Analysis of Payday Lending in Alabama

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February 3, 2014

Commissioned by the Alabama Asset Building Coalition

Table of Contents

Tables and Figures

Introduction

Payday lenders thrive in areas where low wages and underemployment are the norm. The fundamental character of their business model commodifies poverty as a means of profit. The concept of profiting from the economic hardships of working people is not new. Such practices, however, curtail the growth of any society, state, or nation. Indeed economic opportunity for all citizens is the hallmark of an advanced society. This opportunity is threatened by industries that prey on financially vulnerable residents. Payday lenders are one such industry. The application of usury-like interest rates eliminates a large amount of wealth that could otherwise occupy more productive capacities in the economy. Such practices do not benefit low-wage, high-poverty states such as Alabama. Payday lenders do not contribute to wealth-building among their customer base. This would in fact be antithetical to their existence. The existence of payday lenders is a sign of broader economic problems all of which are exacerbated by the lenders themselves. For this reason, policy-makers, concerned citizens, and researchers should invest in methods of helping residents develop assets.

The payday lending industry profits from the financial challenges experienced by working-class and poor citizens through a business model that encourages individual debt. Because payday lenders benefit from the economic challenges of residents, they have little incentive to offers products that will promote financial literacy or asset-building among their constituency. The type of indebtedness that payday lending engenders is empty in that it has no long-term financial benefit to the borrower. Paying off a payday loan does not help one's credit rating as with a credit card; it does not have the potential for future profits, such as a mortgage or small business loan; and it does not provide a means of getting to and from work, such as a car loan.

The debt structure engendered by payday lenders strikes poor and working-class individuals where they are most vulnerable - in their wages. Most payday lending operations require the customer to write a postdated check that includes the amount of the principle, interest, and fees. By definition, poor and working-class residents have few assets. Their primary human capital is defined by their job and paycheck, both of which represent their main opportunity to develop an asset base. When a considerable portion of this mechanism is compromised, it becomes very difficult for these residents to increase their asset base. This is unlike the debt structure of many wealthy or middle-income residents who, except for exceptional cases such as court ordered garnishments, have greater autonomy over how their payments are directed.

According to the Consumer Federation of America, payday lending is legal in 32 states.[1] With no national law prohibiting payday lenders from operating, states are free to determine the legality of such operations. The Safe Small Dollar Loans Research Project conducted by the Pew Charitable Trust carefully examined payday lending across the United States.[2] Findings revealed that an estimated 7% of Alabamians used a payday lender in 2012. This amounts to 258,793 recipients statewide. The same study estimates that after including interest and fees, the typical payday loan takes up approximately one third of a borrower's paycheck. It is therefore apparent that a substantial amount of financial resources among Alabama workers is being lost. Looking at the bigger picture, just how much money is being lost to payday lending in Alabama?

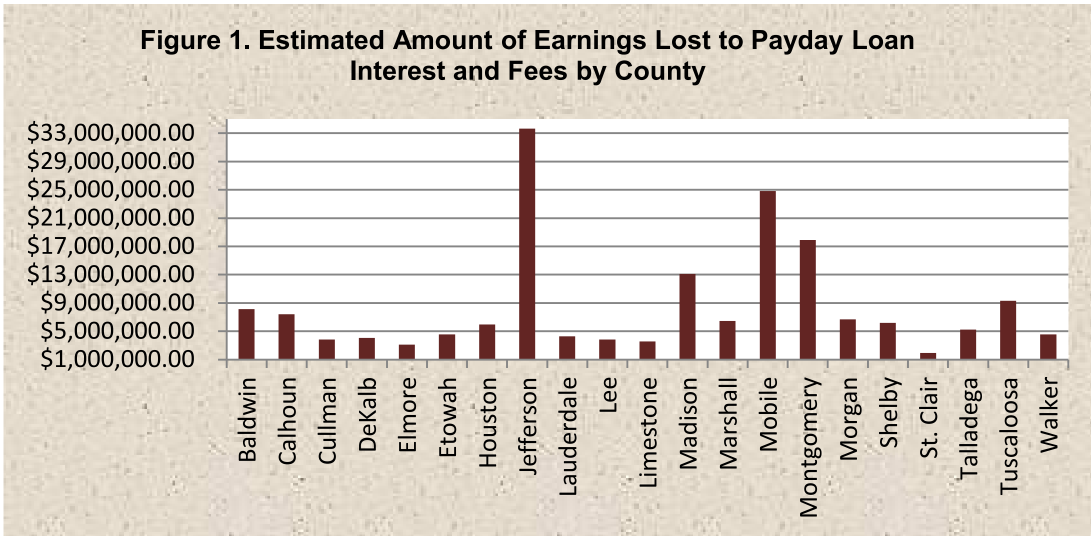


Figure 1: Workers in Alabama's largest county, Jefferson, lost nearly 33 million dollars in interest and fees in 2012 to payday lenders. Alabama's second largest county, Mobile, lost nearly 25 million dollars.

As of 2013, Alabama had 1049 licensed payday lending stores. Each store is licensed under the Deferred Presentment Services Act (DPSA).[3] Although the DPSA does not require stores to report financial accounts for the year, reasonable estimates can be calculated using established metrics. A recent study estimates that there are 19,700 payday lending stores in the United States collecting 4.7 billion dollars in revenue from interest and fees.[4] This averages to $238,578.68 in revenue per store. These data can be applied to this study. Given that revenue consists solely of interest and fees, we can estimate how much money Alabamians spend at payday lenders by multiplying average store revenue ($238,578.68) by the amount of stores in the state (1049). This equates to $250,269,035.30 lost annually to payday loan interest and fees. Analyses may also be conducted on the counties included in this study. For statistical accuracy only counties with over 50,000 residents were included. Combining the above metrics with 2012 Census data, Figure 1 reveals that working residents in each county lose millions of dollars in earnings annually to payday loan interest and fees.

In addition, Figure 2 goes further by examining the percent of total employment earnings lost to interest and fees. Aggregate employment earnings are the total amount of income that nonmilitary citizens receive from working. Several counties report noticeable amounts of work income lost. In most cases, the higher population of the larger counties will help balance this proportion. One exception is with Montgomery County. Montgomery County has the 4th highest population of residents above the age of 18. Nonetheless, its residents spend a comparatively high percentage (.50%) of their total employment earnings on payday loans. This suggests that a high percentage of Montgomery County residents earn low wages and that many of them are frequenting payday lending stores.

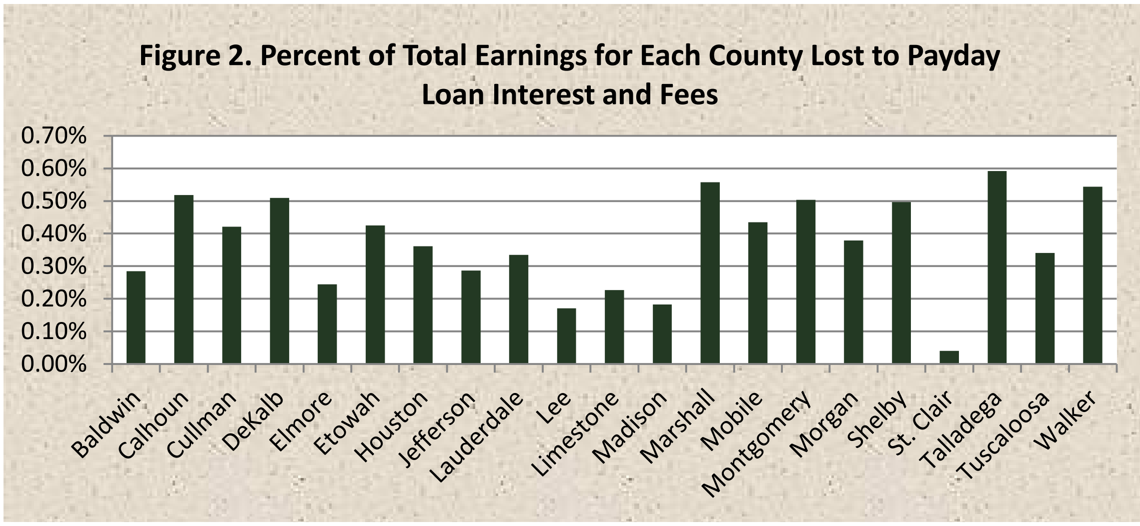


Figure 2: A considerable amount of earnings is lost to payday loan interest and fees

The first phase of this analysis explains why payday lending operations thrive in Alabama. From the demand side, it argues that economic growth is curtailed by policy that restricts opportunities for the average citizen. Economic opportunities in the United States are largely a function of education. Education provides citizens with skills that can be exchanged in the open market. Education also provides a foundation for innovation, which is also a catalyst for employment. Regions with vast amounts of poorly educated residents have trouble attracting high-paying industries. This has become especially salient in the digital age, where the market for unskilled labor is disappearing quickly.

State law limits the amount of loans that a payday lender can give within a certain period. The recipient may not receive more than two loans at one location until the day after he/she pays off the original debt. However, lenders circumvent this law by clustering stores close together as shown above. The clustering of stores in close proximity to each other allows them to exploit a weakness in the law. Patrons with outstanding loans at one store can simply go next door and take out another loan. The governor and other state officials have been working on a statewide database to monitor loan receipts; however, no substantive timeline has been arranged for its implementation.

Inadequate Investment in Education and Innovation: Demand Side

Alabama's low-wage environment is a product of its failure to invest in high quality education for all of its citizens. Alabama's total education expenditure per student has been below the national average for decades. In fact, Alabama's expenditure consistently ranks in the bottom five among states. Expenditure per student is a sound measure of future economic success because it reflects the willingness of a state to invest in the individuals who will determine innovation, job growth, and cultural progress. Simple correlation statistics reflect this relationship. We can look at expenditures from the 1969-1970, 1979-1980, and 1989-1990 school years. Students from these years would be in their late 20's to early 60's today which constitute prime earning years. We find that there is a strong relationship between state expenditure during these years and median household incomes today (Table 1).[5]

Table 1: Student Expenditure and Median Household Income	
Median Household Income 2012 and Expenditure per Student	Strength of Correlation
1989-1990	.71
1979-1980	.65
1969-1970	.70

Table 1: The correlation coefficients above define the relationship between median household income in 2012 and expenditure per student. The strength of the relationship is measured from 0-1 with 1 representing a perfect correlation.

Table 2: Median Household Income for 2012 in Comparison with Expenditure Per Student							
2012 Median Household Income (Mean 51,975)		**1989-1990 Expenditure per Student State Rank**		**1979-1980 Expenditure per Student State Rank**		**1969-1970 Expenditure per Student State Rank**	
Top Five		**Top Five**		**Top Five**		**Top Five**	
Maryland	**71,122**	D.C.	7,871.77	Alaska	4,267.07	New York	1,194.33
New Jersey	**69,667**	Alaska	7,577.33	New York	2,950.44	Alaska	1,059.17
Alaska	**67,712**	New Jersey	7,545.82	New Jersey	2,825.37	D.C.	946.89
Conn	**67,276**	Conn	7,462.78	D.C.	2,811.41	New Jersey	923.81
D.C.	**66,583**	New York	7,050.70	Delaware	2,586.71	Conn	910.76
Bottom Five		**Bottom Five**		**Bottom Five**		**Bottom Five**	
Kentucky	**41,724**	Arkansas	3,229.14	Idaho	1,548.28	Tennessee	530.87
Alabama	**41,574**	Alabama	3,143.70	Tennessee	1,523.24	Alabama	511.63
W. Virginia	**40,196**	Mississippi	2,933.57	Alabama	1,520.48	Arkansas	510.92
Arkansas	**40,112**	Idaho	2,920.89	Georgia	1,491.04	Kentucky	502.00
Mississippi	**37,095**	Utah	2,576.96	Arkansas	1,471.88	Mississippi	456.75

Table 2: Even when adjusting for cost of living, student expenditure appears to impact future earnings.

