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Americans Want Payday Loan Reform, Support Lower-Cost Bank Loans

Results of a nationally representative survey of U.S. adults

The Pew Charitable Trusts

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Overview

Typical payday loans have unaffordable payments, unreasonable durations, and unnecessarily high costs: They carry annual percentage rates (APRs) of 300 to 500 percent and are due on the borrower's next payday (roughly two weeks later) in lump-sum payments that consume about a third of the average customer's paycheck, making them difficult to repay without borrowing again.

In June 2016, the Consumer Financial Protection Bureau (CFPB) proposed a rule to govern payday and auto title loans[1] that would establish a process for determining applicants' ability to repay a loan but would not limit loan size, payment amount, cost, or other terms. The CFPB solicited and is reviewing public comments on whether to include in its final rule alternatives to this process with stronger safeguards, particularly a "5 percent payment option" that would limit installment payments to 5 percent of monthly income, enabling banks and credit unions to issue loans at prices six times lower than those of payday lenders at scale. As such, it would be likely to win over many payday loan customers.[2]

An analysis by The Pew Charitable Trusts determined that the CFPB's proposal would accelerate a shift from lump-sum to installment lending but, without the 5 percent option, would shut banks and credit unions out of the market, missing an opportunity to save consumers billions of dollars a year.[3]

To gauge public opinion on various reforms, including the proposed rule, Pew surveyed 1,205 American adults and found:

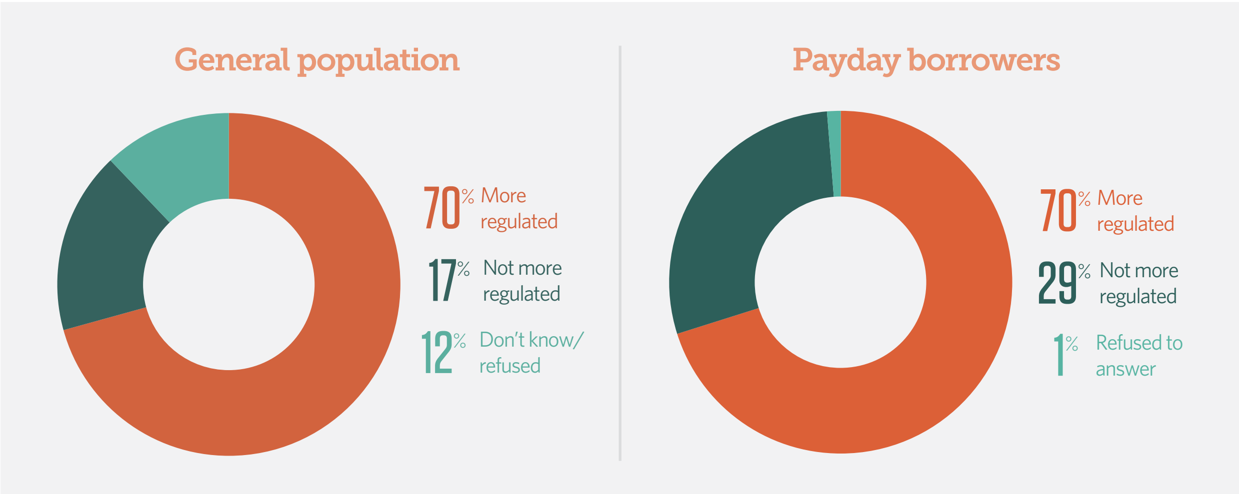
- 70 percent of respondents want more regulation of payday loans.
- 7 in 10 adults want banks to offer small loans to consumers with low credit scores, and the same proportion would view a bank more favorably if it offered a $400, three-month loan for a $60 fee (as reportedly planned).
- When evaluating a loan regulation's effectiveness, Americans focus on pricing rather than origination processes.
- Respondents say typical prices for payday installment loans that would probably be issued under the proposed rule are unfair.
- 80 percent dislike the proposal's likely outcome of 400 percent APR payday installment loans with more time to repay, but 86 percent say enabling banks and credit unions to offer lower-cost loans would be a success.

These results show that the public supports the CFPB's actions but strongly favors allowing banks and credit unions to offer lower-cost loans. A separate Pew survey of payday loan borrowers found similar sentiments.[4] This chartbook delves more deeply into these findings and discusses recommended changes to the proposal, including adoption of the 5 percent payment option, which is supported by Pew as well as many banks, community groups, and credit unions.

