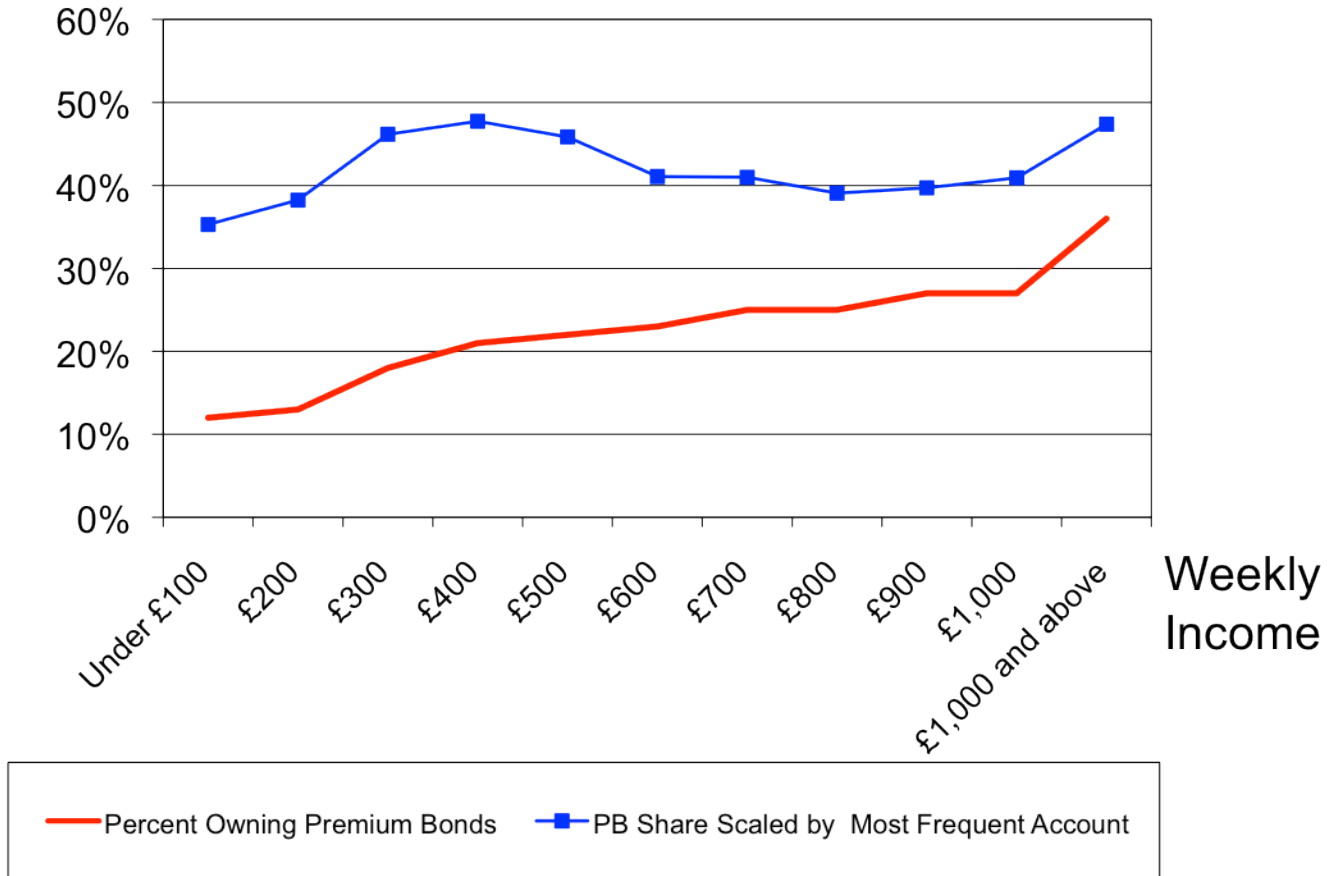
- Currently, 23 million premium bondholders
- The popularity soared in recent decades
 - ✓ From 4 billion pounds in 1994 to 40 billion pounds in 2008
 - ✓ Sales related to large prizes and prize rate: saving and gambling mixed