In fact, the states that had the highest expenditures per student in past years tend to have the highest median household incomes today (Table 2). It is no coincidence that Alabama ranks near the bottom in both categories. Statewide, Alabama has failed to improve its investment in education over time and today this negligence is reflected in the poor economic opportunities afforded to its citizens. Payday lenders thrive in such environments where underemployed residents consistently find themselves unable to meet the demands of a changing economy.

Students in underfunded school systems lack the human and material resources to cultivate future innovations while developing the type of skills that are critical for success in the digital age. Moreover, students must compete with a portion of the culture that derides scientific knowledge, the arts, and formal academics. Such sentiments are based on outdated principles that favor agrarianism, textiles, and heavy manufacturing. Not only are many students subjected to a climate that is anti-education, but also many of them frequently end up as collateral damage in the perpetual war between teacher unions and politicians.

The dearth of educational opportunities and investment in innovation impair Alabama's job market. Most Alabamians work in low-wage sales and service occupations. The median income for workers in these occupations in 2012 was $25,124 and $15,080 respectively, slightly lower than the national averages for the two. Significantly fewer Alabamians work in the "innovation" fields of engineering and architecture (2% employed) and computer and math technology (2% employed).[6] These digital age fields have some of the highest rates of income growth around the country as well as in Alabama, but more importantly, these fields tend to spawn other high paying occupations that attract educated individuals to the state.

The state has, however, made significant efforts to attract biotechnology companies to the area. Birmingham's presence in the burgeoning field of biotechnology is encouraging. One example is Biocryst's Discovery Center of Excellence which maintains a tenuous operation in Birmingham. Nonetheless, like so many digital age companies, its business model focuses on scientific and technological discovery. Few employees are required for this type of product development. In the post-industrial, digital age economy, products are brought to market via intellectual capital instead of vast amounts of labor. To exemplify, only a fraction of one percent of workers in Alabama were employed in science-oriented fields in 2012, which is in fact a decline from the amount in 2007.

Alabama's job problem is further revealed by examining the top five occupations for growth between 2007-2012 (Table 3). Alabama's leading job growth category in terms of median salary is the legal field. Most of the top jobs in this field including judges and lawyers require post-graduate degrees, other well paying jobs in the field such as paralegal or legal secretary still require an associate's or bachelor's degree. Only 1% of Alabamians are employed in legal occupations. Manufacturing or production related industries have the second highest percentage of median income growth between 2007-2012. Manufacturing provides many low-skilled or blue collar workers with the opportunity for wage stability and benefits. The income growth for this field is somewhat misleading because the median salary here is well below the national median. More importantly, manufacturing is an industry that has been in decline for the last 40 years. Because of that, manufacturing companies are hiring fewer workers. In Alabama, there was a 14.7% decline in the amount of workers employed in production or manufacturing occupations between 2007-2012.

Table 3. Top Five Occupations for Median Income Growth 2007-2012				
	2007 Median Income	2012 MHI Median Income	Percent Change in Median Income	Percent of Alabamians Employed in the Field
Legal Occupations	52,089	61,435	17.9	1
Manufacturing	26,286	30,706	16.8	8
Architecture and Engineering	60,599	70,677	16.6	2
Business and Finance	44,303	50,586	14.2	4
Food preparation and Serving	9,979	11,340	13.6	6

Table 3: Only a small percentage of Alabamians are employed in high-paying occupations where high rates of growth are expected. Alabama's low-wage environment fuels the payday lending industry.

Alabamians employed in business or finance related occupations tend to have decent salaries with good growth between 2007-2012; however, the substantial amount of residents employed in the food preparation and service industry report median incomes below the poverty line in 2012, even with 13.6% growth over a five-year period.

From the demand side, the dearth of high quality educational opportunities for all citizens in Alabama and the subsequent effect on employment explains why payday lenders have become an established facet of the economic landscape. Residents of Alabama are below the national average in all educational categories. As described earlier, digital age employment requires a high degree of skill development, a type of human capital that germinates on the elementary level and flourishes in high school and college. The effect of the low-wage environment becomes evident via responses given by research participants in the aforementioned Pew Payday Lending in America study.[7] Sixty-nine percent of participants report using payday loans to "cover a recurring expense, such as utilities, credit card bills, rent or mortgage payments, or food."[8] Cash shortfalls of this type become apparent when (A) cost of living outweighs wages and/or (B) when recipients live beyond their financial means. The former is a structural problem that must be addressed on the policy level. The latter must be addressed through education, financial literacy to be exact; especially given that when recipients were asked what they would have done without the payday loan, 81% of them reported that they would "cut back on expenses."[9]

In either case, payday lending does not appear to be a prudent financial option given that it weakens the source of most people's cash flow which is their pay check. Investments in education would go far in developing the foundation for innovation, jobs, and eventually a higher wage environment in Alabama. Education also exposes many to the nuances of finance essential in developing enduring assets.

Regressive Tax Rates and Limited Corporate Responsibility: Supply Side

Alabama's failure to invest in the development of human capital such as education suggests that it is not concerned with demand side orientations instead its comparatively low business tax rate, its reliance on income taxes for revenue, and its lenient regulations concerning payday lending suggest that it maintains a supply side approach to policy. This focus ultimately contributes to the presence and use of payday lending in Alabama.

For supply side economics to successfully contribute to economic growth, businesses - the "suppliers" of goods and services - must translate tax breaks and incentives into revenue that benefit the financial good of the entire state or society. This is not the case in Alabama. In the same year that the DSPA was passed setting the guidelines for legalized payday lending, the Alabama legislature enacted SB 225 allowing *non residents* who have investment interests in the state to apply state-granted capital income tax credits to their individual tax liability to the state.[10] Other incentives granted to businesses provide similar benefits, but require very little in return. For example, the Capital Investment Tax Credit provides significant tax relief to businesses that invest in the state; however, the minimum requirement for hiring residents is relatively low (50 new hires in most cases) and in qualifying cases, the business can receive the credit for up to *20 years.*[11] According to the Economic Development Partnership of Alabama (EDPA), "the capital credit can effectively eliminate the Alabama income tax liability generated by a qualifying project."[12] The Capital Investment Tax Credit and other similar benefits are, prima facie, genuine attempts to stimulate business growth in Alabama. However, these supply-side methods of generating economic development only work when (A) there is a highly-skilled work force in place (B) the area supports innovation, and (C) the area is welcoming to diverse cultures. Businesses simply move on to other tax-friendly states that meet more of the requirements for growth such as Georgia, Texas, or North Carolina.

The reality is that Alabama's supply-side methods have not been effective in procuring job growth. The W.P. Carey School of Business at Arizona State University maintains job growth numbers for each state. In terms of overall nonfarm job growth, Alabama ranks 49 with an estimated 2,800 jobs created from 2012-2013. That is .15% job growth. This is in comparison to the U.S. average of 1.70% job growth from 2012-2013.[13] Alabama's supply-side tactics alone do not attract businesses or better jobs for residents. They merely sustain a low-wage environment.

While Alabama policy-makers consider themselves pro business, they maintain a regressive tax structure where much of the onus for revenue collection is placed on average citizens. In fiscal year 2012, Alabama's largest source of revenue was income taxes. According to the Alabama Department of Revenue, the state collected more than 3.75 billion dollars in personal income taxes compared to only 451 million dollars in corporate income taxes.[14] Thus, the tax revenue collected from Alabama citizens - most making below the national median - was 8 times higher than that collected from corporations. Moreover, sales taxes, which also reduces disposable income, contributes to financial shortfalls among working Alabamians. Sales taxes are regressive because poor and working-class people pay a larger percentage of their income in sales taxes than wealthy individuals. For example, the sales tax on $100 worth of groceries would be $10 in many areas. That $10 represents a much larger proportion of the income of a low-wage family than that of a high wage family. Although most Alabamians represent the former, they still paid over $2 billion in sales taxes. In fact, sales taxes were the second largest source of revenue in the state. Alabama's gasoline tax (the fourth largest source of revenue) is another tax that hurts the average low-earner in Alabama. Meanwhile, Alabama's lenient regulatory structure collected just a little more than $556,442 from store licenses, an amount that includes payday lending outfits.

Table 4. Selected Revenue Sources for the State of Alabama			
Source	Revenue in US Dollars	Percent of Total Revenue	Percent Rank
Personal Income Taxes	3,753,387,566.17	40.4%	1
Sales Taxes	2,026,866,139.06	21.8%	2
Corporate Income Taxes	450,521,057.17	4.85%	3
Gasoline	402,453,425.25	4.3%	4
Store Licenses	556,442.15	.01%	43
Total Revenue	9,285,142,692.52		

Table 4: The majority of Alabama's revenue is derived from regressive taxes levied against individual citizens while corporations that benefit from generous incentives contribute little to the state in the form of job growth and income. The resulting financial burden experienced by individual citizens reduces their income which in turn stimulates the receipt of payday loans.

Such tax policies are acutely regressive because they reduce the amount of disposable income that Alabamians can spend in the economy. Although policy-makers espouse a pro-business climate in Alabama, average citizens with little extra cash appear to be actually responsible for most of the revenue collected. Ultimately, these regressive policies adversely affect income and cash flow among the people who need it the most. Many of the residents end up using payday loans to offset the resulting shortfalls.

Table 5. Correlation of Payday Lending Stores with Residents Working in High Growth Professional Fields and Median Household Income						
City	Pop.	Stores	Stores per 10,000 People	Pct. in Professional Positions	MHI in US $	Estimated Amount Lost In Interest and Fees to Payday Loans in US $
Auburn	55,207	6	1.1	50.3	37,853	1,431,472.08
Birmingham	211,827	75	3.5	30.9	30,276	7,893,401.00
Decatur	55,774	21	3.8	29.0	41,972	5,010,152.28
Dothan	67,269	25	3.7	32.6	41,417	5,964,467.00
Florence	39,388	16	4.1	30.9	34,305	3,817,258.88
Gadsden	36,760	14	3.8	27.2	25,878	3,340,101.52
Hoover	82,214	6	0.7	53.6	75,606	1,431,472.08
Huntsville	181,734	42	2.3	40.6	46,821	10,020,304.56
Madison	44,402	8	1.8	59.1	92,427	1,908,629.44
Mobile	194,829	76	3.9	34.0	38,566	18,131,979.68
Montgomery	206,346	75	3.6	35.2	42,403	17,893,401.00
Phenix City	36,115	18	5.0	31.6	35,151	4,294,416.24
Prattville	34,462	11	3.2	38.9	57,323	2,624,365.48
Tuscaloosa	92,217	22	2.4	33.0	36,429	5,248,730.96
Vestavia Hills	34,039	0	0.0	65.6	78,968	1,431,472.08
				r= -0.9	r= -0.69	

Table 5: The number of payday lending stores has a strong inverse correlation (r = -.9) with the amount of workers who occupy professional positions in high growth industries. That is, the more workers in such industries the fewer payday lending stores in the city. The same is true, to a slightly lesser degree (r = -.69), for Median Household Income.

Table 5[15] provides a look at the payday lending stores in Alabama cities. It suggests that payday lending is strongly associated with job type and median household income. Also, an estimated dollar amount of money lost to interest and fees can be calculated by multiplying the number of stores by the estimated amount of revenue for the average lender (This metric was discussed on page 2).

