CENTER FOR RESPONSIBLE LENDING

Payday Loans:
A Stepping Stone to Debt, Reduced Credit Options and Bankruptcy

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Industry arguments in support of payday lending hinge on **one** highly-flawed paper. Not only are there significant questions about the accuracy of that research, but it runs counter to the findings of many other studies.

Paige Marta Skiba (Vanderbilt) and Jeremy Tobacman (U. of Pennsylvania),
Do Payday Loans Cause Bankruptcy?
http://tinyurl.com/skiba-tobacman-BK

Using a database of 145,000 payday loan applicants from a large payday and pawn lender in Texas, Skiba and Tobacman compare payday borrowers with similarly situated applicants who were denied payday loans to determine whether this type of borrowing increases or decreases the likelihood of bankruptcy.

Those approved for a payday loan were 88% more likely to file for Chapter 13. Additionally, they were 14% more likely to file for Chapter 13 than their peers who had been denied a payday loan.

Brian T. Melzer, Ph.D. Candidate
University of Chicago Business School,
The Real Costs of Credit Access: Evidence from the Payday Lending Market
http://tinyurl.com/melzer-payday

Access to payday loans increases the chances a family will face a hardship, have difficulty paying bills, or have to delay medical care or prescription purchases.

Melzer's analysis found that 20% of families have difficulty paying bills, but that this will increase by 5% among families with access to payday loans. Also, while normally about 18% of households must postpone medical care, this jumps to 22.5%—a 25% increase—among households with access to payday loans.

University of North Carolina Center for Community Capital,
North Carolina Consumers After Payday Lending:
Attitudes and Experiences with Credit Options
http://tinyurl.com/nccob-after-payday

This study, commissioned by the North Carolina Commissioner of Banks, analyzed how low-income families fared after payday lenders left the state in 2006. The survey and focus groups asked a sample of low- to moderate income North Carolinians about their strategies in dealing with financial shortfalls.

Respondents noted that they use a variety of credit and non-credit options and strategies to deal with financial shortfalls, and were thus unaffected by the absence of a single financial product. Overall, households did not report missing payday lending and had a negative view of the product. Those who were former payday borrowers were glad they no longer had the temptation of what they viewed as an expensive product that was easy to get into, but hard to get out of.

Not only does other research beyond the oft-cited paper by Donald P. Morgan at the New York Federal Reserve counter the argument that the *absence* of payday loans cause bankruptcy, but additional research suggests that access to payday loans also increases the likelihood that borrowers will overdraft their bank accounts habitually, thus leading to the closing of their accounts, and will also increase the likelihood that they become seriously delinquent on their credit cards.

The only bottom line that payday lending helps is that of the payday lending industry. For borrowers, payday loans are a stepping stone to debt, reduced credit options and even bankruptcy.

Dennis Campbell, Asis Martinez Jerez and Peter Tufano, Harvard Business School,
Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures
http://www.bos.frb.org/economic/eprg/conferences/payments2008/campbell_jerez_tufano.pdf

The authors of this study shed light on the underlying causes of involuntary bank account closures, which usually result from an accountholder overdrawing their account too many times.

The concentration of payday lending stores in the accountholder's county is examined to see whether the presence of payday lending (a) increases the number of accounts banks closed due to overdrafts or (b) decreases account closures because payday lending credit presumably decreases overdraft incidents. **The authors find that payday lending is harmful to bank accountholders, increasing the chances they will overdraft.** Specifically, an increase in the number of payday lending locations in a particular county is associated with an 11 percent increase of involuntary bank account closures, even after accounting for county per capita income, poverty rate, educational attainment, and a host of other variables.

Sumit Agarwal (Federal Reserve of Chicago), Paige Marta Skiba (Vanderbilt Univeristy) and Jeremy Tobacman (U. of Pennsylvania),
Payday Loans and Credit Cards: New Liquidity and Credit Scoring Puzzles
http://bpp.wharton.upenn.edu/tobacman/papers/pdlcc.pdf

This research paper, again utilizing their database of payday borrowers from a large Texas payday and pawn lender in addition to credit card accounts and FICO and TeleTrack scores, has a number of critical findings on the impact of payday loans on borrowers with credit cards.

The authors found that taking out a payday loan makes a borrower 92% more likely to become seriously delinquent on their credit card (i.e., 90 days or more late) during the year. Overall, the seriously delinquent rate is 6%; for payday borrowers in this sample it is approximately 11.5%.

The authors also found that 2/3 of borrowers had access to at least $1,000 of available balance that could have been used. This suggests that payday loans' overwhelming availability and seemingly simplistic flat rate of $15 per $100 borrowed are successful in luring cash-strapped borrowers to their stores.