

The Impacts of Payday Loan use on the Financial Well-being of OASDI and SSI Beneficiaries

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MOTIVATION

Motivation

- ❖ This research contributes the mission of the Social Security Administration's interest in the adequacy of benefits, that is borrowing from alternative financial services such as payday loans and other alternative financial services (AFS) has short term (consumption smoothing) and long terms effects (financial security)
- ❖ Payday loan use by social security beneficiaries has been understudied.
- ❖ Payday loan use among the SSA beneficiaries can negatively affect their financial security in retirement by causing more financial hardship
- ❖ Carrel and Zinman (2014) indicate that expensive loan products such as payday loans are labeled "predatory" because lenders can use borrowers' income checks as collateral.
- ❖ Having steady income checks make SSA beneficiaries less risky and, therefore, more attractive borrowers

Payday Loan in Different States

**Permissive
States**

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Allow single-repayment loans with APRs of 391 percent or higher.

**Hybrid
States**

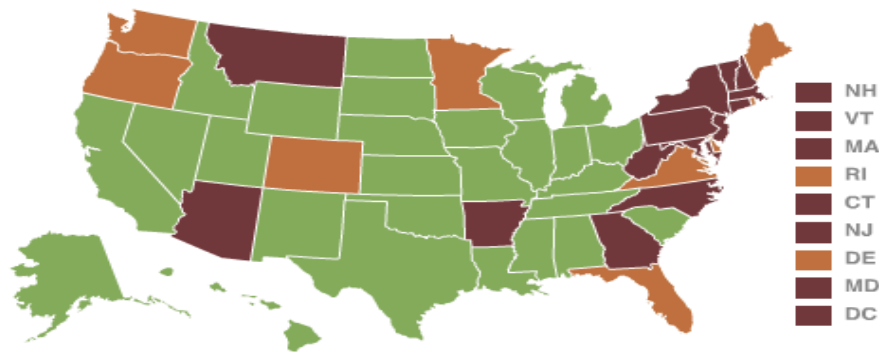
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Have payday loan storefronts, but maintain more exacting requirements, such as lower limits on fees or loan usage, or longer repayment periods.

**Restrictive
States**

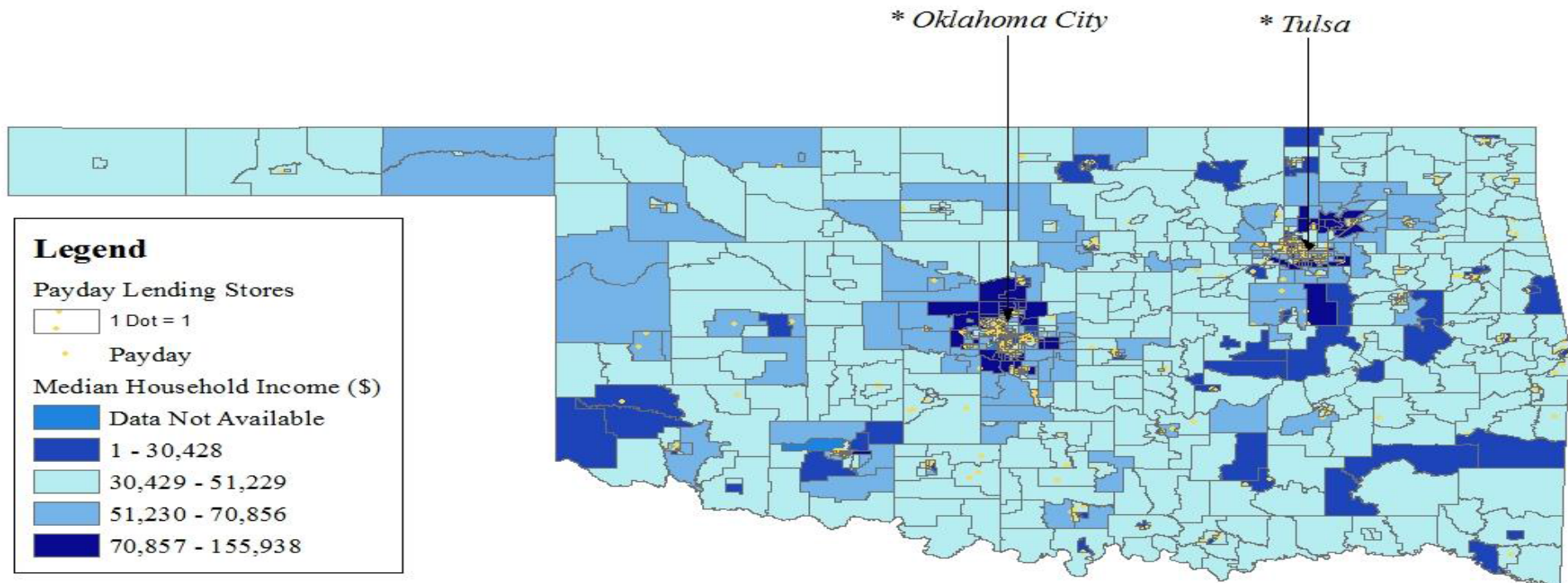
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Have no payday loan storefronts.



