Lending to American Consumers

JULY 15, 2020
- July 8 | Mortgage & Foreclosure Issues
- July 15 | Lending to American Consumers
- July 29 | Consumer Credit & Data

July 15 | Lending to American Consumers
The National Conference of State Legislatures is the country’s most trusted bipartisan organization serving legislators and staff. We promote policy innovation, create opportunities for lawmakers to share knowledge and ensure state legislatures have a strong, cohesive voice in the federal system. We do this because we believe in the importance of the legislative institution and know when states are strong, our nation is strong.
COVID-19 WEB PAGE

Information on state policies and responses related to continuity of government, education, fiscal, elections, criminal justice and more.

Go to ncsl.org
- Consumer Financial Protection Bureau
- Online Lenders Alliance
- Pew Charitable Trusts
COVID-19: Lending to American Consumers

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Small-Dollar, Marketplace and Installment Lending Markets

National Conference of State Legislatures| July 15, 2020

This document was used in support of a live discussion. As such, it does not necessarily express the entirety of that discussion nor the relative emphasis of topics therein.
Material on COVID-19 and Other Resources

• Resources and tips for consumers
  https://www.consumerfinance.gov/coronavirus/

• Compliance and guidance information
  https://www.consumerfinance.gov/policy-compliance/guidance/
State Small-Dollar Loan Reforms

July 2020
Payday Lending Market

- 12 million users per year
- Average borrower pays $520 in fees per year to repeatedly borrow $375 in credit
- Typical loan takes 36% of borrower’s paycheck
- Typical borrower makes $30,000/year
- Borrowers must have checking account and lender can access it to collect
- Payday loans in 35 states; auto title loans in 24
Payday market is not price competitive

- How Borrowers Shop When in Financial Distress: speed, convenience, & certainty of approval
- Lenders typically charge maximum state allows
- Multi-state companies profitably charge 3-4x less when states require it to similar borrowers
The False Choice: 300%+ APRs or No Credit?
Colorado case study

2010: Eliminated the conventional, 2-week payday loan. Replaced it with a 6-month installment loan featuring:

1. Affordable payments (avg. 4% of paycheck, not 38%)
2. Amortizing loan with equal installment payments
3. Had lowest payday pricing in country
   - But still high: avg. APR 120% w/ interest and fees
   - Average loan of $389 repaid in 3 months – cost: $116

2018: Slight changes because of ballot initiative
Percentage of Colorado’s population that lived within 20 miles of a payday loan store:

- Before the law change: 93%
- After the law change: 91%

Stores were widely available after CO law change

Location open after law change (Aug. 1, 2013)
Location open before law change (April 1, 2010)

Percent of total population by county:
- <1
- 1-4
- 4-8
- 8-12
### Evidence-based approach used to ensure access to credit

<table>
<thead>
<tr>
<th></th>
<th>Avg. Payday Loan State</th>
<th>Colorado (2010 Reform)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost to borrow $500 for 5 months</td>
<td>$750</td>
<td>$239</td>
</tr>
<tr>
<td>Share of paycheck due for next loan payment</td>
<td>36%</td>
<td>4%</td>
</tr>
<tr>
<td>Typical APR</td>
<td>391%</td>
<td>120%</td>
</tr>
<tr>
<td>Credit widely available</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>
Ohio Fairness in Lending Act (2018)

Cost to borrow $400 for 3 months

**BEFORE**  
$400+

**AFTER**  
$109

Credit still widely available (approx. 175 locations)

Estimated cost savings of >$75 million per year
Virginia Reform Law (2020, takes effect Jan. 1)

Cost to borrow $500 for 4 months:

**BEFORE** $480  **AFTER** $138

Expands access to installment credit;
Lower-cost providers that previously avoided VA have stated intent to enter market
Ohio & Virginia

- Chose to maintain widespread access to credit
- Reformed payday lending statute
- Required affordable, amortizing installment payments
- Allowed interest between 28% and 36% plus a reasonable monthly fee, resulting in lower but still viable pricing
- Stopped evasion by closing loopholes, requiring online lenders to get licenses, making loans issued without a license void under state law, improving state enforcement powers
States Should Make it Easier for Banks & Credit Unions to Offer Small Installment Loans

• In states with payday & title lending, state-chartered banks and CUs are often prevented by state law from offering lower-cost installment loans

