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Executive Summary

**Loan Fund Program to Restructure  
Excessive Debt among Families Living  
in Poverty**

**Safa Younes**



## About the Milken Innovation Center Fellows Program

The Milken Innovation Center Fellows Program accelerates Israel's economic growth through innovative, market-based solutions for long-term economic, social, and environmental challenges. Our goal is to accelerate Israel's transition from a Start-up Nation to a Global Nation with solutions that others can replicate.

The Program awards annual fellowships to outstanding Israeli graduate students. We train and deploy some of Israel's best and brightest young professionals to create pragmatic financing and economic policy solutions. Our applied research and Financial Innovations Labs® are a launching pad for transformative change, using innovative financing mechanisms, programs and policies to bridge social, regional, economic and productivity gaps within Israel and between Israel and the world.

In addition, Fellows craft their own projects during their internship aimed at barriers to job creation and capital formation in Israel. The Fellows' research, carried out under the guidance of an experienced academic and professional staff, support business and policy makers to shape economic reality in Israel. The program offers the ultimate training opportunity, combining real-life work experience with applied research.

Throughout the year, Fellows receive intensive training in economic and financial analysis, public policy and research methods. They acquire tools for communication and presentation, policy analysis, leadership and project management. The fellows participate in a weekly research training workshop where they work with senior economic and government professionals, business leaders, and top academic and financial practitioners from Israel and abroad. They also participate in an accredited MBA course, taught at the Hebrew University School of Business Administration by Prof. Glenn Yago.

Fellows Program alumni can be found in senior positions in the public and private sectors. Some serve in key positions in government ministries while others work at private-sector companies or go on to advanced graduates studies at leading universities in Israel, the United States and Great Britain.

The Fellows Program is a non-partisan. It is funded, in part, by the Milken Institute and other leading philanthropic organizations and individuals in the United States and Israel.

The State of Israel stands out among Western countries due to its high rate of poverty and social inequality. This reality has become more prominent over the years. A report of Israel's National Insurance Institute (2017) shows that in 2016, 19.1% of Israeli families live in poverty.

In 2015, the Ministry of Social Affairs and Social Services initiated the *Noshmim lervakha* program to improve the situation of families living in poverty and excluded from the normal financial sector. Through systematic and intensive intervention, the program provides families the tools they need to improve their financial situation. The program helps families understand their rights, find higher quality employment, improve household economic efficiency, increase the sense of competence in the individual and the family, create a community as a resource, and raise basic living conditions.

After two years, we can see evidence that the program has succeeded in helping families improve their situation, particularly in the areas of employment integration, raising income levels, and realizing rights. However, the data shows that families continue to face the most significant difficulties in addressing outstanding financial obligations. Large and growing household debt without the ability to reach an arrangement with the various creditors, hurts families' ability to improve their economic situation and leave the poverty cycle, even when the family income grows. People with debt suffer serious psychological, medical and familial effects, due to their financial obligations. The different effects are not separate from each other but intertwined and influence each another in a way that further weakens the family's position.

Economic exclusion plays a major role in this family debt phenomenon. One of the axes of social exclusion, economic exclusion occurs when an individual or family is denied access financial services such as a bank account, savings account, loans, etc., or that these services are provided at very high rates. Those who suffer from economic exclusion often include those who receive annuities from the state, low income families, and communities who have been marked by banks as problematic customers.

In the absence of access to cheap and available credit, those with limited resources may turn to "informal" or "gray" markets where excessive interest rates are paid for short-term loans. These loans often worsen their economic situation and increase poverty and exclusion.

### **Around the world, countries are deploying new policies to address excessive debt**

The problem of excessive debt is now recognized worldwide as a social problem that increases poverty and economic exclusion. In response, countries have deployed new policies with the following components:

#### **1. Improved credit accessibility for excluded populations**

To deal with the structural problems of having large debt, one of the key solutions is to provide alternatives to the expensive credit that exists today, which many people need to deal with exclusion and financial issues.

Examples include:

- a) Loans from financial non-profit organizations such as credit unions and community loan funds)
- b) Government loan funds

## 2. Building financial capabilities for people with excessive debt

Specific and temporary solutions to family poverty issues and financial obligations have not achieved much nor translated to into their financial stability. Because of this, the recommendation calls for a holistic approach that includes personal support and guidance, financial advice, budget assistance, savings encouragement, financial education, as well as access to affordable credit. Various interventions to assist with developing financial capabilities include the following:

- a) Debt counseling services (debt advice)
- b) Programs to promote financial literacy
  - a. Financial education
  - b. Financial advice and accompaniment
- c) Using the tools of behavioral economics to improve financial efficiency

## Recommendations

### 1. Steering committee recommendations

- Establish a loan fund as a component of *Noshmim Iervakha*

The purpose of the loan fund is to rescue families stuck in a vicious cycle where they cannot balance their budget to include debt repayment to various creditors. Families were often granted loans under bad conditions and are liable to make payments in arrears which have accrued interest and collection fees.
- Establish a debt-counseling service as a component of *Noshmim Iervakha*

It is also important to include debt-counseling that provides the following services: initial response to families on anything regarding their debt situation, building a plan to reduce the debt from the loan, negotiating to reach alternative agreements with creditors.
- Provide continual family economic and social support

It is important to continue to provide financial support to the family throughout the period of the loan to strengthen their financial abilities, encourage an atmosphere of savings, promote intelligent consumption and increase the family's resources, while continuing to support the family in other areas of family life.

- **Creating savings incentives**  
The proposed model combines savings incentives in the form of a grant that families will receive upon fulfillment of the loan terms. The amount will serve as a basis for incentives to create savings and as a future safety cushion for the family in the face of sudden lifetime events that require financial organization and access to credit.

## **2. Additional recommendations**

- **Using behavioral economics tools to increase the program's impact**  
It is recommended to design the program and the loan fund interventions, or nudges, based on insights from behavioral economics to help families circumvent behavioral biases, and promote informed financial decisions. Tools to consider include loan repayment reminders, reminders for important dates or meetings, sending meeting summaries to the family, and an easy and accessible loan application process. These interventions should be developed and evaluated through randomized trials.
- **Continued investment in program staff training and knowledge base on fostering families' economic ability**
- **Using a computerized system to streamline the family intervention process in all matters related to economic conduct and dealing of debts.**
- **Building a follow-up program for alumni to maintain the impact on families over time**

The loan fund solution described above provides a unique and winning combination of tools that will enable comprehensive financial inclusion for families living in various poverty cycles and without access to credit at good rates. The program combines credit accessibility and financial capability development through debt counseling and intensive, holistic accompaniment solutions, in addition to tools from behavioral economy to reduce the families' risk of making unfavorable financial decisions.



The Jerusalem Institute for Policy Research  
Milken Innovation Center  
20 Radak St. Jerusalem 9218604  
Office: 02-5630175 (Ext. 34)  
[www.milkeninnovationcenter.org](http://www.milkeninnovationcenter.org)