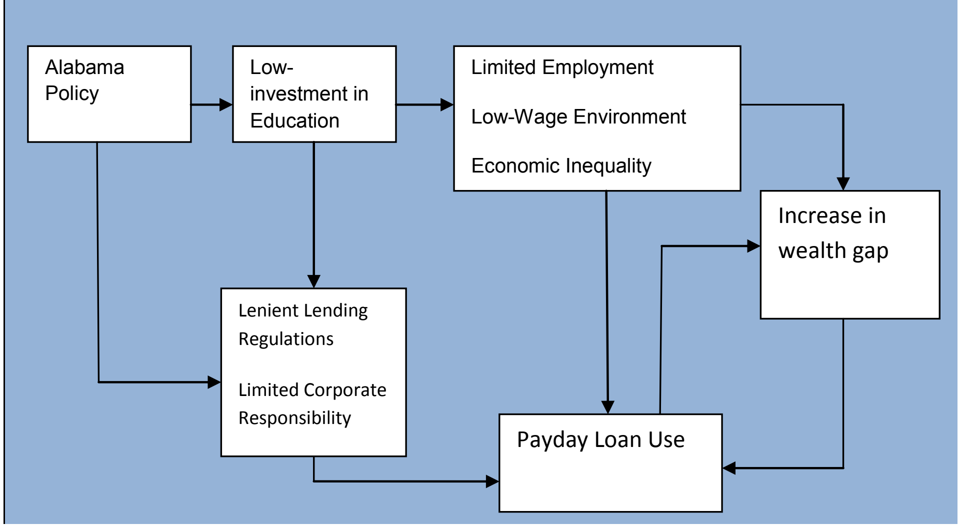
Policy and Payday Loan Regulation: Supply Side

State officials have allowed the payday lending industry to operate with near impunity. State law mandates that individual payday loans have a $500 limit and 17.5% interest rate cap. Nonetheless, lenders are allowed to offer roll over loans which allows customers to take out an additional loan on top of an active loan. Interest rates are then applied to the combined loan. A customer who takes out a $500 loan owes $87.50 in interest. If that customer returns and takes out a $400 loan before he pays his balance, he will then owe $157.50 in interest. The total amount due on his payday will be $1057.50. Such loans promote perpetual debt.

Although the state of Alabama allows only one roll over loan per store and mandates caps on loan amount and interest, such regulations do little to deter these predatory lending practices. Unlike traditional banks, payday lenders in Alabama are not required to report financial statements to the Alabama Banking Department nor is there any statewide restriction on how many stores can populate in one area. The latter is important strategically because by allowing unlimited stores to populate one area, any restriction on roll over loans or loan caps is effectively worthless. An individual can receive the maximum loan at one store and receive subsequent loans at other stores rendering the cap on interest useless.

Alabama policy affects the payday lending industry on both the demand and supply side. As displayed in Figure 3, Alabama's lack of investment in education and innovation has led to a low-wage job environment. Underemployment contributes to the inability of the average citizen to have enough cash flow to meet financial obligations. Hence, the use of payday loan stores. On the supply side, policy-makers have created a business friendly tax environment, but appear to be unable to mandate that businesses contribute more to the economy in the form of jobs and tax revenue. The bulk of Alabama's revenue is still accrued by taxing average citizens. Furthermore, Alabama has maintained a relaxed regulatory environment concerning payday lenders. Although, certain localities like Birmingham have implemented policies to restrain the growth of payday lending, little has been done to mitigate their ongoing presence. The lack of effective statewide policy has ultimately given payday lenders the ability to continue charging usury-like interest to individuals who are economically disadvantaged.

Figure 3. Theoretical Model Explaining the Success of Payday Lending in Alabama



Income Inequality and Payday Lending

Payday lending is a symptom of and contributor to income inequality. Precipitated by lower demand for unskilled workers, the gap between the wealthy few and the depraved many is getting wider. While inflation has remained stable in recent years, the cost of resources essential to life such as fuel, utilities, transportation, and food are increasing. As a result, many low-income households struggle to meet financial obligations associated with the use of these resources. As a result, many households turn to payday loans to meet these needs. Payday lending is therefore a symptom of residents living within a low-wage environment. Until policy-makers become committed to education and more aggressive in their recruitment of businesses, Alabamians will continue to struggle to meet financial obligations and thus, rely on payday lending.

Payday lending is also a contributor to economic inequality. Alabama's median household income is one of the lowest in the nation. Research suggests that the average loan recipient earns less than $40,000 annually, which is below the median for Alabama households.[16] This means that the average recipient is relatively poor. Moreover, the research goes on to say that the typical recipient does not hold a college degree nor are they homeowners. In essence, the typical recipient has little capital that can develop into productive assets. Payday lending contributes to economic inequality by increasing the debt load of people who are already struggling financially. The higher the amount of fees and interest paid by recipients, the lower the amount of financial capital they have to develop assets.

As with the rest of the United States, Alabama has high rates of income inequality. Income inequality can be compared with the rate of payday loan stores for the largest counties in Alabama.

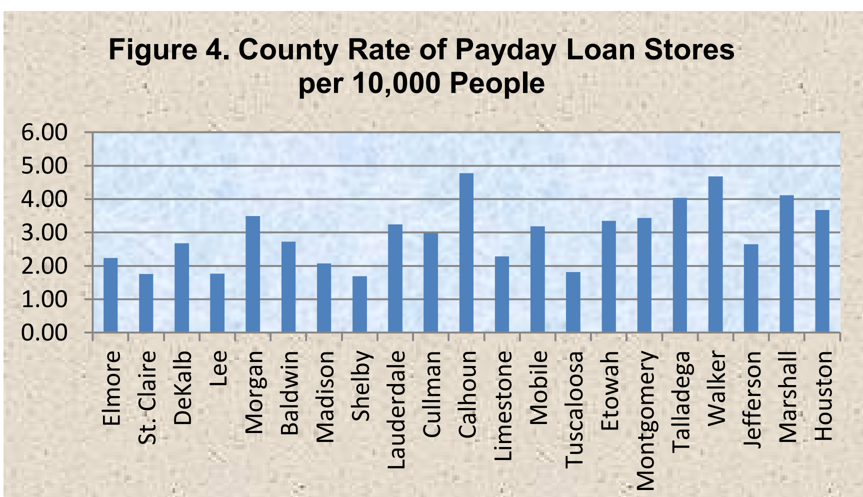


Figure 4: Calhoun and Walker Counties have the highest rates of payday loan stores in Alabama.

These rates can be compared to measures of inequality. There are many ways to calculate inequality. One of the most accurate methods is by averaging the household income of the wealthiest 20% and calculating the difference between it and the median household income for a given geographic region. The same is done for the poorest 20%. The two measures can then be set as a ratio with the difference between the highest 20% and the median set over the difference between the lowest 20% and the median. For example, the wealthiest 20% of residents in Jefferson County earned an average of $167,670 in 2012. The median household income in Jefferson County is $43,959. Thus, the difference between $167, 670 and $43,959 is $123,711. The poorest 20% of residents in Jefferson County earned an average of $8,471. The difference between the median and the average income of the poorest residents is thus $35,488. The median is an unbiased representation of the midpoint. It is unbiased because it is not influenced by excessively large or small numbers. In theory the median provides a fair depiction of income for the common household. The observer can see that there is much greater distance between the wealthiest residents in Jefferson County and the median ($123,711) than the difference between the median and the poorest residents ($35,488). A ratio can be determined by dividing the two differences in income (123,711/35,488 = 3.49). The higher ratios represent greater income inequality.

Figure 5: Several counties exhibit high rates of income inequality. Inequality can be calculated by (1) measuring the gap between the income of the wealthiest residents and the median and (2) measuring the gap between the poorest residents and the median. The two measurements can then be set as a ratio: the higher the ratio, the greater the inequality.

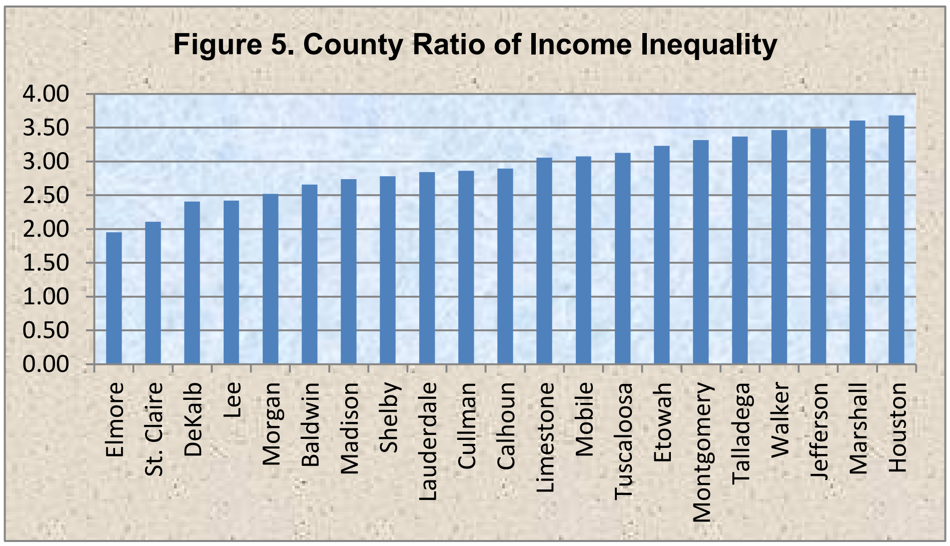
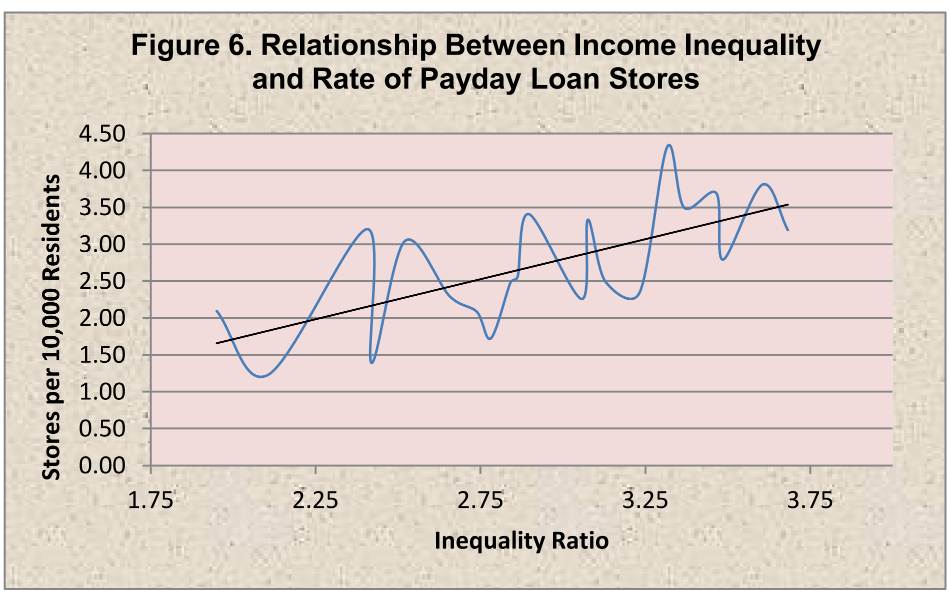


