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Continuous High Interest Rate Borrowing and Consumer Welfare: An Analysis of Maine's "36 Month Limitation" on Finance Company Small Loans*

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* This paper was supported by and prepared for the National Commission on Consumer Finance, who have not as yet accepted the paper and do not necessarily support the views expressed herein.

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Background

Society does not think of "interest" and "credit" simply as "prices" that consumers pay for "goods." In the past, religious strictures and economic beliefs held interest to be immoral and credit a valueless good that consumers should not need or want to purchase. While few people today believe that charging interest for the use of money is immoral, our laws and regulations reflect the still-held belief that people ought not pay more than a given rate of interest and ought not borrow without restrictions.[1] Thus state usury and small loan laws restrict the amount that can be charged and the maximum amount loaned to individuals and some state small loan laws and Federal Reserve regulations restrict (presently and potentially) the maturity of consumer installment loans.

Unlike supporters of minimum price laws (such as "fair trade" laws), whose position often is based on a crass desire to increase their income at the expense of consumers, supporters of interest rate ceilings and maturity limitations on consumer loans appear motivated by a desire to help consumers. Were it not for usury laws and limitations on maturities, they believe, some consumers might be charged too much for credit and be enticed or tricked into long-term "economic slavery." A good expression

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1. Doubt about the morality and value to society of money lending, particularly by high rate lenders, still underlies much legislation, as illustrated in speeches of Maine State Senator Peter Mills, the leading proponent of the restrictive finance company legislation analysed below: "As I said a while ago, you would think that [the finance companies] were manufacturing shoes or producing something good for the economy if you read the official reports in regard to [t]heir expansion over the State. I don't think it is a good thing for the Sta[t]e to have eight or ten of them in Augusta, or five or six in Skowhegan, and I will explain why. They are not like banks. They are not doing a banking business. They are not in there providing a service to people who need money in trouble. They are pandering these loans. They are pushing these loans onto people who shouldn't have them." Journal, Maine State Senate, June 8, 1967, debate on Senate Amendment "A" to bill "An Act Revising Laws Relating to Licensed Small Loan Agencies" (H.P.468)(L.D.681).

of this belief is given by Richard Poulos, Referee in Bankruptcy for the Southern District of Maine:

> High interest has always plagued civilization. Most regulation has concentrated on controlling the rate of interest by setting maximum statutory limits. But this is not enough. Any problems about interest must be resolved by also considering (1) the amount of the loan and (2) the length of time for which it was granted. And the effectiveness of whatever restrictions may exist as far as these two factors are concerned must be tested against their possible evasion by the device of renewals.
>
> Loans for short terms, even at high rates of interest, are not overly burdensome for most poor persons. The cost to meet some monetary emergency by a loan of one or two years is not exorbitant. But no one, let alone a low income person, can long endure (1) high rates of interest (2) on relatively large amounts of indebtedness (3) over long periods of time, from 3-8 years or more.
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> For example, it costs a borrower from a small loan company nearly $440 for the use of $2,000 for a year. Often this represents between 10-15% of his take home pay. Defaults, a common occurrence, create serious problems because interest mounts rapidly. In a situation where the borrower is periodically in default of four months or more, the amount of the interest due (because of the high rate) may become greater than the amount of the installment payment. Unless their installments are greatly increased, something which rarely happens, nearly all subsequent payments are applied to interest and, therefore, the loan can never be repaid. As a result, indefinite extensions of the loan occur, year after year, through frequent renewals.
>
> Renewals soon convert short term loans into long term obligations thereby subjecting the debtor to economic slavery. This has the effect of diverting large amounts of money from a debtor's limited income merely for the purpose of paying interest, thus hampering him from meeting the basic necessities of life for himself and his family. His financial strength is sapped to a point where any common hazard of life such as illness, loss of employment, divorce, etc. inevitably leads to a personal financial catastrophe compelling him to seek relief from welfare agencies or, ultimately, from the bankruptcy court.[1]

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1. Richard E. Poulos, "Proposed Revisions for the Treatment of Uncontrovertable Claims in Chapter XIII Proceedings," unpublished, undated paper, pp. 24-25.