Figure 1

7 in 10 Americans, Borrowers Want Payday Loans to Be More Regulated

Percentage of respondents, by survey group



Notes: Respondents were read the following statement: "Now I'd like to ask you some questions about payday lending. Payday lenders are companies that generally operate through storefronts or the internet. They make small loans, often at high interest rates that are usually due back on the borrower's next payday." Then they were asked: "Which of these statements comes closer to your point of view? 1) Payday loans should be more regulated; 2) Payday loans should not be more regulated." Results are based on 1,205 interviews. General population numbers do not total 100 percent due to rounding. The payday borrower data are from a separate survey of payday loan borrowers that was conducted online, and "don't know" was not presented as an option, though respondents could decline to answer.

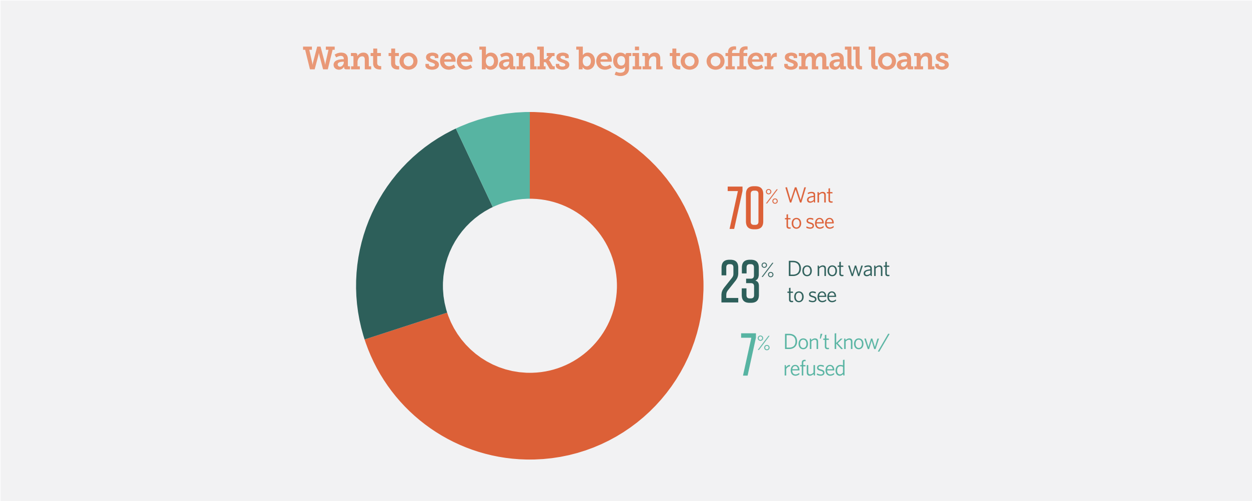
Source: The Pew Charitable Trusts, "Payday Loan Customers Want More Protections, Access to Lower-Cost Credit From Banks" (2017), www.pewtrusts.org/en/research-and-analysis/issue-briefs/2017/04/payday-loan-customers-want-more-protections-access-to-lower-cost-credit-from-banks

Roughly 12 million Americans use payday loans annually, spending an average of $520 on fees to repeatedly borrow $375.[5] Borrowers and the general population support more regulation of the small-loan industry in equal proportions.

Figure 2

7 in 10 Americans Want Banks to Offer Small Loans to Borrowers With Poor Credit

Percentage of respondents



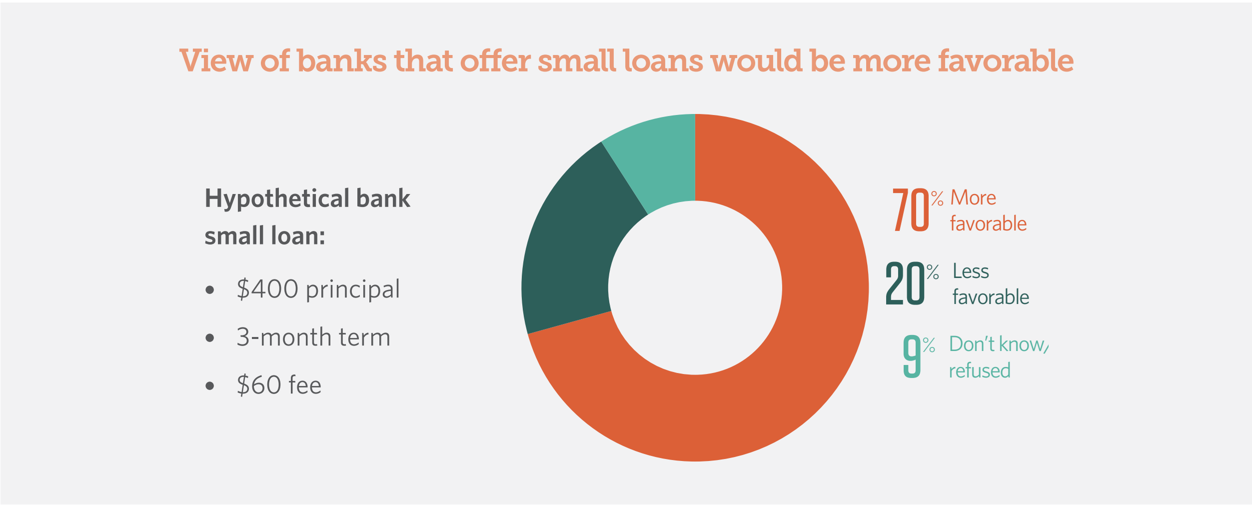
Notes: Respondents were asked: "Today, banks generally do not make loans to people with low credit scores. Do you want to see banks begin to offer small loans of a few hundred dollars to their customers who have low credit scores, or do you not want to see that?" Results are based on 1,205 interviews.