Sources: Pew Safe Small-Dollar Loans Research Project, 2012;
National Conference of State Legislatures, Sept. 12, 2013

Figure 1: Dispersion of Payday Lending Stores by Median Household Income and Census Tract



SIGNIFICANCE/CONTRIBUTION

Significance and Contribution

➤ What is a payday loan?

Payday loans are small, unsecured, short-term, easy to get, and high-cost credit products (Stegman, 2007). The annualized average interest rate on payday loans is approximately **390%** if a payday lender charges \$15 per \$100 borrowed for a two-week loan.

➤ How many Americans use payday loans?

Approximately **12 million** Americans use payday loans each year (PEW, 2014).

➤ How many Social Security (SS) recipients use payday loans?

Based on census data, our calculations show that approximately **1.8 million** SS recipients use payday loans each year.

Significance and Contribution, cont'd.

- The focus of this research is to investigate the predatory aspect of payday lending, focusing on older individuals, primarily social security recipients since consistency of a SS check in conjunction with being low-income make these individuals a prime target for payday lenders.
- Previous research focused on the impact of payday loans on certain demographics –minorities, low-income –, their consequences and access to other credit products.

LITERATURE REVIEW

Literature Review

➤ **Stegman (2007):**

- payday loan stores are located in:
 - higher-poverty neighborhoods
 - states that have more permissive regulations

➤ **Flannery et al. (2005):**

- more profitable for payday lenders to open storefronts in locations with a higher density of borrowers because a typical payday lending store is a small shop that employs 2-3 employees

➤ **Melzer (2011):**

- Access to payday loans increases financial hardship (difficulty in paying mortgage, rent and utility bills; experienced higher rate of foreclosures, evictions; and had to delay needed medical and dental cares)

➤ **Bhutta et al (2014):**

- a payday loan applicant's has impaired credit history but the actual effect of borrowing on credit scores was close to zero

Literature Review, cont.

- **Ellehausen (2008):**
 - about 90% payday loan borrowers have outstanding credit balances, almost no home equity to tap into, and have no credit left in their existing cards.
- **Fitzpatrick et. al (2014):**
 - find that payday loan borrowing helps some households to avoid food insecurity
- **Argawal et al (2009):**
 - suggest that payday loan borrowing reflects long-term liquidity loss from other sources e.g. credit cards
- **Bhutta et al (2016):**
 - Payday loans and other high-interest credit products are found more attractive due to the ease of approval, and that restricting access may make consumers worse off

RESEARCH QUESTIONS

Research Questions

- Are SS recipients more likely to use payday loans than non-SS recipients? (demand and supply issues)
- Do SS recipients use payday loans for different reasons compared to low-income non SS-recipients?
- Is there a variation in the demographics of payday users between SS and non-SS recipients?
- Are SS beneficiaries targeted more by the industry?

DATA AND METHODS

Data Sources

- We use nationally representative multiple data sources to carry out a comprehensive study
- CPS supplement 2009, 2010, 2011, 2013 and 2015
- PEW research reports and CFPB reports indicate that there is demand for payday loans
- Current Population Survey (CPS)
- Survey of Consumer Finances (SCF)
- National Financial Capability Study (NFCS)

Methods and Data

- We merged Annual Social and Economic Supplement (ASEC) of the Current Population Survey (March CPS) with CPS Unbanked & Underbanked Supplements
- SCF data provide information on financial literacy
- NFCS provide information on credit scores

- **Probit regression**

$$*payday_i = \alpha + \beta X_i + \delta SSrecipient_i + \theta ccards_i + \sigma deniedcredit_i + \varepsilon_i$$

$$reasonpayday_i = \alpha + \beta X_i + \delta SSrecipient_i + \varepsilon_i$$

- X_i – vector of controls (African-American, Hispanic, female, log annual income, no college education, old age)
- Full sample*
- SS recipients*
- SS as independent variable*

- **OLS regression**

$$*payday_freq_i = \alpha + \beta X_i + \delta SSrecipient_i + \theta ccards_i + \sigma deniedcredit_i + \varepsilon_i$$