• Price where these loans are attractive to state-chartered banks & CUs is 6-8 times lower than average payday loan pricing

• States can protect consumers and expand access to affordable credit by setting parameters that work for banks, CUs, and borrowers
Americans Are in Favor of These Small Loans

$400 for a fee of $60 paid back over 3 months

80% Fair  18% Unfair

View of a bank that offers this loan

Percentage of respondents

70% More favorable
20% Less favorable
9% Don’t know, refused
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Note: Detailed summaries of all laws and regulations discussed are available upon request
Fintech in Non-prime in America – 100 Million Strong
Over 100 million Americans are underserved by traditional finance companies.
41% of America Has Non-Prime Credit Scores

FICO Score Distribution

- >800: 22.3%
- 750-799: 20.7%
- 700-749: 16.2%
- 650-699: 12.5%
- 600-649: 9.3%
- 550-599: 7.8%
- 500-549: 6.8%
- <500: 4.3%

41% of population have non-prime credit scores

Source: FICO
Credit Rejections are Common for Non-Prime Consumers

Credit Demand (by FICO)

- Less than 680
- Between 680 and 760
- More than 760

Source: Federal Reserve Bank of New York
Growth of Installment Loans over Single-Pay

Funded Loan Volume (online loans)

- **Installment**
- **Single-Pay**

Source: Clarity Services
Growth of Installment Loans over Single-Pay

Growth of Loan Products from 2018 to 2019

Source: Financial Health Network
Credit Demand and Credit Supply During COVID-19

COVID Impact: 2020 Credit Market for New Customers
(Index, Feb 23 = 100)

Source: Online Lenders Alliance
Net Debt During COVID-19

Respondents with more debt than savings
(calculated from open-ended responses)

Source: Center for the New Middle Class
CFPB's Consumer Complaint Database (March 15-July 13)

- Credit Reporting, credit repair services, or other personal consumer reports: 60%
- Debt Collection: 10%
- Credit card or prepaid card: 10%
- Checking or savings account: 5%
- Mortgage: 5%
- Money transfer, virtual currency, or money service: 5%
- Vehicle loan or lease: 5%
- Student loan: 5%
- Payday loan, title loan, or personal loan: 2%

Source: Consumer Financial Protection Bureau
“…[W]hile some forms of interest rate caps can indeed reduce lending rates and help to limit predatory practices by formal lenders, interest rate caps often have substantial unintended side-effects. These side-effects include increases in non-interest fees and commissions, reduced price transparency, lower credit supply and loan approval rates for small and risky borrowers, lower number of institutions and reduced branch density, as well as adverse impacts on bank profitability.”

World Bank, 2018
MLA’s Impact on Servicemembers

Active Service Members

The lack of access to credit is an area of personal finance that currently worries me the most

- 2014: 2%
- 2019: 4%

I am getting calls from collectors and struggle to pay my bills every month.

- 2014: 3%
- 2019: 8%

I struggle to pay my bills every month but have no debts in collection.

- 2014: 3%
- 2019: 9%

I sometimes miss a payment but have no debts in collection.

- 2014: 10%
- 2019: 14%

I am most worried about paying debts.

- 2014: 10%
- 2019: 20%

Source: Harris Polls
“We find virtually no statistically or economically significant evidence of any adverse effects of payday lending access on credit and labor outcomes. In a few cases, we find suggestive evidence of positive impacts of access. For example, our second strategy suggests that a 1 standard deviation increase in the fraction of time spent in a payday loan access state decreases the probability of being involuntarily separated from the Army by 10%.”

U.S. Military Academy, West Point, 2017
Laws and Regulation

States have accepted and acknowledge risk-based lending.

By doing so States have ensured that millions of Americans with less than perfect credit can pay bills and are not shut out of credit alternatives.

Source: Online Lenders Alliance
1. Servicemembers Civil Relief Act (1940)
2. Specially Designated Nationals List of the U.S. Department of Treasury Office of Foreign Asset Control (1950)
3. Truth-In-Lending Act (1968)
7. Internal Revenue Service Form 8300 (2012)
12. FTC Privacy Rule (2001)
13. USA Patriot Act (2001)
18. CFPB Small-Dollar Rule (2020)
Questions and Answers

Please type your questions into the chat box in the lower left-hand corner of your screen.

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