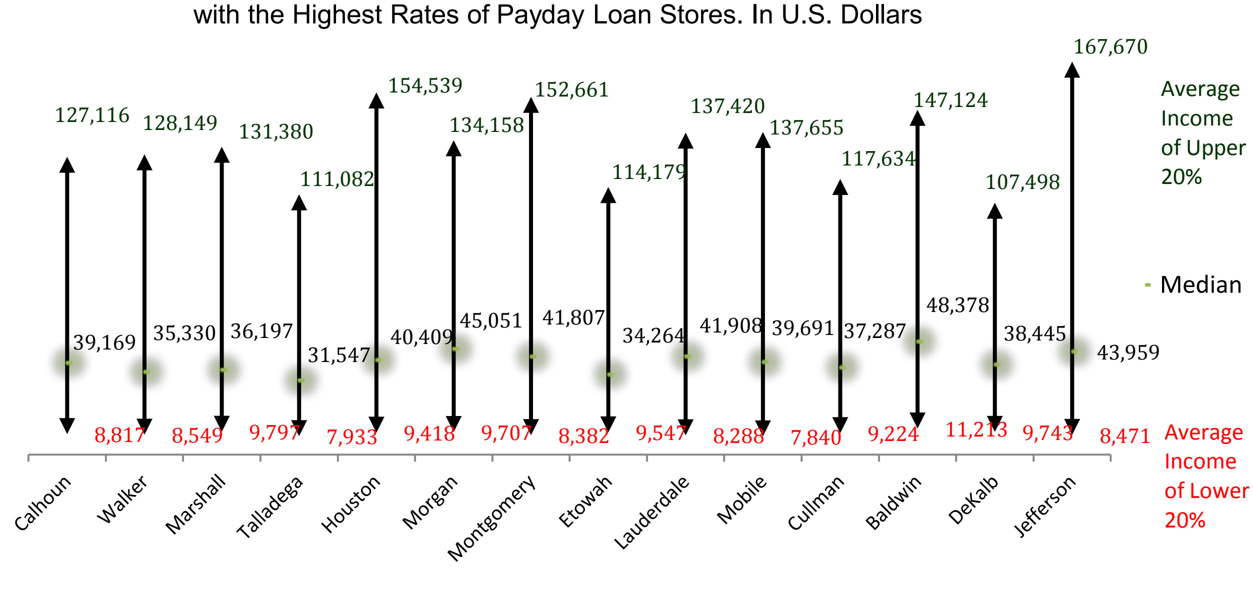
Figure 6: There is a positive linear relationship between the rate of payday loan stores and income inequality: the greater the income inequality of an area, the more payday lending stores will exist in that area.



In Alabama, the rate of income inequality is associated with the rate of payday lending stores as indicated by Figure 6. This suggests that payday lending thrives in places where high-wage jobs are held by a fortunate minority of residents. Meanwhile, the majority of residents are left to compete against each other for low-wage jobs.

The level of county-wide income inequality can also be examined graphically by displaying the distance between the average income of the wealthiest 20% of residents and the poorest 20%. Figure 7 does this while including median income as a reference point. In areas with income equality, the distance between the wealthiest residents and the median will be equal to the distance between the poorest residents and the median. Income inequality is evident if there is a noticeably larger difference in distance between one of the groups. Notice that, for most Alabama counties, there is a large difference between the median and the wealthy and a short distance between the median and the poor. In most counties, therefore, the median income is much closer to those in the lowest quintiles of earnings. This suggests that there is a higher concentration of poor people in such counties. For example, the median income in Jefferson County is $43,959. Half of Jefferson County's population makes under this amount. The wealthiest 20% of residents earn an average of $167,670. The poorest 20% earn an average of $8,471. Thus, there is a high concentration of people earning between the average low of $8,471 and the median of $43,959. In contrast, there is a wider spread of people making between the median and the average high of $167,670. The counties with high rates of payday loan stores possess similar measures of inequality.

Figure 7. Income Range of the Wealthiest and Poorest Residents for Counties with the Highest Rates of Payday Loan Stores. In U.S. Dollars



Summary Points

Alabama state policy promotes a low-wage environment that benefits payday lenders.

Alabama fails to invest in education and innovation both of which are proven methods of stimulating job growth.

State policy focuses on supply-side measures that benefit corporations; however, the incentives that corporations receive do not translate into economic opportunities for citizens or substantial revenue for the state.

As of 2013, Alabama had 1049 payday loan stores. This number does not include other entities in the poverty industry such as pawnshops and title loan operations.

There are fewer payday lenders in areas that have sufficient amounts of high growth employment.

Residents in Alabama lost an estimated $250,269,035.30 to payday loan interest and fees in 2012.

Residents in Alabama's largest county, Jefferson, lost approximately $33,000,000 to payday loan interest and fees in 2012.

Payday lending contributes to Alabama's high level of income inequality.

There is a positive correlation between income inequality in Alabama and the amount of money spent on payday loan interest and fees.

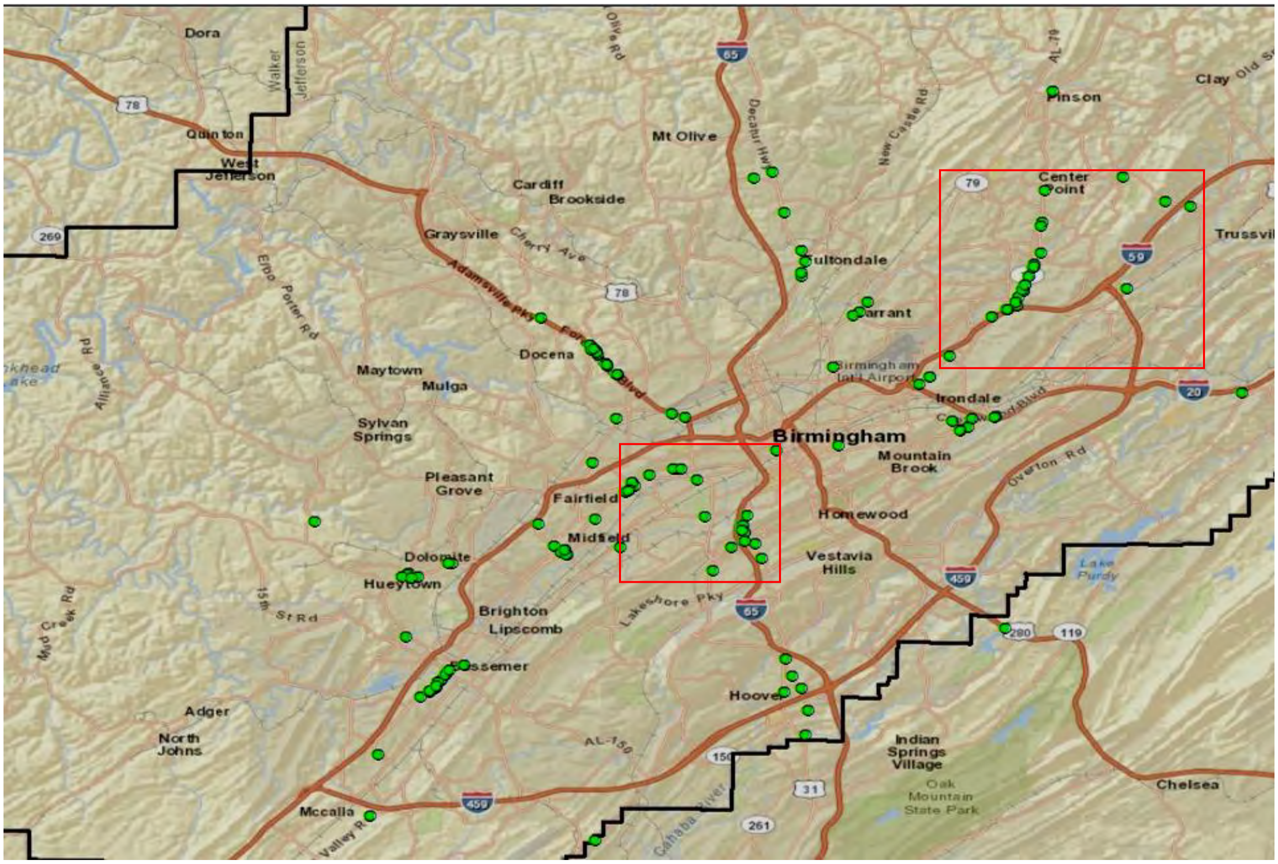
The Market for Payday Loans

Payday lenders must adhere to a business model that defines profit potential as a function of economic despair. It follows then that many such lenders thrive only in circumstances where low wages, income inequality, and financial hardships are the norm. As discussed earlier, Alabama sufficiently meets these criteria. The refusal to invest in education and innovation along with the scarce revenue yielded from supply side economic incentives have left many Alabama citizens in a low-wage trap. As a result, many residents have turned to payday lenders to offset financial shortfalls.

Given their business model, payday lenders have to maintain a presence in neighborhoods that provide them the best opportunity to succeed. This means that payday lenders will likely operate in areas where economically vulnerable citizens reside. Furthermore, in adherence to their business model, payday lenders will have no incentive to promote economic progress within their community as would other businesses, such as traditional banks, grocery stores, or restaurants. These businesses tend to benefit from the economic strength of the community under the logic that they will sell more products if their patrons have more money to spend. Payday lenders on the other hand sell more products when their patrons have less money. An illustration of the local environment of payday lenders will help clarify this point. The next part of this analysis will provide a geographic representation of payday lender locations and the markets from which they capitalize.

The two-mile stretch of road known colloquially as the “Parkway” on Birmingham’s eastside contains 17 payday lending stores or 22.6% of the stores in Birmingham, an amount that does not include title lenders and pawn shops.[17] The high concentration of stores promotes clustering, a tactic that facilitates the receipt of multiple loans by one individual. The neighborhoods adjacent to the Parkway contain a demographic profile ideal for payday lenders. According to U.S. Census data the area is 69.5% African American, only 16.6% of residents have at least a bachelor’s degree, median earnings from work is $26,432.33 annually and the median home value is $89,000.[18]

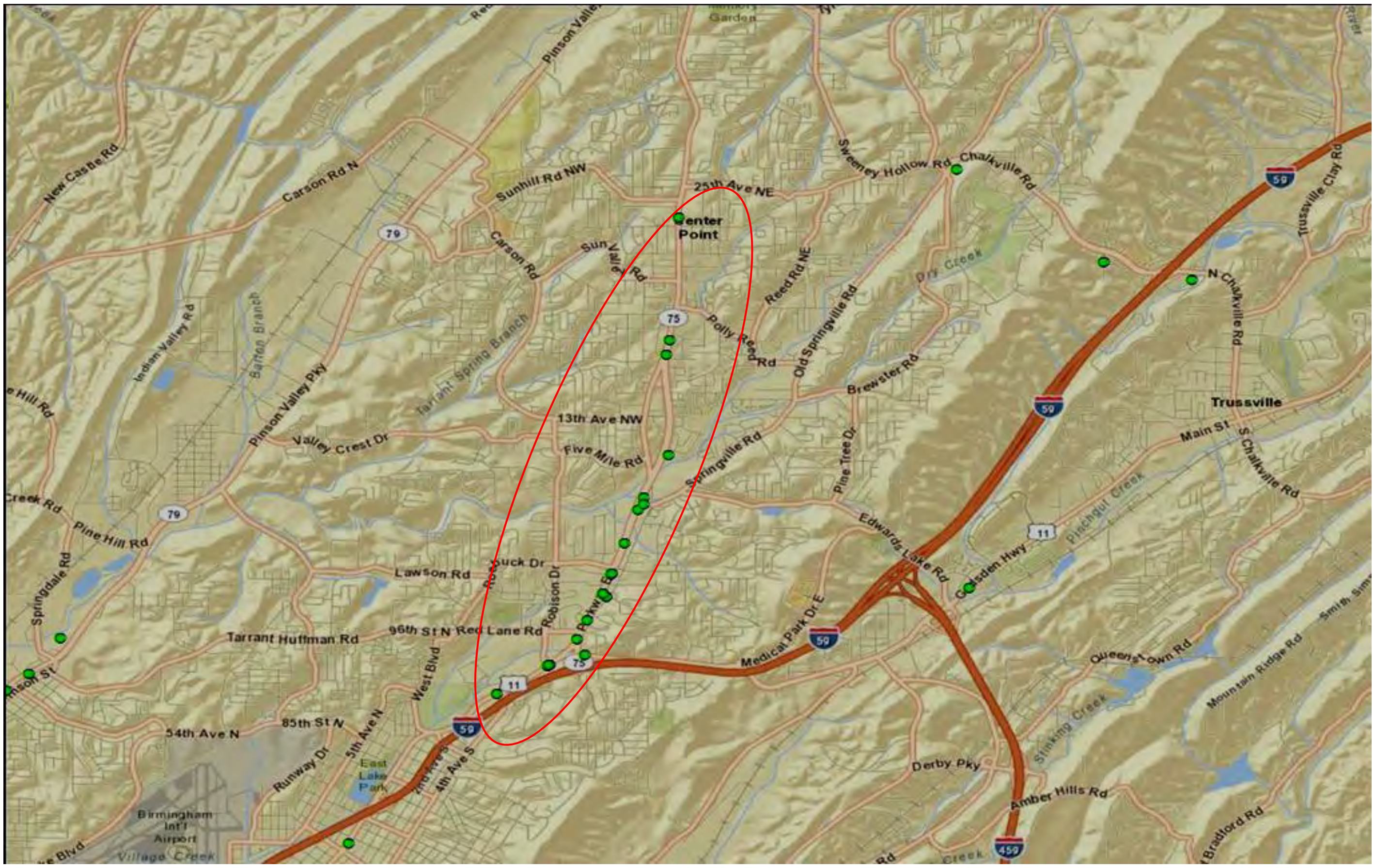
Figure 8. Locations of Payday Lenders in Jefferson County