In large measure, due to the efforts of Referee Poulos and Gerald Cope, Mr. Poulos' Trustee in Bankruptcy,[1] the 103rd legislature of the State of Maine adopted, in 1967, the "36 month limitation." This law reduced the maximum interest rate that licensed loan agencies could charge to 8 percent on any small loan remaining unpaid at the expiration of 36 months. This limitation has been applied very strictly; the maturity of a loan is dated from its inception, and extensions, rewritings and additional cash advances are not considered new loans. Nor can the effects of the "limitation" be avoided by splitting loans, since this practice was previously (and still is) prohibited. Much the same arguments as those quoted above were made in support of the legislation and in Governor Kenneth Curtis' veto in 1969 of a law that sought to relax somewhat the 36 month limitation.

Perhaps as a consequence of the 36 month limitation, the number of small loan offices in Maine went from 116 as of June 30, 1967 to 20 as of June 30, 1972. Tables 1 and 2 show and Chart I illustrates the number of companies and offices operated in Maine since 1965. Similarly, the dollar amount of loans outstanding went from $31.0 million in December, 1967 to $10.8 million in December, 1971. Opponents of the 36 month limitation point to these data as clear evidence of the disasterous effects of such legislation. Proponents of the law reply that other factors were more important. Among those cited are the relatively poor business conditions in Maine, the reduction of the maximum monthly rate of interest on the first $150 of loans from 3 percent to 2 1/2 percent, limitations on charges for

1. The referee in bankruptcy is appointed for a renewable six-year term by the federal district court for the district in which he sits. The referee must be a lawyer. He occupies a judicial position in that almost all cases filed under the federal Bankruptcy Act are automatically referred to him. His decisions may be appealed to the district court and thence to the federal court of appeals and the Supreme Court of the United States. In wage earner cases under Chapter XIII of the Bankruptcy Act the referee appoints a trustee to administer debtors' repayment plans. In ordinary bankruptcy cases, in which the debtor's assets are liquidated for distribution to his creditors and the debtor obtains a discharge, the referee appoints a trustee if the creditors fail to elect one.

health and accident insurance and a reduction of the maximum loan size from $2500 to $2000 that also were enacted in 1967 with the 36 month limitation. A decision by Referee Poulos in December 1965, reversed by the United States district court but upheld on further appeal to the Court of Appeals for the First Circuit, In re Richards, 412 F. 2d 635 (1st. Cir. 1969), also reduced the revenue.[1] It held that charges made by finance companies for creditors' insurance were "excessive" under Maine law and therefore not allowable in cases under the Bankruptcy Act. In addition, limitations in the small loan companies' collection practices as a result of reform of Maine's antiquated "debtors' prisons" law and elimination of prejudgement garnishments of wages in 1971 and unfavorable rulings by the Federal Referees in Bankruptcy are believed to have increased their costs and/or reduced their ability to collect from over-extended borrowers.

In any event, some supporters of restrictive legislation maintain that consumers in Maine are better off without the small loan companies. As state Senator Levine put it in the debate on April 13, 1971, on a bill to revise the 1967 law: "Sure, we have all got to agree that the number of small loan companies in the State of Maine dropped and some of them went out of business. I think that is the best thing that ever happened to the people of the State of Maine. After all, we are here to legislate for the benefit of the majority of the people."

The hypotheses about consumer behavior and welfare and the operation

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1. In re Richards, CCH Installment Credit Guide, 98.556, January 4, 1966. Also see In re Perry, 272 F Supp 73 (D Me. 1967), affirming Referee Poulos' decision that under Section 656(b) of the federal Bankruptcy Act, a claim for repayment would be totally disallowed unless the lender could prove that the loan was free from usury. Because the finance companies were charging the maximum rates allowed for interest, creditors' insurance charges that they could not prove to be "not excessive" were held additional interest that was usurious. All except one company chose to settle their claims at about 50 percent of the amount due rather than attempt the required proof.

of small loan companies held by supporters of the "36 month limitation" are outlined next, together with the counter-hypotheses of opponents of the legislation. This structuring of the argument serves as a basis for analyzing the effect of consumer loan legislation on consumer welfare.