Table 2: Percent of Families holding Premium Bonds by Income Quintiles

Income Quintiles	All			With Accounts		
	All Families	Married	Single	All Families	Married	Single
1	8.8	21.1	6.6	10.4	22.8	8.0
2	13.2	24.3	10.6	14.4	25.1	11.9
3	18.1	24.4	10.6	19.0	25.1	11.5
4	23.4	26.9	13.0	24.0	27.4	13.9
5	31.1	36.3	19.4	31.7	37.0	20.0
<i>N</i>	33,182	16,005	17,177	30,992	15,464	15,528

Current PLS Programs: UK Premium Bonds

Premium Bond Ownership by Household Income



Current PLS Programs: South Africa's Million a Month Account (MaMA)

- MaMA : privately run PLS program by South Africa's First National Bank (FNB)
 - ✓ Monthly drawings
 - ✓ Prize structure with large prize of 1 million Rand.
 - ✓ Paid nominal interest rate as well
- MaMA accounts were successful in attracting new accounts and deposits
- But MaMA product was short-lived due to Court-ordered shutdown

PLS Programs exist all around the world

Country	Year Start	Total Balances (US\$)	Maximum Prize (US\$)
Brazil	2003	\$48.4 million	Car
United Arab Emirates	1995	n/a	\$272,000
Ireland	1956	\$701 million	\$187,000
Great Britain	1956	\$47 billion	\$1,790,000
Sweden	1918	\$5.7 billion	\$130,000
Pakistan	1972	\$2.8 billion	\$833,333
Pakistan	1993	\$780 million	\$190,000
Germany	1952	\$7.5 million	\$125,000
Turkey	1954	n/a	cash prizes
Kenya	1978	\$560,000	n/a
Indonesia	2002	\$152.6 million	\$10,900
Spain	1996	n/a	100 cars (2004)
Mexico	1996	\$178 million	Car (daily)
Argentina	1997	\$233 million	car
Argentina	1997	n/a	\$220,000
Denmark	1972	\$34 million	n/a
Oman	1992	\$280 million	\$54,000
New Zealand	1970	n/a	\$1,000,000
Sri Lanka	1997	n/a	\$20,000
India	1963	n/a	n/a

Recent PLS Demonstrations Within the U.S.

- Centra Credit Union Project in Indiana
 - ✓ Demonstrated substantial interest among (a) people with little savings; (b) people without a savings plan; (c) lottery players; and (d) optimistic people.
- “Save to Win” Demonstration in Michigan
 - ✓ Collaboration between 8 Credit Unions, MCUL, FRI, D2D, CFSI
 - ✓ Project results (11 months): 11,66 accounts opened; \$8.6 MM deposits
 - ✓ Survey findings (n=6,027 / 50%+):
 - Wealth: <\$5k in financial assets & savings: **28%**
 - Income: household income less than \$40K: **44%**
 - Less than \$20k: **16%**
 - Non-Savers: report not having a regular savings plan: **66%**
 - Gambling: spent on lottery in prior 6 mos: **59%**

Potential Impediments to Widespread Implementation in U.S.

- Legal Issues
 - ✓ Currently illegal in most states due to private lottery prohibitions
 - ✓ Also illegal for banks to have anything to do with any type of lotteries
 - ✓ ...except for credit unions in Michigan
- Political Economy Issues
 - ✓ May compete with state lotteries
 - ✓ Reduce revenues for the states

Summary

- PLS products are an intriguing way to encourage savings
- Despite a long international history, little US experience
- Need rigorous research to determine:
 - ✓ If these programs generate *new* savings
 - ✓ If so, what other spending they displace
 - ✓ Their impact on public finance and social welfare
- If promising, will require changes in laws