Geographic Information System (GIS) software was used to assess payday loan store locations relative to their market - the residents within the communities in which the lenders exist. Jefferson County was selected for this analysis because it has the most payday loan stores in the state. Jefferson County also has a diverse racial population as well as a broad range of occupations and income categories. Figure 8 displays a map of Jefferson County with a focus on the principal city of Birmingham. The location of payday loan stores is represented by green dots.

The insets (defined within the red boxes) represent the two areas with the highest concentration of payday loan stores in Jefferson County. These areas consist of the west/southwest and the east/northeast sections of Birmingham. The majority of payday lenders in Jefferson County are in the city of Birmingham. Payday loan stores have become a fixture on busy streets in many areas; specifically those where a large amount of working-class residents live. The clustering of stores not only heightens visibility, but also increases opportunities for lenders to provide loans to those who may have outstanding debts at a neighboring store. Although it is against the law, there is no systematic method of tracking the amount of outstanding loans belonging to an individual. This neutralizes any positive effect of increased competition. One store does not have to provide a price advantage over a competing store. Figures 9 through 16 provide a more nuanced look at important demographic properties of the selected areas.

Figure 9. Payday Lending Locations in East/Northeast Birmingham



The map of east/northeast Birmingham demonstrates the clustering of stores on a primary corridor. In a stretch of road that is less than 2 miles long, there are 17 payday lending stores. The road, known as the "Parkway" contains not only payday lenders, but also a proliferation of title loan stores and pawnshops. The Parkway supports traffic from Downtown via First Avenue North and Interstate 59. It also supports traffic to and from Birmingham's northeastern and eastern suburbs. The neighborhoods surrounding the Parkway are fully populated and vacancy rates are relatively low. As a result, the Parkway is one of the most heavily traveled roads in the Birmingham metropolitan area.

As Figure 9 demonstrates, payday lenders on the Parkway are often situated next to each other. As mentioned above, the immediate juxtaposition of lenders is a sign that competition is not a concern for the owners and that there is a strong market for repeat borrowers. The high concentration of stores lowers the amount of available retail space while simultaneously existing as marquees for poverty and blight. The image that they support could potentially threaten property values and future investments in the community.

Figure 10. Locations of Payday Lenders in West/Southwest Birmingham

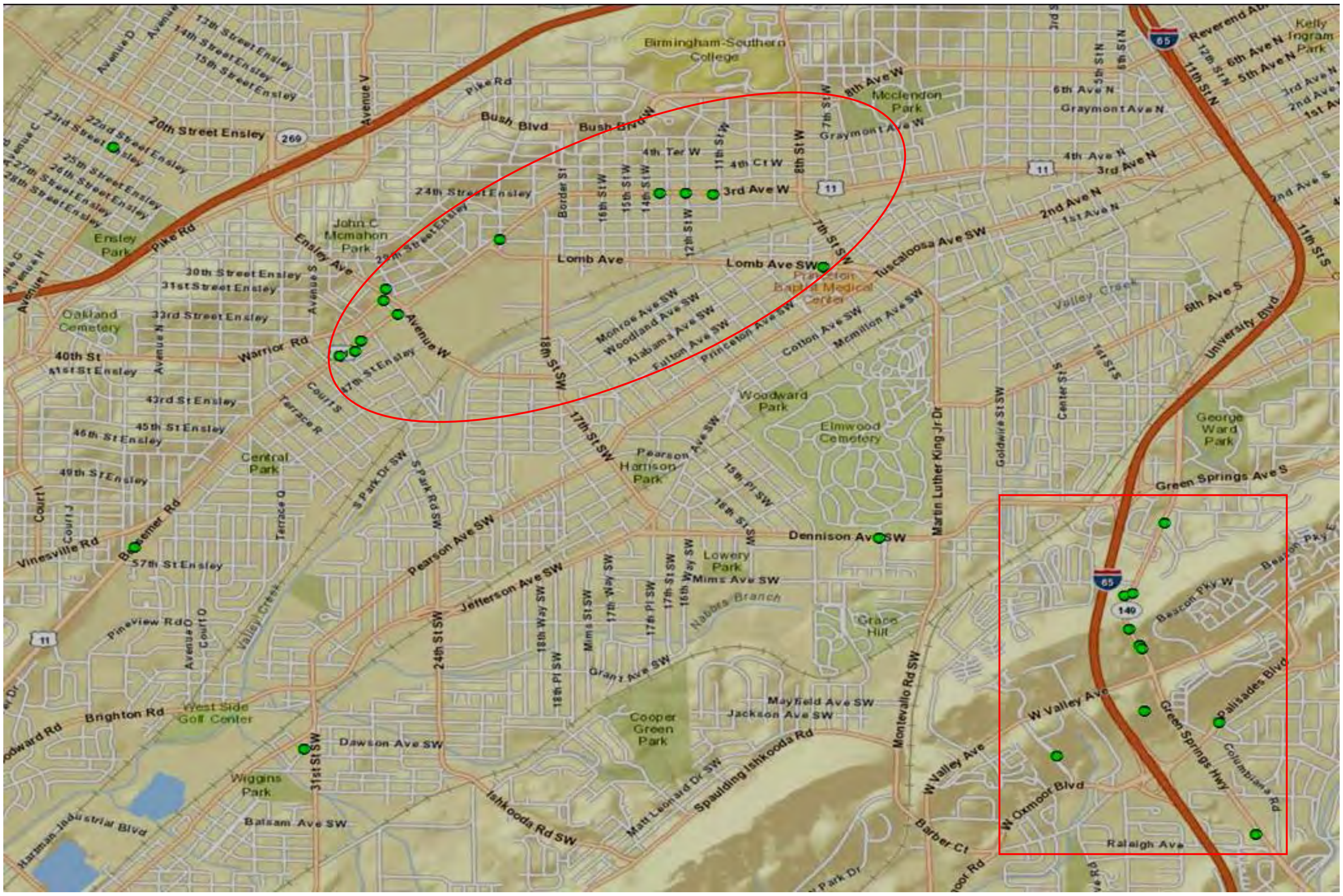


Figure 10 provides a close up illustration of payday lenders in west and southwest Birmingham. Unlike the northeast and east section, these stores are clustered primarily in two separate areas. Similar to northeast and east, most of the stores are located on busy corridors. One group of stores is located on heavily traveled 3rd Avenue West which eventually turns into Bessemer Super Highway. There are 11 stores located on this one street. The Greensprings area located in southwest Birmingham and neighboring Homewood also has a large cluster of stores, most of which sit on Greensprings Highway. The graphic above does not include title loan stores or pawnshops.

Figure 11. Per Capita Income East/Northeast Birmingham

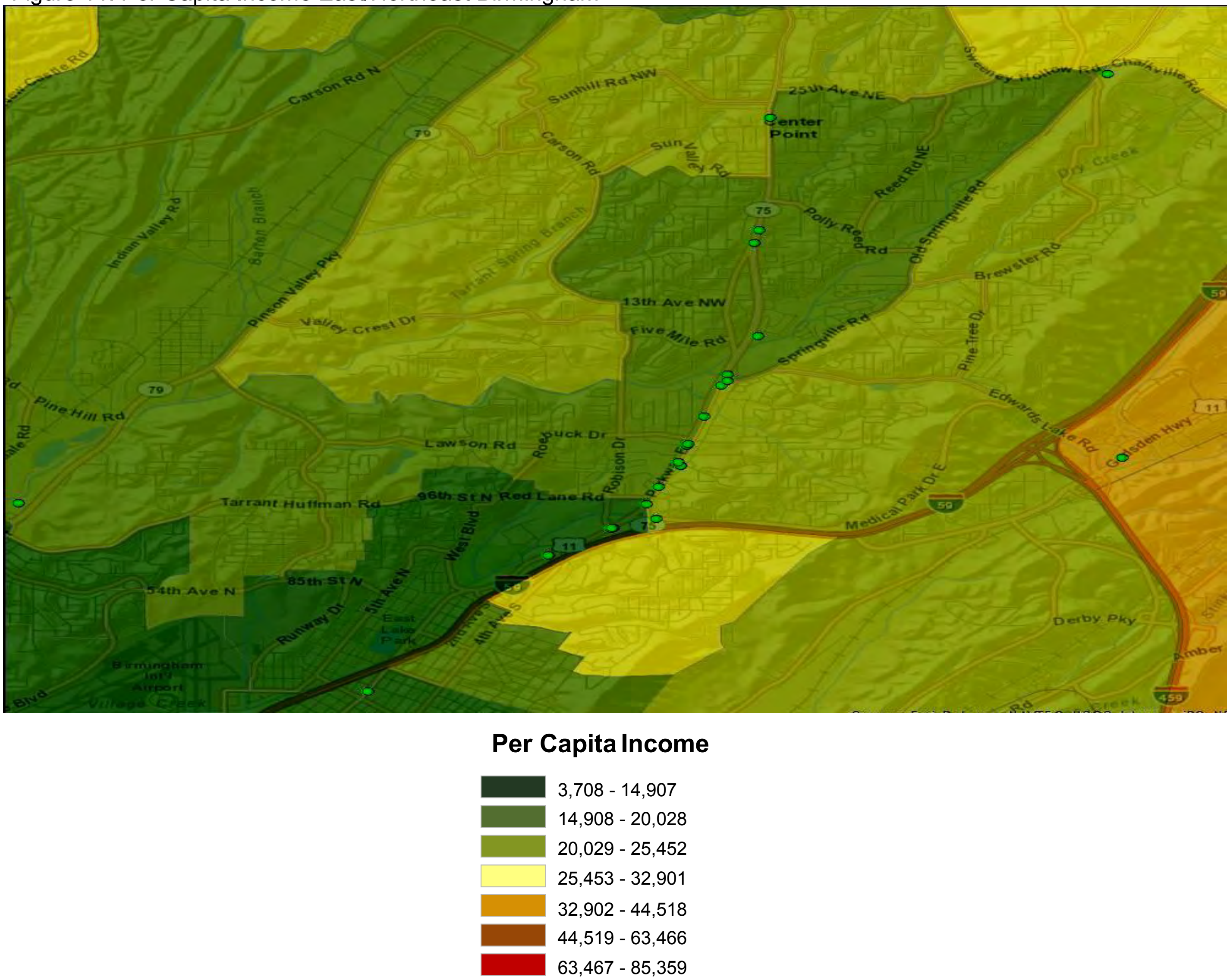


Figure 11 provides an illustration of per capita income for the neighborhoods surrounding the payday loan stores in east/northeast Birmingham. Per capita income is used instead of median household income in this instance because it provides a closer look at the distribution of total income among all residents living in the area. The area is partitioned into Census tracts. Census tracts are meant to approximate neighborhoods. The income levels move upward from green to red. A look at the locations of payday loan stores reveal that they are located in areas that have the three lowest income ranges. These areas consist of mostly working-class wage earners. The majority of residents in this area make below or right at the state average for per capita income of $22,815 annually and the majority of residents make below the national average of $27,319 annually.