Underlying Assumptions about Consumer Behavior

A number of assumptions about consumer behavior apparently are made by supporters of legislation to restrict the maturity and amount of loans that consumers can obtain (hereafter called "regulators.") The first assumptions considered concern the rationality and competency of consumers. Some regulators view consumers' decisions to borrow from small loan companies as "unnatural" and "not justifiable." The regulators consider that anyone who borrows money at a 36 percent annual interest rate (the highest legal rate on loans up to $150 in Maine before the 1967 law change) or even 30 percent (the present maximum rate for loans up to $300) is not making a rational decision. This hypothesis about consumer decision making may take two forms. One is that some consumers cannot realize how much the funds they borrow really are costing them. Such borrowers are envisioned as unable to understand how much of their income will be required to meet the interest and principal payments despite the disclosures mandated by the "Truth in Lending" legislation. The second version of the irrationality assumption is that no (or very few) decisions made subject to such a high interest rate for funds can be rational, by definition. ("No one needs money that much.")

Other regulators believe that borrowing at "high" rates is rational for periods of a year or two (or are willing to accept consumers' relatively short run irrational decisions), but believe that the consumer is not com-

petent to plan his income and expenditures over a time horizon beyond three years. Hence, he borrows now to satisfy a present perceived need (perhaps extravagance) without considering or understanding that the amount borrowed plus interest will have to be repaid. Lenders, it is believed, take advantage of the borrower's lack of planning competence. They lend him the funds he wants even when they do not expect him to repay the principal plus interest within the contract period. Rather, lenders want him to extend the loan (perhaps with some additional funds added) over as long a period as possible in order to collect as much of the huge interest charged as possible.

Another version of the way regulators believe lenders take advantage of a borrower's incompetence or weakness is by offering him more money (perhaps by actually showing him cash) before a loan is fully repaid, to tempt him into continuing indebtedness. Thus, regulators claim, lenders get borrowers to mortgage their lives; the borrowers are, in effect, indentured servants to the loan companies.

A second set of assumptions held by some regulators is not based on consumer irrationality or incompetence. Rather, they believe that consumers are rational and hence would not borrow at such high rates ordinarily, but due to special situations, such as unexpected illness, auto repairs or replacement, loss of job, inability to cope with bills from many creditors, etc., are "driven" to borrow money from high interest rate lenders. Once in debt to these lenders, a consumer cannot fully pay off his loan because the high interest charges take too much of his income. Consequently, the loan company has him "on the hook."

Another sub-hypothesis within this set postulates that consumers are not aware of the lower rates at which they could borrow from commercial banks and credit unions. Rather, they are enticed into the small loan company offices by advertising or arrive by accident, and once in debt, cannot repay their loans because the high interest takes so much of their income.

Finally, in response to the finance companies' arguement that they wouldn't lend if borrowers could not or would not want to repay the funds, regulators contend that the companies rely on harsh collection tactics to compel repayment. Threats of attachment of personal property, debtors' prison and garnishment of wages (allowed until 1971 in Maine), badgering and psychological persuasion are examples of the methods allegedly used to get unsophisticated borrowers to sacrifice a large part of their income to repay the loan companies. Alternatively, large interest charges make it profitable for the finance companies to provide funds beyond many borrower's ability to repay so long as enough of them will (or can be persuaded to) repay their loans.

To summarize, regulators believe that consumers make irrational borrowing decisions, are incompetent to understand the future effect of present actions, are forced to borrow because of emergencies, and/or are ignorant of lower cost alternative sources of funds. For any or all of these reasons, borrowers become indebted to high rate small loan companies and cannot and/or are not allowed to get out of debt. Therefore, a law that limits the period over which lenders can charge more than eight percent interest on loans is necessary to protect borrowers from themselves and/or rapacious lenders. Otherwise lenders will be further encouraged to "push" money on people who should not borrow at rates they cannot afford.

Opponents of restrictive legislation (hereafter called "anti-regulators") argue that the regulators' hypotheses are either incorrect or irrelevant. That consumers borrow at what seems to be a "high" rate is not evidence of irrational behavior. Several rational explanations can explain this behavior. First, the anti-regulators argue, the interest rate charged is not "too high." Rather, the rate reflects the cost of lending relatively small amounts in a particular setting to a relatively high risk group of consumers. Small loan companies offer their customers "personalized" service. The loan company manager knows his customers individually, treats them with consideration, takes time with them to work out new payment schedules when some unexpected occurence makes them behind in payments, etc. The manager does not provide this service because he is a humanitarian but because this is part of the "good" that the borrower is buying for the "high" interest rate he pays.

Also, these borrowers present lenders with a greater risk of default than is faced by low interest rate lenders, such as commercial banks. To reduce losses through default, loan company managers endeavor to know their customers and work closely with them to work off loans. These services and the loan losses that do occur result in costs that are reflected in what appears to be high interest rates when compared to the rates charged for loans by other lenders.

