The Impact of Payment Plans on Feelings of Financial Constraint

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**Background**

- Consumers with limited liquidity have many options available for financing purchases.
- While there has been a recent proliferation of monthly installment plans, there is sparse research on how selection of these plans impacts psychology.
- We explore how paying in monthly installment affects perceptions of financial constraint compared to paying in a lump sum either upfront or at a later time. Three possibilities:
  1. Paying upfront could feel least constraining because it gets the payment over with.
  2. Deferring the payment could feel least constraining by maximizing available resources.
  3. Paying monthly could feel least constraining by allowing consumers to align their income with their expenses.

**Importance of Perceived Financial Constraint**

- Perceived financial constraint taxes cognitive capacity and shifts attention to focal financial issues.
- This can lead to negative financial outcomes, such as overborrowing.
- Limited research identifying antecedents of financial constraint.

**Design of Studies 1 - 3**

- We investigated three interest-free payment options using samples from Mechanical Turk: 1) Pay all upfront, 2) Pay in six equal monthly installments, and 3) Pay all in six months.
- **Study 1:** To test for financing preferences, participants read a scenario about the purchase of a couch and loveseat set, along with the three financing options above. They stated which plan they would prefer and which would cause them to feel the least financially constrained.
- **Study 2:** Using the same scenario, we randomly assigned participants to a payment option. We elicited perceived financial constraint and intended retirement contributions over six hypothetical months.
- **Study 3:** Same design as Study 2 with intended beverage purchases replacing retirement contributions.

**Design of Study 4**

- Texas A&M undergraduates participated in an eight-round lab study where they earned credits that could be used to purchase M&Ms or lottery tickets for an Amazon gift card.
- Some credits were used to pay a participation fee. Participants were randomly assigned to pay this fee upfront, pay in equal installments for six rounds, or defer the payment for six rounds.
- In each round we elicited perceived constraint and M&M purchases.

**Results**

**Study 1**

- **Preferred Plan**
- **Study 2**
  - **Perceived Financial Constraint**
  - Preregistered contrast of Monthly vs. (Upfront & Deferred), \( p = .04 \)

**Study 3**

- **Perceived Financial Constraint**
- Preregistered contrast of Monthly vs. (Upfront & Deferred), \( p = .002 \)

**Study 4**

- **Perceived Constraint**
- Preregistered contrast of Monthly vs. (Upfront & Deferred), \( p = .058 \)

**References**


**Conclusions**

- Consumers fail to predict the effect of monthly payment plans on perceived financial constraint.
- Paying in monthly installments leads to greater perceived financial constraint and fewer non-focal monetary outlays, relative to paying in a lump sum.
- Expectations may make consumers more likely to accept these plans, which could exacerbate problems of existing financial constraint.
- This research offers insights for banks or credit card companies that offer installment plans and are affected by the consumers’ subsequent financial decisions.