Banks generally cannot profitably make loans to people with low credit scores in the current regulatory environment. In May 2016, *American Banker* reported that at least three large banks were planning to use the 5 percent payment option that the CFPB proposed in its 2015 framework to offer such customers small loans repayable in affordable installments at prices roughly six times lower than average payday loans, such as a $400, three-month loan for a $60 fee.[6] Most Americans would like to see banks begin offering these loans.

Figure 3

70% of Americans Would View a Bank More Favorably if It Offered Lower-Cost Small Loans

Percentage of respondents



Notes: Respondents were asked: "Some banks are considering offering a $400, three-month loan with a $60 fee. Payday lenders charge about $350 for the same loan, while using a credit card would usually cost less than $60. If a bank began offering a $400, three-month loan for a $60 fee, would your view of that bank be more favorable or less favorable?" Results are based on 1,205 interviews. Numbers do not total 100 percent due to rounding.

Seventy percent of survey respondents said they would have a more favorable view of a bank if it offered a $400, three-month loan for a $60 fee (as some banks are planning to do).[7] Banks report that they would need to use the 5 percent payment option in order to make these loans available.

Figure 4

Americans Say Loans That Have More Time to Repay but Still Carry 400% APRs Would Be a Negative Outcome

Percentage of respondents in favor of each possible result

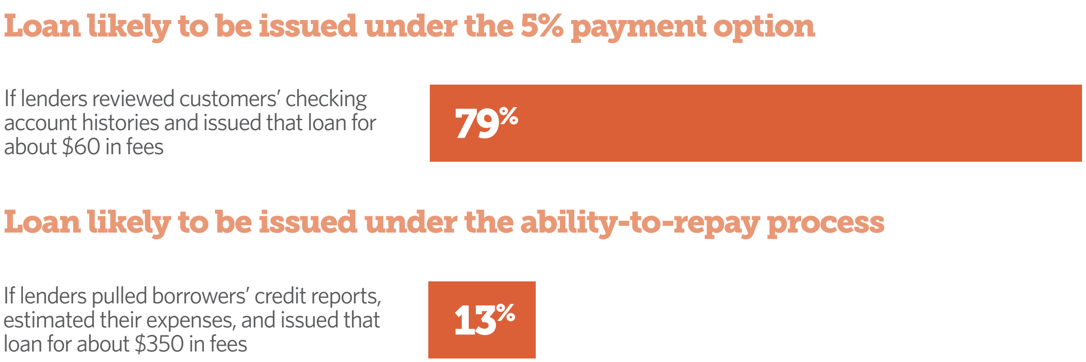
Notes: Respondents were read the following statement: "The government agency that regulates payday lending has proposed some new regulations. I'd like to get your opinion on some of the possible outcomes of the new regulations. For each, please tell me if you would view it as mostly a good outcome or mostly a bad outcome. a) If most people who use payday loans got more time to repay them, but the annual interest rates continued to be around 400 percent; b) If most people who use payday loans could get loans from their banks and credit unions that cost six times less than payday loans; c) If some payday lenders went out of business, but the remaining lenders charged less for loans." Results are based on 1,205 interviews. The order of these statements was randomized in the survey. Numbers do not total 100 percent because "don't know" and "refused" responses (indicated in gray) were omitted.

The most likely outcome of the CFPB's June 2016 draft rule would be to shift the market to longer-term payday installment loans. Similar loans today carry interest rates of around 400 percent, and prices would not be likely to decline under the proposal. Most Americans view that as a bad outcome. If the CFPB modified its proposed rule to include the 5 percent payment option it featured in the 2015 framework, banks and credit unions would be likely to offer lower-cost loans, creating a better alternative for borrowers. The public overwhelmingly said that would be a good result.