Second, anti-regulators believe that consumers who borrow at "high" rates are not irrational. That these consumers are willing to pay a relatively high payment in the future need not be foolish. Who is to say that people should not have the right to meet present needs for medical care,

education, auto or home repairs, clothing, reorganization of financial affairs, or even vacations or luxuries by contracting for payment from future income?

Nor do the anti-regulators believe that most consumers who borrow from loan companies are incompetent to understand future commitments. Andreasen points out that borrowing, even at high rates, is a rational strategy for persons with unstable income.[1] For one thing, poor persons with relatives and others who are in need may find it difficult to maintain saivngs. For another, as Andreasen puts it, "...given high uncertainty of future incomes [borrowing is] a maximax strategy that takes the course of action that would yield the best outcome if the most favorable future circumstance prevailed."[2]

Third, anti-regulators question the assertion that small loan company customers can or wish to borrow from lower cost lenders. Commercial banks, they contend, would not lend to most of the people served by small loan companies because these people present the banks with excessive potential losses and/or too much trouble. Further, many of the loan company customers cannot get bank credit cards or charge accounts at the better retail stores. While many of these people do purchase merchandise on credit from other stores, they may pay as much or more for this credit in higher prices or poorer service on the merchandise purchased. Loans from credit unions are not available to people who do not have steady jobs, work for companies or belong to churches who run credit unions, or who cannot or do not want their employer, co-workers or church to know their financial condition.

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1. Alan R. Andreasen, "Consumerism in the Inner City," unpublished paper, May 1972, presented at the consumer Affairs Conference at the University of Rochester.

2. Ibid., p.14.

The dilemma of necessitous borrowers is recognized by the antiregulators, but they say that denying them the services of small loan companies hardly solves their problems. If society believes that the cost of unforeseen medical or other disasters should not be borne by those afflicted, direct welfare transfers or loans can be made by a government agency. But those who wish to borrow should not be denied this alternative.

Finally, the anti-regulators admit that some borrowers are irrational, incompetent, and, generally, unable to forego gratification. But, they argue, finance companies provide some of these people with a discipline and management of their finances that allows them to function. More importantly, even though there may be some people who, by some standards, should not borrow, it is bad social policy to deny others the right to contract for the loans they wish. (Similarly, it is wrong to deny all people the right to buy liquor legally because some are alcoholics.) Not only does this policy wrongly limit the rights of others -- it is doomed to failure. People who want to borrow will do so, illegally if necessary, at higher rates and with less consideration and protection from the courts than they would get from licensed small loan companies.

Regrettably, many of the arguments presented cannot be resolved by reference to data or logic. Rather, they are in the realm of philosophy on the proper role of government and the desirability of allowing people to make their own decisions, even when they may harm themselves and their families. However, many important differing assertions by regulators and anti-regulators may be resolved with empirical analysis. In the next section, the effect of the law on small loan company operations is considered to determine why and whether it could be the cause of the companies'

unwillingness to operate in Maine. Next, the profitability of small loan companies in Maine before and after the law is measured to gauge whether their operations were so profitable that they could have (but chose not to) absorb the additional costs imposed by the 36 month limitation. Then, the extent of the small loan companies' reduction in lending is measured to determine the effects of the legislation on the people of the state. Finally, the characteristics of long term borrowers and their propensity to declare bankruptcy are analyzed to test hypotheses about these people and their need for protective legislation.

Small Loan Companies' Operations and the 36 Month Limitation

Many supporters of legislation that reduces the rate of interest on small loans outstanding more than 36 months to 8 percent simply do not believe that a consequence will be the demise of the companies. In his veto message of an act passed by the 104th Maine legislature in 1969 that would have softened the provisions of the "36 month limitation," Governor Curtis recognized the small loan companies' "...important and legitimate role in the financial affairs of our communities." He continued, "They are often the only source of credit for people who are badly in need of financial help and who, because of marginal financial status, are cut off from other sources of credit." However, Governor Curtis evidently did not believe that the "36 month rule" would be severely damaging to the companies' economic condition, because he went on to say that "...in return for the risk of providing credit to those marginal borrowers, the state permits the small loan companies to charge a high rate of interest. Indeed, our small loan regulatory laws are, and they remain, favorable to small loan concerns."

