

Restrictive Annual Rate Cap on Payday Advances in Oregon Harms Consumers, Drives Borrowers to “Inferior Substitutes”

“Restricting Consumer Credit Access: Household Survey Evidence on Effects Around the Oregon Rate Cap,” by Dartmouth College Professor Jonathan Zinman finds that restricting access to payday loans “caused deterioration in the overall financial condition of Oregon households.”

The study surveyed 400 payday loan users in Oregon both before and after legislation was passed capping the annual interest rate on payday loans. Zinman found that the cap “dramatically reduced access to payday loans in Oregon,” and, as a result, borrowers turned to “inferior substitutes.” Respondents were also “significantly more likely to experience an adverse change in financial condition.” The results suggest that restricting access to payday loans harmed Oregon residents.

Read study at http://www.dartmouth.edu/~jzinman/Papers/Zinman_RestrictingAccess_oct08.pdf.

Noted in the study:

➤ **Annual percentage rate caps on payday loans restrict access to short-term credit**

The number of licensed payday lending outlets in Oregon fell from 346 in December 2006 [before the annual percentage rate cap] to 82 by September 2008.

“The five month results...suggest that the Oregon Cap reduced the supply of credit for payday borrowers, and that the financial condition of borrowers (as measured by employment status and subjective assessments) suffered as a result.”

“The proportion of Oregon respondents reporting that it was harder to get a short-term loan recently rose by 17 to 21 percentage points.”

➤ **Consumers turn to inferior, more costly credit options without access to payday loans**

“Former payday borrowers responded by shifting into incomplete and plausibly inferior substitutes.”

“Most substitution seems to occur through checking account overdrafts of various types and/or late bills. These alternative sources of liquidity can be quite costly in both direct terms (overdraft and late fees) and indirect terms (eventual loss of checking account, criminal charges, utility shutoff).”

➤ **Overdraft protection is the closest substitute to a payday loan**

“The closest substitute for a payday loan is arguably overdraft protection on a bank account.”

“Credit card cash advances and auto title loans are poor substitutes for payday loans...Fewer than 10% of borrowers reporters that a title loan or cash advance would be their second choice if they could not get a payday loan.”

➤ **Eliminating access to payday loans hurts consumers’ employment and financial status**

“Reducing payday loan access in Oregon hindered productive investments or consumption smoothing that facilitated job retention (or search).”

“The proportion of respondents saying their financial situation had been getting worse in the last 6 months increased by 6 to 8 percentage points in Oregon relative to Washington.”