$$payday_freq_i = \alpha + \beta X_i + \delta SSrecipient_i + \varepsilon_i$$

RESULTS

Findings

2010, 2013, 2016 SCF Data

VARIABLES	2016			2013			2010		
	(1) Full Sample	(2) SS Recipients	(3) SS IV	(4) Full Sample	(5) SS Recipients	(6) SS IV	(7) Full Sample	(8) SS Recipients	(9) SS IV
Older	0.02 (0.27)	0.20 (0.45)	0.09 (0.32)	-0.16 (0.31)	-0.48 (0.45)	-0.70** (0.35)	-0.26 (0.41)	-0.30 (0.55)	-0.27 (0.45)
African-American	0.09 (0.19)	-0.81 (0.74)	0.09 (0.19)	0.44** (0.22)	0.73 (0.68)	0.52** (0.22)	0.52** (0.24)		0.52** (0.24)
Hispanic	-0.37* (0.22)	-0.24 (0.58)	-0.38* (0.22)	0.49* (0.27)		0.58** (0.28)	0.14 (0.30)	-0.50 (0.61)	0.14 (0.30)
Female	0.63 (0.46)	2.18*** (0.79)	0.64 (0.45)	0.68 (0.45)		0.76* (0.45)	0.33 (0.47)		0.33 (0.47)
Log Annual Income	-0.07 (0.07)	0.46** (0.18)	-0.07 (0.07)	-0.30*** (0.10)	-0.57* (0.34)	-0.25** (0.10)	-0.09 (0.08)	0.12 (0.32)	-0.09 (0.08)
No College Degree	0.32* (0.18)	0.25 (0.42)	0.31* (0.18)	0.68*** (0.18)	0.93** (0.38)	0.74*** (0.18)	0.54*** (0.16)	0.89** (0.44)	0.54*** (0.16)
Social Assistance	0.45** (0.18)	0.67 (0.46)	0.45** (0.18)	-0.22 (0.39)	0.75 (0.65)	-0.32 (0.38)	0.32 (0.34)	-0.55 (0.68)	0.32 (0.34)
Denied Credit	0.73*** (0.15)	1.82*** (0.38)	0.73*** (0.15)	0.43** (0.17)	0.48 (0.43)	0.45*** (0.17)	0.51*** (0.17)	1.48*** (0.46)	0.51*** (0.17)
Credit Cards	-0.44*** (0.16)	-0.70* (0.36)	-0.44*** (0.16)	-0.48** (0.21)	-0.78 (0.56)	-0.51** (0.20)	-0.59*** (0.19)	-1.39** (0.63)	-0.59*** (0.19)
Social Security			-0.08 (0.21)			0.68*** (0.22)			0.01 (0.23)
Constant	-1.32 (0.85)	-7.67*** (2.20)	-1.25 (0.87)	1.29 (1.14)	4.68 (3.56)	0.61 (1.11)	-0.90 (0.94)	-3.42 (3.43)	-0.90 (0.95)
Observations	2,240	464	2,240	1,815	323	1,815	1,853	273	1,853

Robust standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1

Findings cont'd

2009 CPS Data

VARIABLES	(1) Demographics	(2) SS IV
Female	0.13 (0.14)	0.13 (0.14)
African-American	0.65*** (0.17)	0.65*** (0.17)
Family Income	-0.00* (0.00)	-0.00* (0.00)
Age	0.01* (0.00)	0.01 (0.00)
Social Security		0.05 (0.14)
Constant	3.63*** (0.28)	3.61*** (0.29)
Observations	3,637	3,637
R-squared	0.01	0.01

Standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1

Findings cont'd

➤ SCF Data:

- More likely to take out a payday loan if:
 - African-American*, Hispanic~, lack a college degree, have been denied credit, lack credit cards (2010~, 2013, 2016*)
 - Lower income (2013)
 - Hispanic, receive social assistance (2016)
- SS recipients more likely to take out a payday loan if:
 - Lack college degree, have been denied credit, lack credit cards (2010)
 - Younger, lower income, lack college degree (2013)
 - Female, have been denied credit, lack credit cards (2016)
- SS recipients more likely to use payday loans than non recipients (2010)
- No significant difference between why SS recipients vs. low-income non-SS recipients use pay day loans

Findings, cont'd.

- Little to no demographic variation between SS and non-SS recipients who use payday loans
- 2013 only year that showed SS recipients more likely to use payday loans – they are actually younger
- 2016 only year to show a relationship between receiving social assistance and payday loan borrowing
- One surprising result: higher-income SS recipients more likely to engage in payday loan borrowing

Findings, cont'd.

- the top three reasons cited by SS recipients for payday borrowing were
 - “emergency”,
 - “convenience”
 - and “only option”
- while “pay other bills/loans” was the third most cited reason among non-SS recipients .

Findings, cont'd.

- The NFCS data show that:
 - SS recipients with lower credit scores are more likely to take out payday loans
 - SS recipients with higher financial literacy less likely to take out a payday loan
 - SS recipients who also use pawnshops are more likely to borrow payday loans

CONCLUSIONS

Preliminary Results

- this study explicitly incorporates the variables that directly measure financial hardship, financial literacy, and the availability of alternative credit options, including alternative financial services into the analysis.
- Do payday lenders target SS recipients more?
- Our data sets do not allow us to directly address this question
- Based on the CPS data we observe that SS recipients are not using payday loans more intensely than the non SS-recipients
- Among SS-recipients lower income groups use payday loans more intensely

Thank you!

Questions?



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