In contrast, the small loan companies claim that they cannot operate successfully under the "36 month limitation." The law not only prohibits them from making loans with maturities longer than 36 months (which is not an important limitation), but prohibits them from renewing loans. This prohibition, they claim, does not allow them to serve regular customers or extend the term of a loan on which a borrower is unable to make scheduled payments. As one company vice-president put it: "Each time the borrower refinances his loan with the lender, the term of the loan becomes shorter and the monthly payment is larger than the payment on the previous loan. Eventually, because of the 36 month limitation that dates from the initial loan, the term of the loan becomes so short and the payment so large that

the lender can no longer serve the borrower's needs since he is unable to make the big payment each month." Consequently, the small loan company cannot renew or extend loans, but must limit its operations to making one-time loans. While data on the percentage of loans made to present customers are not reported to the Banking Commissioner in Maine, data from large companies and from other states indicate that about 62 percent of the number of loans made are renewals (with and without cash added) and about 27 percent are made to new borrowers.

As discussed above, regulators believe that renewals of loans by small loan companies is evidence of their exploitation of consumers' inability to withstand temptation. The regulators also believe that the companies profit additionally from frequent renewals because they can add 60 days of unpaid interest to the principal (thus compounding interest in contravention of the law which does not allow interest charges on more than 60 days of unpaid interest). In addition, regulators believe that other changes in the laws of Maine that restrict the ability of small loan companies to "force" low income borrowers to continue their payments (such as threats of debtors' prison, wage garnishments and attachment of personal property) and the unsympathetic attitude of the Referees in Bankruptcy (particularly Mr. Poulos) towards their claims against the property of bankrupt borrowers have reduced the (perhaps excessive) profits of the companies.[1] Consequently, the regu-

1. A serious flaw in the logic of this argument must be pointed out. If loan companies find renewals profitable because they can use legal and quasi-legal force borrowers to pay off loans that otherwise would be defaulted, severe limitations on creditors' collection remedies would cause loan companies to abandon renewals and concentrate on short term loans. In this event, a legal penalty for extended maturities would not be necessary. However, regulators might retort that the loan companies can avoid restrictions on their collection practices because they deal with unsophisticated customers who are unaware of the creditors' actual legal powers and thus can be bullied or tricked into signing away their rights. The 36 month limitation, on the other hand, is a relatively unambiguous, easily enforced control.

lators claim, factors other than restrictions on "normal" operations are the primary cause of the decline in the number of small loan licensees.

In operational terms, these factors reduce the loan companies' income. Most important, the regulators believe that the now reduced income came not from service to ordinary borrowers, but from "the hides" of those who can least defend themselves -- weak, confused, unsophisticated, necessitous, easily tempted people whom government must protect.

Thus the regulators see the companies as having made exorbitant and immoral profits and view their leaving the state because they are not satisfied with ordinary profits. Also, some regulators believe that national companies have left to "teach the states a lesson," to show other states that restrictive legislation means losing the small loan companies. These regulators beleive that the national companies find the cost of a normal profit a price well worth paying.

In contrast, the anti-regulators believe that the 36 month limitation operates primarily to increase the loan companies' operating expenses. Although they agree that the other factors listed above do reduce the companies' income somewhat, they believe that the emphasis presented above is misplaced. (Of course, they do not agree that most if not all income was improperly earned.) The primary reduction of income, they claim, is due to the reduction of interest earnings on funds in the possession of customers to a rate not much different from the rate that the companies pay to banks, eight percent. The companies' operating expenses continue -- indeed are higher for customers in default -- and the funds are not repaid to the banks or available for loans to other customers. In reply, regulators might argue that within 36 months most borrowers have paid back the principal

and the "funds" that the companies claim are borrowed from banks actually represent the high interest charged by the companies. The anti-regulators can counter-argue by stating that this interest was earned by the companies as a consequence of the operating expenses they incurred and risk they took and, as such, are as much funds as are the amounts originally loaned.

The companies deny the regulators' belief that they ought to be able to make sufficiently profitable one-time loans with maturities of less than 36 months. Operating expenses will go up under such restrictions, they claim. Lending to a present borrower is much less expensive than lending to a new customer. The credit check required is much less extensive, the interview need not be as long and, most important, the risk is less since the present customer's payment record is known. Also, the cost of acquiring business is lower when additional loans can be made to present customers.

