

Applied Economics Letters >

Volume 25, 2018 - [Issue 11](#)

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Financial literacy and use of payday loans in the United States




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Pages 781-784 | Published online: 13 Aug 2017

 Cite this article  <https://doi.org/10.1080/13504851.2017.1366635>

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ABSTRACT

Using the 2012 National Financial Capability Study, this study investigated the relationship between financial literacy and payday loan use. An instrumental variable approach was employed to address a possible endogeneity issue using a newly developed instrument of financial literacy based on the community network effect. Results from linear regressions indicated that financial literacy was associated negatively with the use of payday loans, and its effect was greater with the use of the instrument.

KEYWORDS:

Financial literacy

payday loans

national financial capability study

instrumental variable approach

JEL CLASSIFICATION:

Disclosure statement

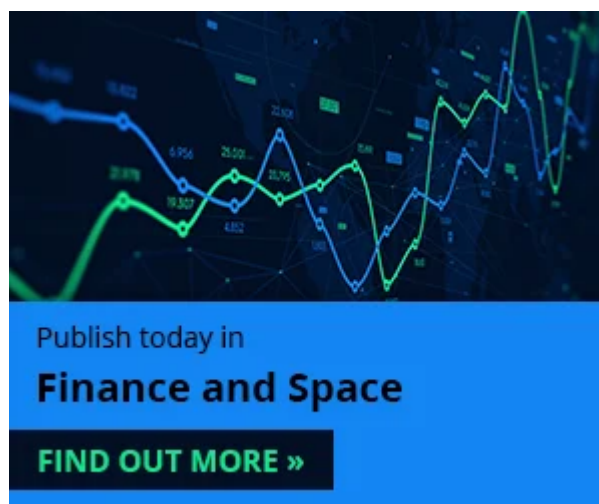
No potential conflict of interest was reported by the authors.

Notes

¹ With respect to financial literacy variables, we dropped cases where the respondent chose 'prefer not to say' as the answer to the objective financial knowledge questions and where the respondent answered 'prefer not to say' or 'don't know' to the subjective knowledge question. And all other 'prefer not to say' responses to the control variables are also excluded.

² Full results are available from the authors upon request.

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