

# **Comparing Payday Loans and Two Alternative Small Loan Products**

***Focus Group Two***

***By Jerry Buckland, PhD***

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# Outline

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# Introduction

- The second focus group, a component of the field research undertaken to examine consumer experiences with payday lending, was undertaken on 5 March 2016 in Winnipeg
- The purpose was to hear their thoughts regarding the strengths and weaknesses of the payday loan product available currently in Manitoba from a number of payday lenders as compared with two other small loan products found elsewhere, Vancity credit union's Fair and Fast loan, and the state of Colorado's (US) regulated payday loan.
- In addition to asking participants for their views about these products, they were asked about their use of payday loans, and if they had any other suggestions for improving payday loans.

# Methods

- This focus group meeting was a qualitative method that asked open-ended questions to a group of participants to learn their individual and group feedback about payday loans and alternatives
- As a researcher I strive to identify my assumptions, biases, and position because the purpose was to hear, understand, and amplify the voice of vulnerable payday loan consumers and to understand their experiences with payday loans

# Methods

- The sample of participants was selected with the assistance of a local nonprofit organization that recruited from past and present clients and some of their (clients') contacts.
- The group included nine participants, from diverse socio-economic backgrounds, who currently or in the recent past use/used payday loans.
- The focus group discussion lasted 2.5 hours.

# Methods

- The session began with a brief conversation about the participants' use of payday loans .
- A presentation followed that explained how annual percentage rate (APR) is a measurement that allows for comparison of different credit products.
- Then three models were presented –the Manitoba payday loan and the two other small loan products– and participants were asked to identify the strengths and weaknesses of each product, in addition to their overall preference.

# The Participants

- Participants were aged from 25 to 67 years old, with half of the participants between the ages of 25 and 45 and the remaining four in their 60s (Table 1).
- The majority of participants were women. Seven of the nine participants have children under the age of eighteen living with them.
- Half the participants are single while the other half are married or common-law.
- Nearly half of the participants are unemployed, while two are retired, two work full-time and one is a seasonal worker.
- Annual household incomes ranged from \$11,600 to \$45,000. One participant did not provide their annual household income.

# The Participants

Age (years)	Marital Status	No. of Children <18 yrs. old in Household	Annual Household Income (\$)	Employment Status
25	Single	4	-	Full-time
29	Single	1	30,000	Full-time
32	Single	1	17,500	Unemployed
36	Married	5	25,000	Seasonal worker
44	Common-law	2	22,800	Unemployed
62	Married	0	11,600	Unemployed
66	Single	0	13,000	Unemployed
66	Married	2	45,000*	Retired
67	Married	2	45,000	Retired



# Results

- Assessment of payday loans
  - Frequency and period of use
  - Purpose of loans
  - Why payday loans?

# Results

- Assessment of alternatives
  - Interest rates
  - Repayment structure & duration
  - Loan size
  - Credit reporting

# Discussion

- Results suggest that using payday loans is a part of a strategy consistent with bounded rational behaviour
- This is a view promoted by behavioural economists that real people follow when they are subject to time and institutional constraints

# Discussion

- Several focus group participants explained that for them there were few alternative loan products.
- Some of them were unable to get credit from mainstream banks, due to bankruptcy, or a poor or no credit rating.
- For some of these participants, friends/family and pawn loans were one of the few options for these underbanked people.
- However, relationship-based loans and pawn loans are small as compared to payday loans. Also, pawn loans require depositing a household item with the pawnbroker.

# Discussion

- Some respondents noted that due to the high cost of repaying the loan they fell into a dependence on payday loans. Two participants who took out at least twelve payday loans per year struggled with addiction issues.
- They noted that the consequences of their personal and financial struggles were bankruptcy or accumulating unrepayable debt.
- For these participants, payday loans were not helping them, but were delaying their need to address personal and financial issues.
- Moreover, the accumulation of unrepayable debt added an additional challenge.

# Discussion

- One respondent explained that she had adequate savings to pay for bills, but preferred to use payday loans for some bills in order to keep her savings intact.
- This approach to using payday loans is consistent with ‘mental accounting,’ a term used in behavioural economics (Shefrin and Thaler 1988), associated with a bounded rational strategy undertaken by individuals facing constraints. Rather than seeing money as perfectly fungible, it is understood to fit in different categories, e.g., employment income, benefit income, emergency expense, gift expense.

# Discussion

- The principal purpose of the focus group was to explore participants' views about alternative financial products. Several respondents were quite interested in the Vancity loan because of its longer term and lower annualized interest rate.
- They felt that this loan would be easier to pay off because of the installment plan and the lower fees.

# Discussion

- Some participants preferred the short term one-time repayment for reasons described as ‘less worry’ and ‘pay it off and be ok for a little bit.’
- Other participants talked about ‘not trusting’ oneself with a larger or longer-term loan. For them, the small-sum and short-term loan offered them the discipline to limit their borrowing.
- Once again these strategies seem consistent with a bounded rational strategy in which people are making decisions with limited information, time, and self-control.
- For them there is a benefit to short-term, one-time repayment so that this product is worth the cost.



# Discussion

- Two types of payday users became apparent through the focus group conversation:
- Those who are able to use small loans from time-to-time, in a strategic fashion, and are able to repay them in a timely fashion, and
- The more vulnerable repeat borrowers who eventually become dependent on the loans.
- In this way, the ease of accessibility and the convenience of Manitoba's current payday loan system can help some borrowers and harm others. The credit-challenged payday loan users appeared to be the most vulnerable to potential risks and would benefit most from an alternative product.