Post-Dispatch Prefers Broken Legs Over Court Dates!

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The editorial board for the *St. Louis Post-Dispatch* recently published a piece denouncing politicians who support payday loans . The editorial is filled with rhetoric, but doesn't contain much economic analysis or critique of the bill's actual provisions. I'd like to expand on the discussion here.

From the editorial:

> **The big losers** are the vulnerable Missourians who are being ripped off with impunity by payday lenders. Republicans have let the public down. Gov. Jay Nixon, a Democrat, hasn't been much help either.

The highly charged language of this paragraph ignores that payday loans are consensual agreements made by individuals. Payday loan customers are not forced to take these loans, but rather take them out voluntarily for any number of personal reasons.

People who apply for payday loans usually have a high risk of default, or need money immediately — otherwise, a bank would be willing and able to offer a longer-term loan at a much lower interest rate. When payday loan stores lend out money, they have to take into account the risk of that loan remaining unpaid. Because these loans are made to people who are less likely to pay them back, that higher risk is counterbalanced by a higher interest rate. If rates are lowered by force of law, many higher-risk borrowers will find themselves entirely without access to legitimate forms of credit.

(For those who read Show-Me Daily often, you know that payday loans have been a regular discussion topic for the past two years . The previous posts are well worth reading.)

The *Post-Dispatch* also includes an AP photo of a group of payday loan stores, which well illustrates the abundance of stores in the market. This image illustrates an important free-market principle: competition. The close proximity of the stores means that payday loan lenders need to compete for customers. If one store is charging a higher rate than warranted by customer risk factors, accounting for an individual's ability to pay back the loan, then another lender will be willing to undercut their competitor by offering that loan at a lower rate (an ongoing process, until the "market rate" is reached). Any worry about people being "ripped off" should be abated when one factors in the idea of marketplace competition: Each store sets rates to vie for customers while balancing the risk of repayment.

The *Post-Dispatch* ignores the fact that some people who really need loans cannot always get those loans from a bank, but that the necessity of the money immediately outweighs the longer-term potential cost of a payday loan. Setting any sort of regulations on payday loan operations means that some people will not be able to get loans legally. That does not mean they won't get loans at all, but they will have to use underground or black market means to obtain them. This puts high-risk borrowers in an even worse situation, because if someone can't pay back a payday loan or a bank loan, there are legal methods to handle the situation, like bankruptcy. If someone doesn't pay back a loan, on the other hand, the lender has little recourse other than black market violence.

Deciding to increase payday loan regulations amounts to misguided paternalism. People at the margin will still take out loans they cannot afford to pay back — but that will happen whether they get them from a payday lender or, as the present mortgage crisis has shown us, from a traditional bank. In an attempt to save consumers from themselves, such loan regulations push desperate borrowers to illegal sources. Payday loan rates should be left to market competition, not government officials.

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Advancing liberty with responsibility by promoting market solutions for Missouri public policy.

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