Figure 5

Americans Care More About Loan Prices Than Origination Processes

Share of respondents that favors each $400, three-month loan



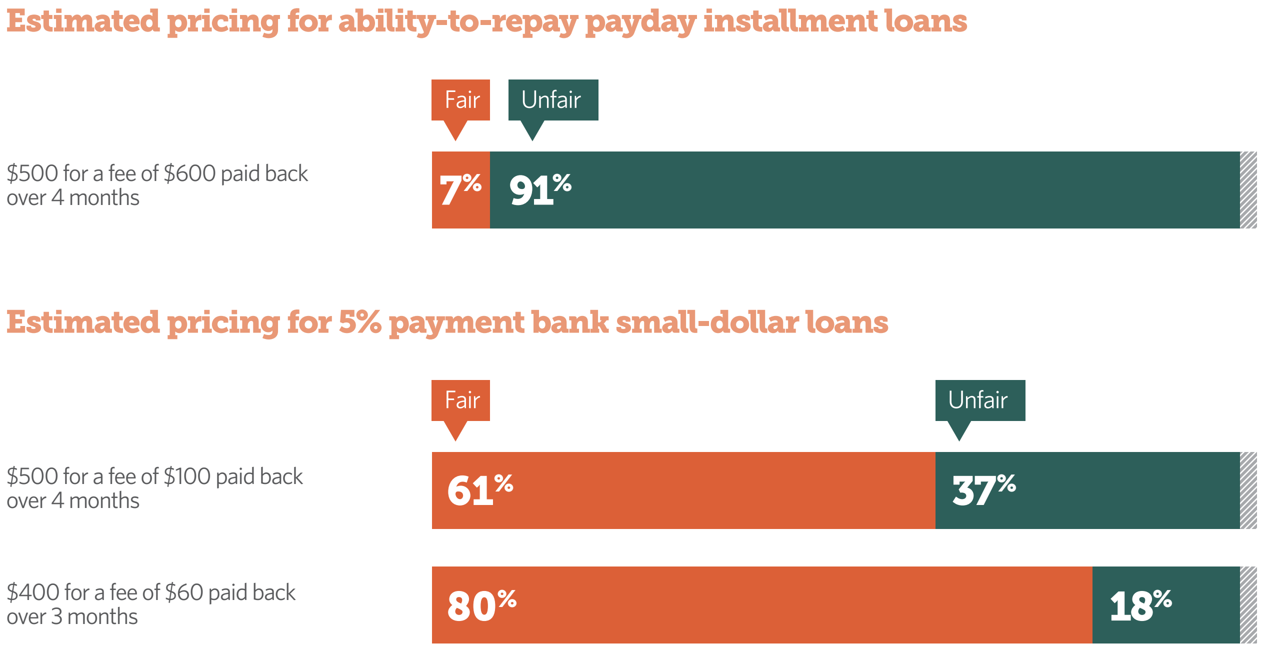
Notes: Respondents were read the following statement: "Here are two possible outcomes of the proposed regulations for payday lending. Please tell me which of the two you would view as a better outcome for a $400, three-month loan: If lenders pulled borrowers' credit reports, estimated their expenses, and issued that loan for about $350 in fees; If lenders reviewed customers' checking account histories and issued that loan for about $60 in fees." Results are based on 1,205 interviews. The order of these statements was randomized in the survey. Numbers shown do not total to 100 percent because "don't know" and "refused" responses were omitted.

The CFPB's proposed rule focuses on establishing the process that lenders must use to originate loans, allowing those willing to comply with those guidelines to charge high prices and preventing lower-cost providers, such as banks and credit unions, from offering lower-cost loans at scale. If banks are permitted to issue loans using borrowers' checking account histories instead of the bureau's proposed ability-to-repay process, their pricing for small-dollar loans would be roughly six times lower than that of typical payday lenders. By a margin of 6 to 1, Americans prefer the loans that would be available from banks and credit unions under the CFPB's earlier 5 percent payment option to those that payday lenders would issue under the proposed ability-to-repay provision.

Figure 6

Americans Say Payday Installment Loan Charges Are Unfair but That Planned Bank Small-Loan Prices Are Fair

Share of respondents, by loan type and terms



Notes: Respondents were read the following statement: "Here are some examples of small loans that might be available to people who have low credit scores. For each, please tell me whether you think the terms seem fair or unfair. (Insert item.) Do you think the terms seem fair or unfair? a) $500 for a fee of $100 paid back over 4 months, so a person who borrows $500 will pay back $600; b) $500 for a fee of $600 paid back over 4 months, so a person who borrows $500 will pay back $1,100; c) $400 for a fee of $60 paid back over 3 months, so a person who borrows $400 will pay back $460." Results are based on 1,205 interviews. The order of these statements was randomized in the survey. Numbers shown do not total 100 percent because "don't know" and "refused" responses (indicated in gray) were omitted.