In large measure, then, the alternative positions are based on assumptions about the loan companies' income, expenses and return on capital. To put these viewpoints into perspective and render them testable, a model is presented next of the revenue and costs that a profit maximizing lender faces when deciding whether or not to grant a loan. With this model, the effect of the maturity and other restrictions on the lenders' decision making function can be shown. With the important parameters of the model estimated, a test of the alternative hypothesis about loan company behavior can be made.

Revenue and Costs from Small Loans

A consumer finance company's revenue and cost functions may be expressed as:

(1) $$NI = PV[CI - (BA+OC+RC+INT+TAX)],$$ where

NI = net income to equity (owners),

PV = present value of the net cash flow discounted at the firm's cost of capital,

CI = cash inflow from loan payments (including fees and charges),

BA = business acquisition costs (measured as a cash outflow, as are the balance of the costs listed),

OC = operating costs,

RC = risk cost,

INT = interest on debt, and

TAX = income taxes.

As do other firms who maximize their owners' wealth, consumer finance companies attempt to maximize NI. The relevant variables for the decision on whether or not to lend to a specific borrower, are

(2) $$NP = CI-CO,$$ where

NP = net profit from a borrower,

CI = present value of cash inflows from the loan (described further below), and

CO = present value of cash outflow for the loan (described further below).

The CI and CO from and for a loan are analyzed next, first for a new borrower, then for a present and a former borrower.

The expected gross cash inflow (CI) from a first-time borrower may be expressed as:

(3) $$CI = PV(AP_t \cdot pp_t + RN_{t+n} | pp_t = 0), \text{ where}$$

PV = present value as defined above,

AP_t = amount of the periodic payments at time t, times

pp_t = probability of payment (the loan is not defaulted) in time t, and

RN_{t+n} = recovery net of collection expenses, given that the loan is defaulted in a prior period (probability of payment = 0).

When a loan is defaulted, the recovery may take two forms. First, the lender may renew the loan for a longer period, which reduces the amount of the borrower's periodic payments. In this event, the recovery amount, R, equals the present value of the payments, CI, less the operating cost of rewriting the loan and collecting the payments, CO (as explicated below). As a second alternative, the lender may sue to recover the defaulted loan and possibly garnishee the borrower's wages and/or attach his property. In this event, the recovery amount, R, equals the present value of the amount collected less the costs of collection. In the equation, R is the greater of the two alternatives.

The expected gross cash outflow (CO) for the borrower is:

(4) $$CO = AA + CM + PV[CP_t \cdot pp_t + (DC_t \cdot pd_t | pp \neq 0)], \text{ where}$$

AA = amount of cash advanced to the borrower,

CM = operating cost of making the loan (interviewing the customer, assessing the risk, filling out forms, checking credit, recording the loan, etc.),

PV = present value, as defined above,

CP_t = operating cost of collecting periodic payments at time t, times

pp_t = the probability that payments will be made (the loan not defaulted) in time t,

DC_t = additional operating cost of a delinquency at time t, less late charges assessed, times

pd_t = the probability that the payments will become delinquent, given that the loan is not a "loss."

The net profit (NP_n) from lending to the first time borrower, then, if the borrower does not renew or extend the loan, is

$$NP_n = CI - CO. \tag{5}$$

The expected net profit from lending to a former borrower is greater because the borrower presents less risk and requires lower expected operating costs. Because the borrower paid off a previous loan(s), the probability of the loan being good (pp) is greater and the probability of delinquency (pd) may be lower. The operating cost of making the loan (CM) and collecting delinquencies (DC) may be lower because information on the borrower is already in the lender's records. Where the borrower is renewing or extending a loan, the expected net profit is higher yet, to the extent that the cost of making the loan is lower and information on the risk of default and delinquency more current.

Considering that the expected net profit from lending to a former or present borrower is greater than the profit from a loan to a new borrower, the probability that the new borrower will become a longer term customer must be factored in. Thus, the expected net profit (NP) from a new borrower is:

(6) $$NP = NP_n + PV(NP_{rt} \cdot pr_t) + PV(NP_{ft} \cdot pf_t), \text{ where}$$

NP_n = net profit from the initial (new) loan,

$PV(NP_{rt} \cdot pr_t)$ = present value of the net profit from a loan renewed at time t times the probability that the loan will be renewed (pr), and

$PV(NP_{ft} \cdot pf_t)$ = present value of the net profit from an additional loan from the borrower (who then is a former borrower) at time t times the probability that another loan will be made (pf).