Figure 12. Per Capita Income West/Southwest Birmingham

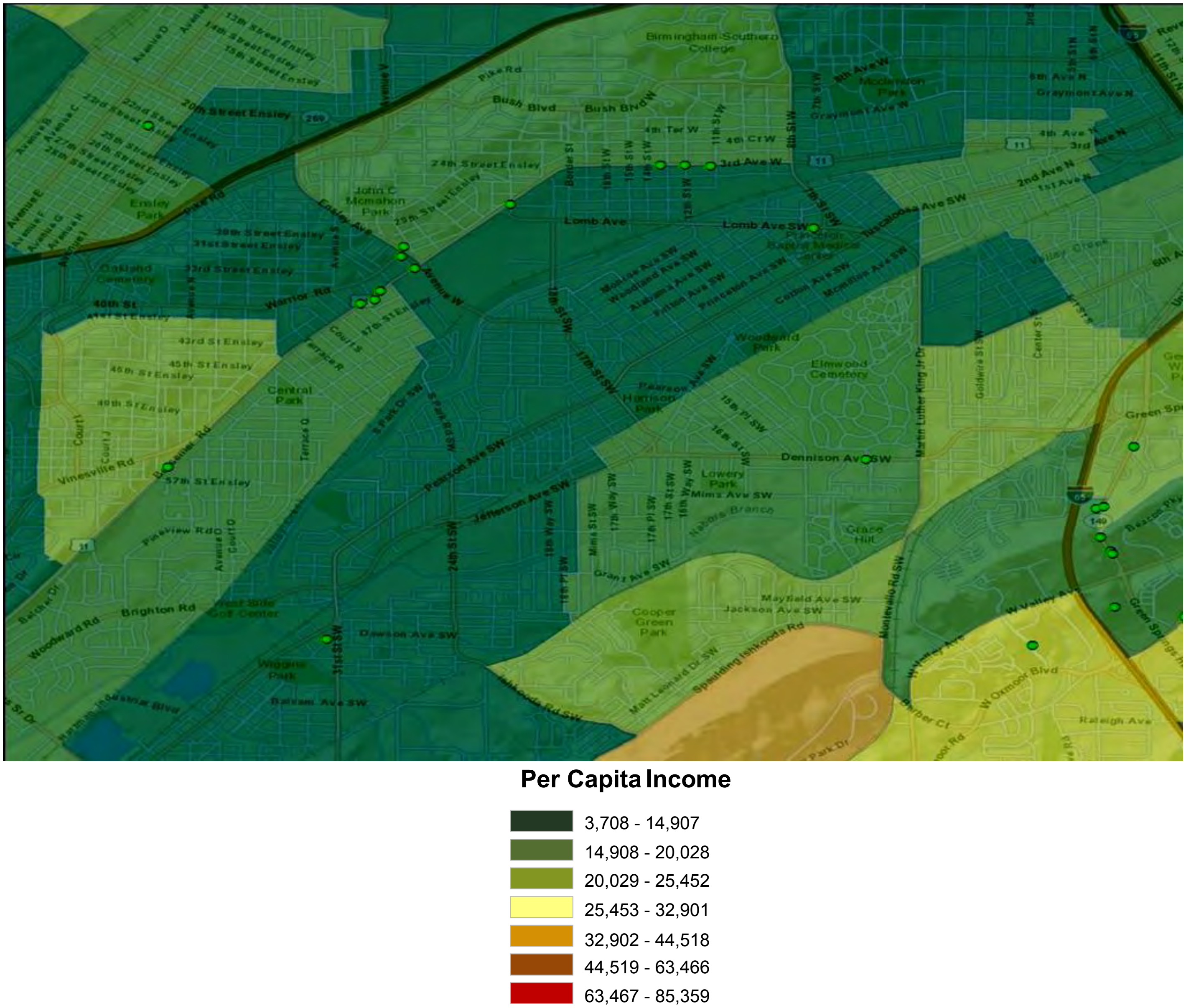
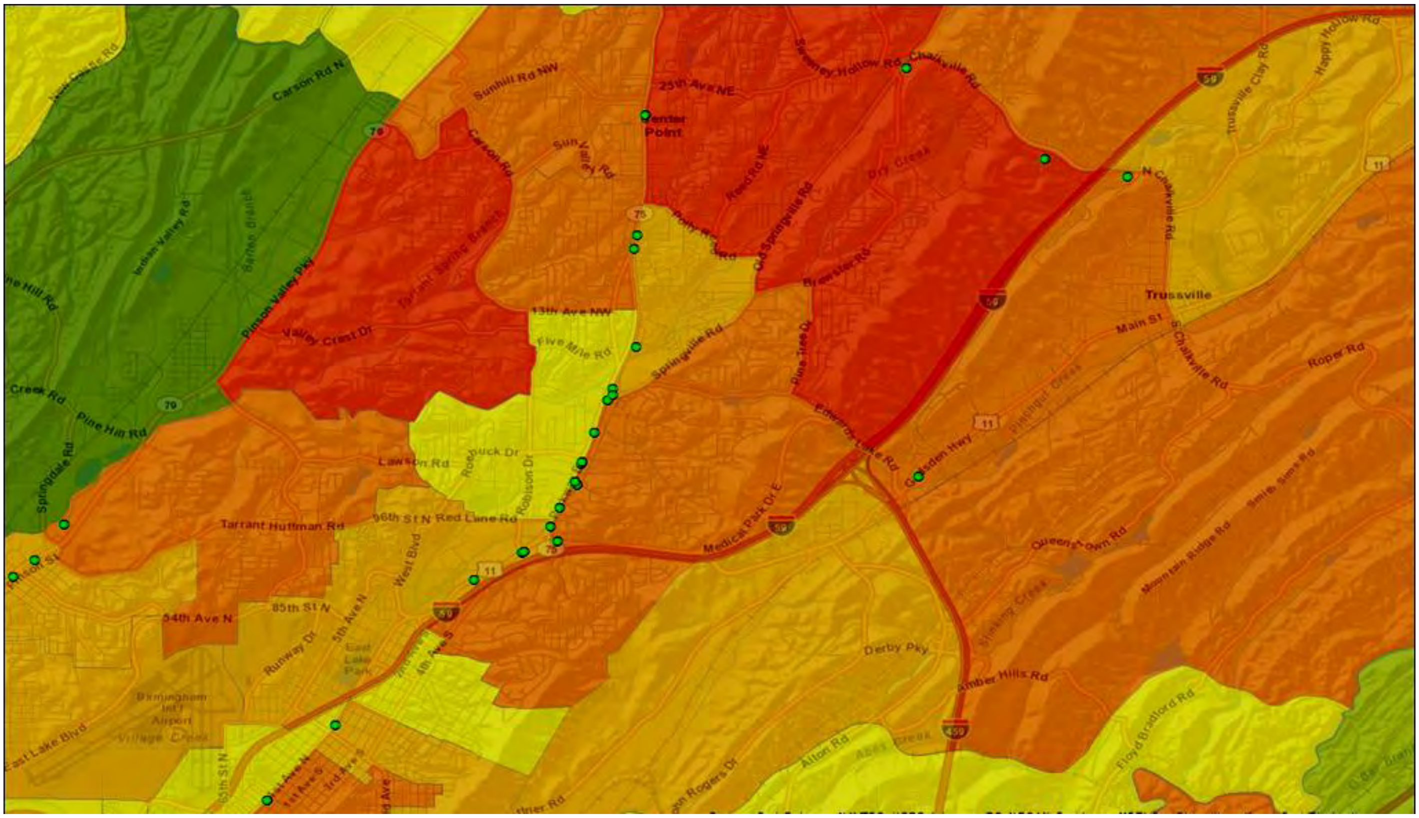


Figure 12 provides the location of payday loan stores relative to per capita income for Census tracts in west and southwest Birmingham. The distribution of income in this area is noticeably low. Residents receive between $3,708 and $20,028 per capita annually ($22,815 is the state average and $27,319 is the national average). There appears to be a relationship between the location of payday lenders and income received by individuals in the surrounding neighborhoods. As expected, payday lenders tend to favor areas where economic hardship is widespread.

Figure 13. East/Northeast Birmingham: Percent of Households Below Federal Poverty Line Consisting of a Single Mother



Percent of Households Below Federal Poverty Line Consisting of a Single Mother

- 0.00 - 24.30
- 24.31 - 41.70
- 41.71 - 49.20
- 49.21 - 55.50
- 55.51 - 61.40
- 61.41 - 68.30
- 68.31 - 86.40

Single mothers are an economically vulnerable group. To target them would fit the business model of payday lenders who thrive off of the economic hardships of workers. Single mothers have to manage the finances for their entire household which include children. As the cost of raising children continues to increase, many of these households may have difficulty building assets. Figure 13 provides a layout of households below poverty occupied by single mothers for east and northeast Birmingham. The map reveals that at least half of the households in poverty are occupied by single mothers. In two of the Census tracts, the number of such households range from 68.31 to 86.40 percent.

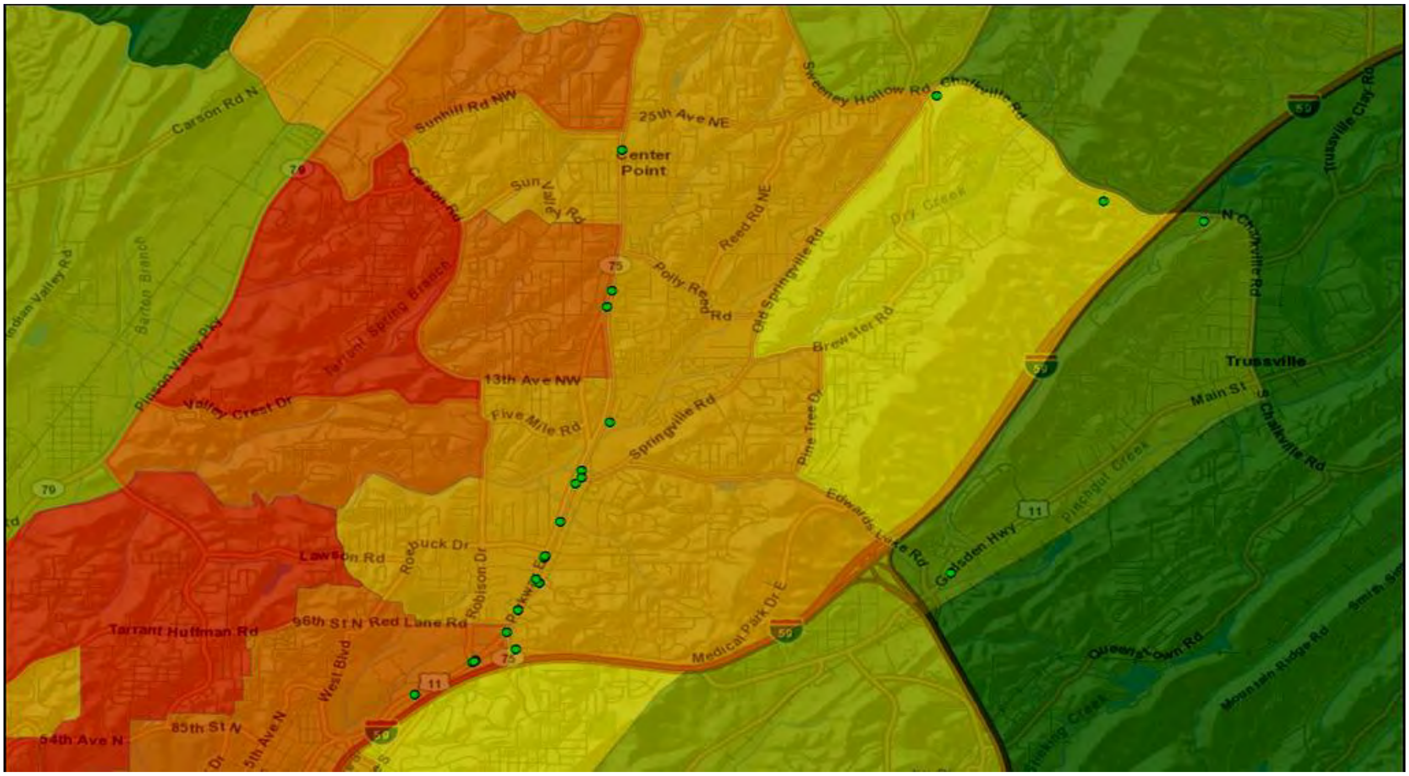
Figure 14. West/Southwest Birmingham: Percent of Households Below Federal Poverty Line Consisting of a Single Mother

