THE PEW CHARITABLE TRUSTS

PAYDAY LENDING IN AMERICA:

Who Borrows, Where They Borrow, and Why

Executive Summary & Key Findings

This report series, *Payday Lending in America*, presents original research findings from the Pew Safe Small-Dollar Loans Research Project on how to create a safe and transparent marketplace for those who borrow small sums of money.

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Executive Summary

Payday loan borrowers spend approximately $7.4 billion[1] annually at 20,000 storefronts and hundreds of websites, plus additional sums at a growing number of banks. The loans are a highly controversial form of credit, as borrowers find fast relief but often struggle for months to repay obligations marketed as lasting only weeks.[2] While proponents argue that payday lending is a vital way to help underserved people solve temporary cash-flow problems, opponents claim that the practice preys on overburdened people with expensive debt that is usually impossible to retire on the borrower's next payday.

Many state officials have acted to curb payday lending. However, there has been little opportunity for federal policy on payday lending until now. Resolving the debate over the ways in which payday loans and lender practices may help or harm borrowers will fall to the Consumer Financial Protection Bureau (CFPB), which Congress recently created and charged with regulating payday lending. Other federal agencies, such as the Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), and Federal Trade Commission (FTC), also will have important roles to play as banks and online providers continue to enter the payday loan field.[3]

Existing data show that, in at least two significant respects, the payday lending market does not function as advertised. First, payday loans are sold as two-week credit products that provide fast cash, but borrowers actually are indebted for an average of five months per year. Second, despite its promise of "short-term" credit, the conventional payday loan business model requires heavy usage to be profitable—often, renewals by borrowers who are unable to repay upon their next payday. These discrepancies raise serious concerns about the current market's ability to provide clear information that enables consumers to make informed decisions.

This report, ***Who Borrows, Where They Borrow, and Why***, is the first in Pew's *Payday Lending in America* series. The findings provide policy makers with research to address concerns about small-dollar loans and to promote a safe and transparent marketplace. In addition to discussing Pew's focus groups, the report presents selected results from a first-ever nationally representative telephone survey of payday borrowers. The report answers six major questions: Who are borrowers, demographically? How many people are borrowing? How much do they spend? Why do they use payday loans? What other options do they have? And do state regulations reduce payday borrowing or simply drive borrowers online instead?

Key Findings

1 Who Uses Payday Loans? Twelve million American adults use payday loans annually. On average, a borrower takes out eight loans of $375 each per year and spends $520 on interest.

Pew's survey found 5.5 percent of adults nationwide have used a payday loan in the past five years, with three-quarters of borrowers using storefront lenders and almost one-quarter borrowing online. State regulatory data show that borrowers take out eight payday loans a year, spending about $520 on interest with an average loan size of $375. Overall, 12 million Americans used a storefront or online payday loan in 2010, the most recent year for which substantial data are available.

Most payday loan borrowers are white, female, and are 25 to 44 years old. However, after controlling for other characteristics, there are five groups that have higher odds of having used a payday loan: those without a four-year college degree; home renters; African Americans; those earning below $40,000 annually; and those who are separated or divorced. It is notable that, while lower income is associated with a higher likelihood of payday loan usage, other factors can be more predictive of payday borrowing than income. For example, low-income homeowners are less prone to usage than higher-income renters: 8 percent of renters earning $40,000 to $100,000 have used payday loans, compared with 6 percent of homeowners earning $15,000 up to $40,000.

2 Why Do Borrowers Use Payday Loans? Most borrowers use payday loans to cover ordinary living expenses over the course of months, not unexpected emergencies over the course of weeks. The average borrower is indebted about five months of the year.

Payday loans are often characterized as short-term solutions for unexpected expenses, like a car repair or emergency medical need. However, an average borrower uses eight loans lasting 18 days each, and thus has a payday loan out for five months of the year. Moreover, survey respondents from across the demographic spectrum clearly indicate that they are using the loans to deal with regular, ongoing living expenses. The first time people took out a payday loan:

- 69 percent used it to cover a recurring expense, such as utilities, credit card bills, rent or mortgage payments, or food;
- 16 percent dealt with an unexpected expense, such as a car repair or emergency medical expense.

3 What Would Borrowers Do Without Payday Loans? If faced with a cash shortfall and payday loans were unavailable, 81 percent of borrowers say they would cut back on expenses. Many also would delay paying some bills, rely on friends and family, or sell personal possessions.

When presented with a hypothetical situation in which payday loans were unavailable, storefront borrowers would utilize a variety of other options. Eighty-one percent of those who have used a storefront payday loan would cut back on expenses such as food and clothing. Majorities also would delay paying bills, borrow from family or friends, or sell or pawn possessions. The options selected the most often are those that do not involve a financial institution. Forty-four percent report they would take a loan from a bank or credit union, and even fewer would use a credit card (37 percent) or borrow from an employer (17 percent).

4 Does Payday Lending Regulation Affect Usage? In states that enact strong legal protections, the result is a large net decrease in payday loan usage; borrowers are not driven to seek payday loans online or from other sources.

In states with the most stringent regulations, 2.9 percent of adults report payday loan usage in the past five years (including storefronts, online, or other sources). By comparison, overall payday loan usage is 6.3 percent in more moderately regulated states and 6.6 percent in states with the least regulation. Further, payday borrowing from online lenders and other sources varies only slightly among states that have payday lending stores and those that have none. In states where there are no stores, just five out of every 100 would-be borrowers choose to borrow payday loans online or from alternative sources such as employers or banks, while 95 choose not to use them.

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