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# Payday lending isn't helping the poor. Here's what might

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# Payday lending isn't helping the poor. Here's what might.

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A public interest lawyer [once explained](#) that “poverty creates an abrasive interface with society; the poor are always bumping into sharp legal things.” Indeed, the poor are also constantly bumping into sharp financial things. Without a financial cushion, every mistake, unexpected problem or minor life change can quickly turn into a financial disaster. [Half of the U.S. population has less than \\$500 in savings](#), living paycheck to paycheck and sometimes relying on payday lenders in a pinch. The reality is that people need short-term loans and we have to find a way to provide credit that is safe and accessible.

This month, the Consumer Financial Protection Bureau [proposed new rules](#) to blunt some of the sharpest edges of the payday industry. Up until now, regulating the shark-like behavior of these lenders has been a state-by-state endeavor, and looked a lot like a cat and mouse game. A state would ban payday lending, and the industry would shift to title loans. Or one state would cap interest rates, and the lenders would migrate to states with very high or no interest rate caps and lend back into that state. The CFPB rules could end all of that: this cat has federal jurisdiction and there aren't many places to hide from its reach.

This is why a lot of payday lenders claim that these rules will wipe out the entire industry, which offers an essential service to their clients who are better off with access to these loans.

This is not entirely true: These loans do not make customers *better off*. Many stay indebted for months or even years and most pay interest rates of between 300 to 2,000 percent. By the time they've paid off the loan, they are further in the hole than when they started.

But are these loans an *essential service* for poor borrowers? Yes. Most people assume that with some education and better money management, the poor would not need such ruinous loans. Thus, the argument goes, it's fine for a paternalistic state to forbid them to protect the borrowers from their own mistakes. But this view ignores the reality of poverty and all of its sharp edges.

These loans offer liquidity — a financial lifesaver — when those living on the financial edge bump against an unexpected problem. Most of us rely on loans to get by or to get ahead. The poor also need loans, but usually just to stay afloat. *So if we are going to regulate them away, the next step has to be providing an alternative.*

One option would be to persuade banks to do it — after all, they are the institutions primarily responsible for lending. However, they aren't interested and haven't been for decades — banks don't want to lend because they can make much more money with larger loans to wealthier borrowers. In fact, as I show in my book, [“How the Other Half Banks,”](#) payday lending is a fairly recent phenomenon that has ballooned to fill a void created by banks. Instead, after researching this industry and all the possible options, the one that seemed most promising was to create a public option in banking for the poor. A public option should not be seen as a “handout” to the poor, but merely a leveling of the playing field. The supply of credit has always been a public

policy issue, with banks functioning as intermediaries. When the middle class borrows to buy a house or go to college, these mortgage and student loans come with heavy government subsidies and guarantees — that's why they can have interest rates of less than 5 percent. These interest rates do not just reflect the borrower's financial capacity, but also the federal government's investment in these loans. These loans created the American middle class, which is why these subsidies have remained politically popular.

Insofar as the state enables credit markets, all creditworthy Americans deserve equal access to credit, especially because reasonable and safe credit can provide a smoother path both through and out of poverty.

How would a public option work? Postal banking. The post office was America's first institution, and it's not an overstatement to say that it helped create our robust democracy. Their services have always been available to all, regardless of income, location or race. And so, it is not unreasonable to suggest that as America's oldest instrument of democracy in action, the post office can create an equal credit market through a public option, and in the process, even save itself from imminent demise.

The basic idea of modern postal banking is that your local post office branch would offer a wide range of transaction services, including deposit-taking and small lending. Most of these transaction services are straightforward products. The post office can build on its existing network of employees and branches to meet a significant market demand at a much lower market price. Many of the low income have to pay up to 10 percent of their income for debit cards, check cashing and other services just so they can use their money.

Postal banking has operated in many Western countries since the 1800s and currently, 51 countries use postal banking as their primary method of financial inclusion — only 6 percent of postal carriers worldwide do not offer banking

services. It is estimated that postal banking [has banked over one billion people](#) worldwide. Postal savings accounts can even reinvigorate a culture of saving that has been long lost in the United States but retained in Japan and Germany precisely because of their strong postal banking network.