Americans view current payday installment loans and those likely to be issued under the CFPB's proposed ability-to-repay provision as unfair, but they say the loans that banks and credit unions plan to offer under the 5 percent payment option would be fair. Banks and credit unions have said they cannot take on the paperwork, compliance, and regulatory risk of the ability-to-repay process but are interested in offering small credit at lower prices with stronger safeguards under the 5 percent option.

Figure 7

3 in 4 Americans Say It Would Be Good if Banks Offered Small Loans, Even With Higher APRs Than Credit Cards

Percentage of respondents that agree

Notes: Respondents were read the following statement: "Here are two views regarding small loans that banks might begin offering. Please tell me which of the two you agree with more. It would be a good thing if banks started offering small loans to their customers who use payday loans today because the prices would be six times lower than payday loans; It would be a bad thing if banks started offering small loans to their customers who use payday loans today because the interest rates would be higher than credit cards." Results are based on 1,205 interviews. The order of these statements was randomized in the survey. Numbers shown do not total 100 percent because "don't know" and "refused" responses were omitted.

By a margin of almost 5 to 1, respondents said it would be a good thing if banks began offering small loans at prices six times lower than those of payday lenders, even if the rates would be higher than those for credit cards. All payday loan borrowers have a checking account because it is a loan requirement, so if these loans became available, they would be likely to replace a large share of high-cost loans.

Methodology

On behalf of The Pew Charitable Trusts, Social Science Research Solutions conducted a nationally representative random-digit-dialing (RDD) telephone survey of 1,205 adults Aug. 12–21, 2016. The survey included an oversample of approximately 200 African-American and Latino respondents, which was weighted to match the demographic incidence of the RDD sample, producing an overall sample representative of the general population. The margin of error including the design effect is plus or minus 3.37 percent at the 95 percent confidence level. A detailed methodology is available at http://ssrs.com/omnibus.

Endnotes

1 Proposed rule, 81 Fed. Reg. 47864 (July 22, 2016), https://www.federalregister.gov/documents/2016/07/22/2016-13490/payday-vehicle-title-and-certain-high-cost-installment-loans. For a summary of the proposed rule, see The Pew Charitable Trusts, "How the CFPB Proposal Would Regulate Payday and Other Small Loans: A Summary of the Draft Rule" (2016), http://www.pewtrusts.org/en/research-and-analysis/analysis/2016/09/07/how-the-cfpb-proposal-would-regulate-payday-and-other-small-loans.

2 The Pew Charitable Trusts, "An Analysis of the Draft Rule: The CFPB's Proposed Payday Loan Regulations Would Leave Consumers Vulnerable" (2016), http://www.pewtrusts.org/en/research-and-analysis/analysis/2016/09/07/the-cfpbs-proposed-payday-loan-regulations-would-leave-consumers-vulnerable.

3 The Pew Charitable Trusts, "How CFPB Rules Can Encourage Banks and Credit Unions to Offer Lower-Cost Small Loans" (2016), http://www.pewtrusts.org/en/research-and-analysis/analysis/2016/04/05/how-cfpb-rules-can-encourage-banks-and-credit-unions-to-offer-lower-cost-small-loans.

4 The Pew Charitable Trusts, "Payday Loan Customers Want More Protections, Access to Lower-Cost Credit From Banks" (2017), www.pewtrusts.org/en/research-and-analysis/issue-briefs/2017/04/payday-loan-customers-want-more-protections-access-to-lower-cost-credit-from-banks.

5 The Pew Charitable Trusts, *Payday Lending in America: Policy Solutions* (October 2013), 12–16, http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2013/pewpaydaypolicysolutionsoct2013pdf.pdf.

6 Ian McKendry, "Banks' Secret Plan to Disrupt the Payday Loan Industry," *American Banker*, May 6, 2016, http://consumerbankers.com/cba-media-center/cba-news/banks-secret-plan-disrupt-payday-loan-industry; Consumer Financial Protection Bureau, *Small Business Advisory Review Panel for Potential Rulemakings for Payday, Vehicle Title, and Similar Loans: Outline of Proposals Under Consideration and Alternatives Considered* (March 26, 2015), http://files.consumerfinance.gov/f/201503_cfpb_outline-of-the-proposals-from-small-business-review-panel.pdf.

7 Ibid.

For further information, please visit:

pewtrusts.org/small-loans

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