Traditional Installment Loans
Still the Safest and Most Affordable Small Dollar Credit

In addressing concerns the Consumer Financial Protection Bureau (CFPB) has regarding the structure and use of payday loans, CFPB Director Richard Cordray stated, "We want to make that consumers can get the credit they need without jeopardizing or undermining their finances."

Traditional Installment Loans are a Time-Tested Consumer Credit Product

- The loan is structured to be beneficial to the consumer with fixed terms, no prepayment penalties and is fully amortized to be repaid in manageable monthly installments of principal and interest.
- Traditional Installment Loans are a smart option for borrowers, offering them better rates and significantly higher levels of safety and affordability.
- Traditional installment lenders assess a borrower's ability to repay a loan by calculating a monthly net-income/expense budget to ensure that proposed installment payments can be met through the borrower's monthly cash flow.
- The product is designed to avoid a cycle of debt by scheduling regular, manageable payments of principal and interest, giving the borrower a clear roadmap out of debt.

Traditional Installment Loans Help Build Credit

- Traditional installment lenders report to credit bureaus, allowing borrowers to establish creditworthiness or to rehabilitate damaged credit.
- Traditional installment lenders work with borrowers who are late with payments and often work out terms to see the loan to completion.
- This in turn allows borrowers access to mainstream credit options, often at even lower interest rates.

Traditional Installment Loans Meet a Critical Need for Consumers

- According to the Center for Financial Services Innovation (CFSI), access to high-quality small-dollar credit is a key component of financial success for many Americans.[i]
- 15 million consumers used small-dollar credit products in 2012, including payday, pawn, auto title, nonbank installment or deposit advance loans, spending an estimated $41.2 billion on such products.[ii]
- Having the ability to borrow relatively small sums, on reasonable terms, can help individuals weather a financial shock, smooth income fluctuations, build a positive credit history, and facilitate a wealth-building purchase.
- However, millions of Americans do not have access to small-dollar credit or only have access to high-cost, low-quality small-dollar credit products that too often lead them into a cycle of repeat usage and mounting debt.

Suitability of Small-Dollar Credit Depends upon Borrower Need and Ability to Repay

- CFSI's research identifies four primary need cases in the small-dollar credit market:
    1. Unexpected Expense borrowers;
    2. Misaligned Cash Flow borrowers;
    3. Planned Purchase borrowers; and
    4. Exceeding Income borrowers.
- The distinct profiles of the first three need cases suggests that different types of products might meet those borrowers' needs.
- However, for Exceeding Income borrowers (one third of small-dollar credit users in 2012), access to credit might only worsen their financial situations. (CFSI)
- Lenders have a responsibility to use the best tools available to determine whether an applicant lacks the ability to repay, in which case the lender should not extend credit.

Affordability is More Important than the Price of Credit

- The "price" of small-dollar credit, as expressed in Annual Percentage Rates (APR) is often discussed as a primary determinant of quality.
- While affordable prices are certainly one aspect of high-quality small-dollar loans, what is "affordable" to any given borrower depends on many factors, including the loan size, repayment period, interest rate and fees, as well as the individual borrower's unique financial situation.
- CFSI defines an affordable small-dollar loan as one for which the loan amount, repayment period, interest rate and fees are such that the borrower can successfully repay the loan without re-borrowing and while still meeting basic needs and other financial obligations.

CFSI Compass Guide Principles Provide a Rubric for Success

- CFSI has developed its *Compass Guide to Small-Dollar Credit* as "a tool to help lenders improve the design and delivery of small-dollar credit products."
- The Compass Guide defines a high-quality small-dollar loan as one that:
    1. Is made with a high confidence in the borrower's ability to repay;
    2. Is structured to support repayment;
    3. Is priced to align profitability for the provider with success for the borrower;
    4. Creates opportunities for upward mobility and greater financial health;
    5. Has transparent marketing, communications, and disclosures;
    6. Is accessible and convenient; and
    7. Provides support and rights for borrowers.
- AFSA endorses the Compass Guide as a rubric for lenders who aim to meet the borrowing needs of financially underserved consumers.

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[i] *Compass Guide to Small-Dollar Credit.* Center for Financial Services Innovation, Feb. 2014.

[ii] According to CFSI's *Financially Underserved Market Size Study,* consumers spent an estimated $41.2 billion on small-dollar credit products in 2012; these include deposit advance, tax refund anticipation checks, pawn loans, payday loans, overdraft protection, secured and subprime credit cards, auto title loans, installment loans and rent-to-own.