Percent of Households Below Federal Poverty Line Consisting of a Single Mother

- 0.00 - 24.30
- 24.31 - 41.70
- 41.71 - 49.20
- 49.21 - 55.50
- 55.51 - 61.40
- 61.41 - 68.30
- 68.31 - 86.40

The payday loan stores in Figure 14 are located in areas where the percent of households below poverty consisting of single mothers is greater than 49.21%. The stores that are on 3rd Avenue West exist in neighborhoods where rates are between 49.21% and 68.30%. However, the stores located on Greensprings Avenue have rates between 68.31% and 86.40%. A paucity of job opportunities and subpar education are conditions that promote economic hardships among residents in Alabama. Individual households in Alabama suffer the associated consequences of the state's refusal to promote serious economic development. This affects single-parent households given that there is usually only one earner present. To the benefit of the payday lenders, there appears to be a large percentage of such housholds in west and southwest Birmingham.

Figure 15. Locations of Payday Lenders in East/Northeast Birmingham Relative to the Percent of the Population that is African American

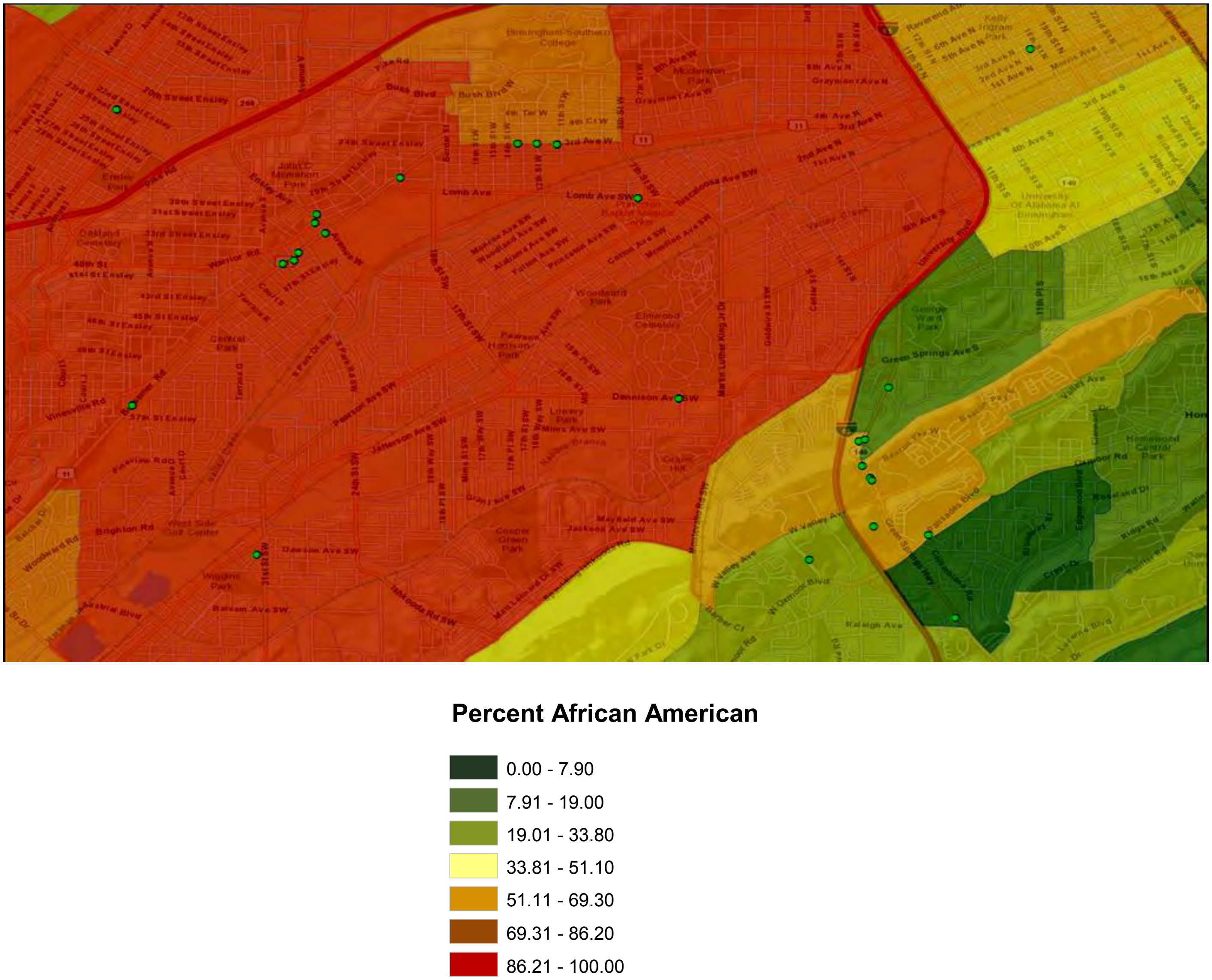


Percent African American

- 0.00 - 7.90
- 7.91 - 19.00
- 19.01 - 33.80
- 33.81 - 51.10
- 51.11 - 69.30
- 69.31 - 86.20
- 86.21 - 100.00

The percent of African Americans living in the tracts increases from green to red. The immediate neighborhoods surrounding the payday loan stores in east and northeast Birmingham tend to be between 51.11% and 69.30% African American. The overall racial makeup of the northeastern Census tracts is predominantly African American with the surrounding suburban tracts consisting predominantly of Whites. Two Census tracts in the area are more than 86.21% African American.

Figure 16. Location of Payday Lenders in West/Southwest Birmingham Relative to the Percent of the Population that is African American



The overwhelming majority of residents in the west/southwest neighborhoods are African American. The Census tracts immediate to the payday loan stores tend to be 86.21% to 100% African American. Even in the Greensprings district, a part of which is in mostly White Homewood, the area immediate to the payday loans stores contains 51.11% to 69.30% African American residents.

Summary Points

Payday lenders locate in areas where there is a market for their product. Thus, they locate in areas where there is a large amount of economically vulnerable residents. However, the indebtedness that they promote potentially exacerbates the economic problems faced by residents, which in turn intensifies the financial hardships they face. <u>In this sense, they sustain a perpetual market base</u> through their practice of issuing non-investable debt to residents.

GIS mapping further substantiates the point that payday lenders in Jefferson County populate areas where per capita income is low.

Single-earner households headed by a mother are one of the most economically vulnerable groups. The areas of Jefferson County that have the highest rates of payday loan stores also contain high rates of single-mothers living below the poverty line.

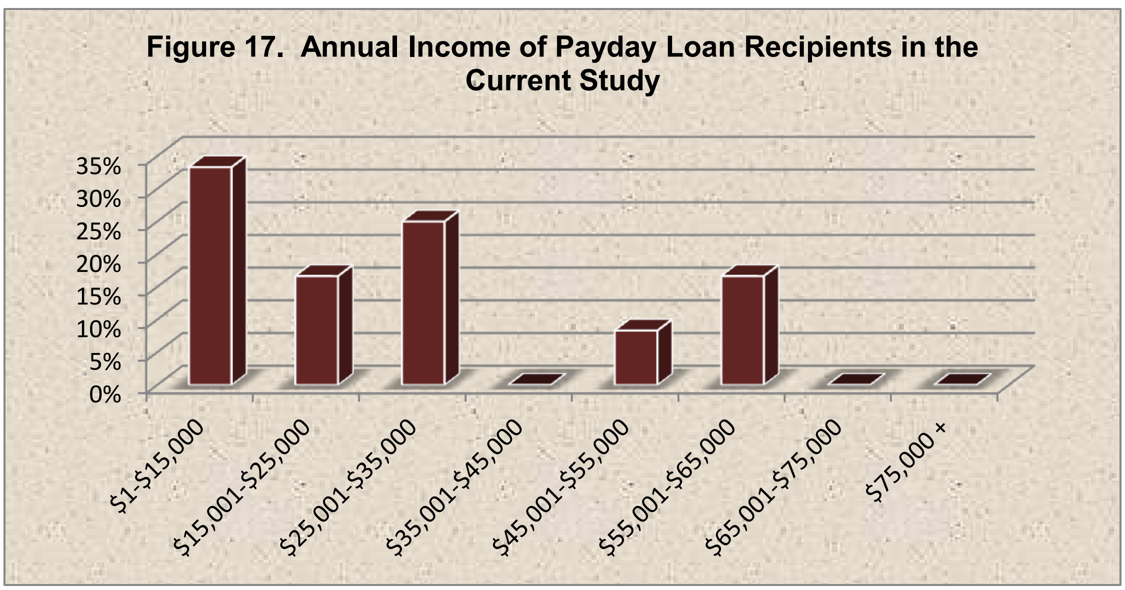
Although Jefferson County is 53.2% White, payday loan stores are mostly concentrated in neighborhoods with a majority African American population.

High traffic streets in low-income communities attract clusters of payday loan stores.

Personal Experiences

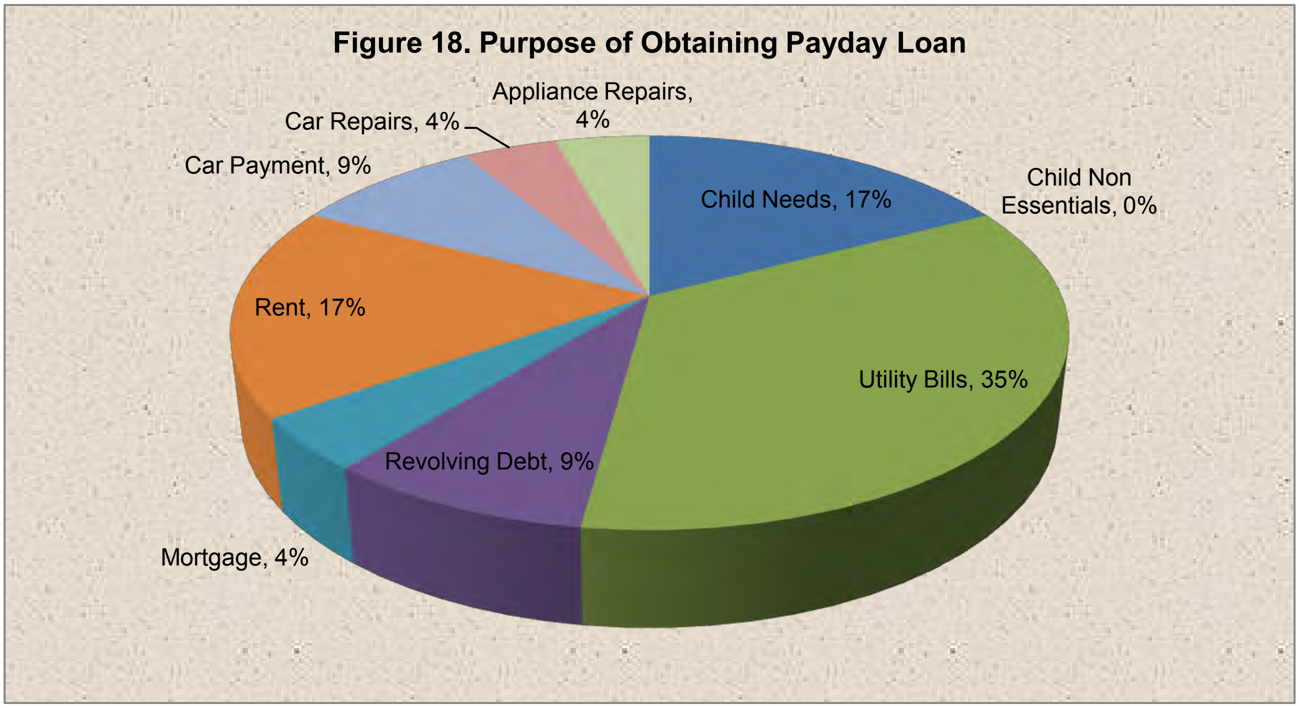
This section provides a micro-level perspective on the effect of payday lending on loan recipients. Using a focus group format, a small sample of residents (n=12) in Jefferson County expressed opinions related to their experience with payday lending as well as the circumstances that led them to pursue the loan. All respondents received at least one payday loan in their lives. After providing basic demographic information, the respondents discussed the effect that receiving a payday loan had on their personal financial status and that of the community. Respondents also provided data on potential alternatives to receiving a payday loan. Specific results of the focus group are provided below followed by an analysis of the data. Major themes that arose during the study will also be discussed.

All of the participants reported having a job. As with the general population, the majority of loan recipients in this sample were low-wage workers. Descriptive income data in Figure 17 reveals that 35% of the participants made $15,000 or less annually. The second highest income category was between $25,001 and $35,000 annually. The low-wage environment in the state of Alabama creates a large pool of workers who are underemployed. The choice to earn higher wages is compromised by the limited opportunities available to residents in a climate unfriendly to commerce development.



Purpose for Obtaining Loans

Participants were asked to provide the purposes behind their decisions to obtain a payday loan. They were provided with several options from which to choose including two that addressed childcare. The first dealt with child needs such as food, clothing, and school supplies. The second allowed for child nonessentials such as gifts, birthday parties, allowance or spending money. Another group of options focused on household expenses such as utility bills, rent, and mortgage. The options also contained categories for car payment and revolving debt. Finally, a fill-in-the blank "other" category was provided. Figure X illustrates the proportion of responses for each purpose. Participants were allowed to choose more than one option.



Consistent with the Pew study discussed earlier, the most cited reason for taking out a payday loan was to pay utility bills. The second highest amount of responses was rent and child needs. From this sample of participants, it becomes evident that the average recipient is not obtaining loans for superficial reasons. If people are short on money and their power or water is under threat of being discontinued, then obtaining a payday loan may become a matter of necessity. Such necessity becomes more prevalent in areas where the economic environment promotes poverty. The environment presents enough obstacles to where they feel compelled to obtain a payday loan. This does not validate the need for a high concentration of noncompeting payday loan stores. There is no evidence suggesting that the high concentration of stores in low-income areas provides a financial advantage to residents.

While the purpose for obtaining a payday loan reflects the needs of residents who attempt to function in a low-wage environment, the high concentration of lenders in low-income neighborhoods is an exploitive measure designed to encourage repeat borrowing. Half of the participants reported taking out three or more loans over their lifetime while half reported that they have used multiple locations. The propensity for recipients to take out multiple loans and use multiple locations helps to explain the clustering phenomena associated with payday loan stores in low-income communities. The proliferation of stores and the option to receive one "roll over" loan facilitates multiple lending deepening the debt obligation of recipients. Many will argue that the individual is responsible for his/her own financial missteps which is true. The purpose of this analysis is not to argue that point, but to suggest that payday lenders take advantage of individuals living in a low-wage environment with few financial alternatives when facing economic hardships.

A Vicious Economic Circle

Accordingly, participants were asked to opine on the effect that payday loans had on their financial status. A major theme that arose can be described in terms of a vicious economic circle. That is, the structure of the lending terms makes it easy for a small loan to grow into a debilitating financial obligation. For example, Participant 10 articulated how easy it was to get behind on her loan repayments in the face of tough economic circumstances. She experienced the vicious economic circle of payday lending when her payroll check was not enough to cover the postdated check held by the lender. The lender sent the check to the bank repeatedly. Each time, the her account accrued a $36 insufficient funds fee. Unbeknownst to her and to perhaps even the lender, Alabama state law prohibits the act of repeatedly sending a previously-bounced check for payment. On top of her loan principle, she ended up being responsible for four insufficient funds fees and loan interest - a total that was more than double the amount of her original loan. In the end, it was not until she received her income tax refund check months later that she was able to get back into the black. Throughout this time, she did not have access to her bank account because her account was in the red.

Providing further insight on payday lending as a vicious economic circle, Participant 1 believes that such loans are "a rip off because when you can't pay the full amount and [you are] just paying the interest, you have paid the loan off over and over again with just the interest." Meanwhile, Participant 9 remarked that the "interest on the loans makes it hard to pay it back , sometimes it put you in a bind worse than you were before you got the loan." According to Participant 2, a payday loan:

> Makes you stay behind. And if you never pay it off or have the means to pay it off, it's really a waste of your time. You have to get a hold on your finances otherwise payday loans are no different from taking drugs. You feel like you have to get the money.

The vicious economic circle that participants suggest arises from receiving payday loans makes it more difficult for recipients to develop long-term wealth. The economic circumstances within a low-wage environment provide few choices for those who encounter economic hardships. Like sharecropping, the recipients may enter the agreement with the hopes of short-term relief, but end up in an enduring cycle of debt. The majority of the respondents reported experiencing a form of this vicious circle.

Powerlessness

The second major theme that arose dealt with powerlessness. Several of the participants described their experience with payday loans as a constant battle between their income and their debt. Although payday lending is a feature of broader economic problems, its ability to intensify these matters is unique given that most other financial instruments are designed to help recipients develop financially. Participant 12 has a bachelor's degree from a major university, a good job, three children, and a husband. Before, however, as a college student, she used payday loans on multiple occasions to help with bills and child expenses. She found herself trapped in debt. Although she knew the potential danger of payday lending, she felt powerless. Both of her parents were deceased and her friends were in similar situations. She stated having “no other resource” and after receiving her initial loan, she was “locked in for over a year.” Indeed, she felt powerless before and after receiving the loan. Others expressed sentiments related to the limited power they have over their economic environment as well as over the terms of improving their personal financial situation. Participant 8 articulates this point by arguing that payday lending “generally takes financial advantage of those with limited resources.”

The vicious economic circle and powerlessness themes reflect the challenges faced by residents who make the decision to obtain a payday loan. Study participants appear to all recognize the dangers involved in attaining payday loans. Many feel that they are pushed into bad deals out of necessity. Interestingly, most of the respondents replied that if payday lenders did not exist, then they would have to borrow money from family or friends. This may be a better financial alternative in the short-term, although it does not address the broader financial problems experienced by many residents.

Title loan stores often share lots or even buildings with payday lending stores. Notice how the word “easy” is emphasized on the façade suggesting that an easy solution to one’s financial problems can be found within the store.

Conclusion

While to receive a payday loan or not is a matter of personal choice and individual responsibility, no financial decision is made independent of the influence of the surrounding economic environment. Within this environment, every decision is made based on the pool of options available which include access to training, an opportunity to demonstrate merit, innovation, education, corporate reinvestment, and sound economic policy. Poor economic environments do not reflect these qualities. Thus, individuals within poor economic environments often make decisions based on a set of factors that are antithetical to growth. Payday lenders are a feature of poor economic environments. They provide a service devoid of value to the individual.

The interest and fees paid by loan recipients in Alabama amounts to millions of dollars in lost wages. An environment conducive to economic growth would allow for the distribution of such funds in a more productive capacity. If the money spent on interest and fees were invested or saved, it would help advance asset-development among residents. To accomplish this, residents must adhere to money-management principles and be privy to an economic environment that provides a wider range of progressive financial options. However, few individual residents have the power to engender the type of large-scale investments that promote job development in high-growth fields relevant to the 21st Century. That is the job of policy-makers and executives on the state level.

The state has heretofore failed to make widespread investments in education and innovation, the two most important characteristics in determining future economic growth. Adequate investment by the state and Federal government as well as by private and public institutions transformed the rural Santa Clara Valley in California to the world's largest center for software, chip, and web development known today as Silicon Valley. Between 1950-1960, San Jose, the principal city in Silicon Valley, grew from 95,280 residents to 204,196 in the ten-year span that marked the beginning of the chip boom. By the time of the dot com era of the 1990's, its population had grown to 782,248. Today San Jose with an estimated population of 982,765 is one of the largest cities in the United States. More importantly, it has the highest per capita income of any large city in the country. Similar growth is taking place in Texas and North Carolina, two red states that have embraced the idea of increasing commerce through innovation. The point is that investments in relevant innovation are returned in the form of jobs and higher wages.

Poverty and low wages stimulate the demand for payday lending. In the long-term, eliminating the demand will take a united effort from the state. In the short-term, policy-makers must take genuine steps to limit the concentration of payday lenders in low-income areas. The combination of a low-wage environment with a high concentration of payday loan stores promotes borrowing. The debts incurred through payday loans do not amount to leveraged capital to be invested with a potential for return. Instead, loan recipients tend to experience an intensification of their economic hardship; hence the vicious economic circle. The state's attempt to limit the amount of loans a recipient can receive by monitoring them via a database will be difficult to enforce. The best solution is to invest in an environment where payday lenders are not needed. Clustering not only engenders more borrowing, but it also contributes to neighborhood blight. As a part of the neighborhood built environment, payday loan stores are symbols that repel progress. Social scientists have known for many years that blight tends to attract more blight. Wilson and Kelling describe this as the broken windows phenomena.[19] A high rate of payday loan stores in a particular area may detract from potential investment in the community, which diminishes its ability to attract legitimate businesses and jobs.

By addressing the issues associated with payday lending in Alabama, policy-makers and concerned citizens have the opportunity to make changes that are fundamental to its economic and social growth. Alabama has the environmental resources, private research institutions, universities, progressive nonprofits and, most importantly - a critical mass of people who are willing to help the state advance economically and socially. Decision-makers and executives must use our past and present economic condition as an impetus for creating an environment free of industries that profit from poverty. Ignoring the effects of payday lending and the broader circumstances that give it prominence in Alabama will eventually cost the state far more than the price to develop a productive economic course for the future.

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[10] SB225 by Senator Holley is an Amendment to Section 40-18-194, Code of Alabama 1975.

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[15] Table uses data combined from the U.S. Census. Selected Economic Characteristics 2010-2012 American Community Survey 3 Year Estimates and the Alabama Banking Department.

[16] See Payday Lending in America. (July 19, 2012).

[17] The "Parkway" occupies several names as it winds northeast before leaving Birmingham and entering into the adjacent suburb of Center Point: (1) Parkway East, (2) Roebuck Parkway, and (3) Center Point Parkway.

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