Thus, an "unprofitable" loan to a new customer may be made if the lender expects him to borrow again.

Differences in the cost of lending to new and former compared to present borrowers were measured in a study of the branch operations of three major consumer finance companies. The methodology and data used and detailed findings derived are reported in another paper.[1] In that study, data from approximately 2500 branches for each of three years were analysed. Regressions of direct cash operating expenses (total direct branch expenses not including occupancy, advertising, losses and interest) were run for each year of each company on output (the average number of loans serviced), and cost homogeneity variables (percent of loans made to new borrowers, large (over $1000) loans, percent of other than personal loans

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1. George J. Benston, "Operating Costs, Economies of Scale, and Regulation in the Small Loan Industry," study prepared for the National Commission on Consumer Finance (Washington, D. C., 1972).

made, relative factor prices in the county, and whether or not the branch was in a suburb), and market structure and legal variables (concentration ratios, state laws on entry restrictions, and creditors' remedies). The elasticities (and standard errors) of the percentage of loans made to new borrowers ranged from .009 (.026) to .077 (.019). All except one year of one company were over .022. All the balance were over .045 (the most common being about .050) and significant at least at the .05 level. Thus, a doubling of the percentage number of new customers serviced might increase a loan company's operating costs by five percent. The data on former borrowers is not consistent. Two companies' data show operating costs to be lower the higher the percentage of former borrowers, while the third's reveals higher costs.

It appears, then, that new borrowers are served at not much higher costs than present or former borrowers, such that if a finance company made 54 rather than 27 percent of its loans to new customers, its operating costs might increase by only five percent. Consequently it does not appear that a law that restricts lending to the present customers would increase operating costs sufficiently to "explain" the demise of the small loan companies in Maine.

To answer the question more directly, operating costs data as reported to the Maine Bank Commissioner were gathered for each year 1960 through 1971. After extensive checking (that proved both time consuming, frustrating and necessary), some of the data had to be rejected for obvious deficiencies in reporting. Data from the first full year of operation and the last year of operation were discarded as unrepresentative of normal operating conditions. Table 3 gives the number and type (local and national, assets under

$300,000, from $300,000 to $1,000,000 and over $1,000,000) of the companies whose data were used. Table 3

For each year, 1960 through 1971, regressions were computed as follows:

(3) $$OE = b_1CONST + b_2NLO + b_3NLM/O + b_4NLL/M + b_5DEL60+ + b_6NLO/OF + b_7LOCAL$$

where all variables are in common logarithms and

CONST = constant term

NLO = average number of loans outstanding: (number year beginning + number year end)/2

NLM/O = number of loans made/NLO

NLL/M = number of large (over $1000) loans made to the total number made, in percentages

DEL60+ = dollars of loans delinquent 60 days or more per dollar of loans outstanding, in percentages

NLO/OF = NLO per office

LOCAL = 1 if the company is local, 0 if it is national.

"Output" is measured by NLO; NLM/O measures the rate of growth of a company; NLL/M is an output homogeneity measure which extensive testing of a much larger amount and detail of branch data from three major companies showed to be the only meaningful distinction of loan size[1]; DEL60+ measures the additional costs of handling delinquencies; NLO/OF measures the economies of scale related to office size rather than company size; and LOCAL measures differences in reported operating costs between local companies that tend to be owner-run and national companies that allocate central company overhead and interest costs to their Maine oper-

1. Ibid.

ations. Unfortuantely, data on loans to new, present and former borrowers are not reported to the state nor could these data be gotten from a sufficient number of companies.

Table 4 gives the regression coefficients (standard errors) and t values computed for each year. Notable in the table are the positive (and fairly large) coefficients for large loans (NLL/M), positive (though not consistently significant) coefficients for local vs. national companies (LOCAL), and generally insignificant coefficients for the size of office (NLO/OF). The coefficients of the last variable provide evidence contrary to the hypothesis of some regulators that the finance companies left the state because there was insufficient business to allow offices large enough for efficient operations.[1] In any event, the geometric mean number of loans per office for the sample was 367 in 1960, 246 in 1964, 278 in 1967, and 269 in 1970. Even if there were economies of scale related to the size of offices (as is indicated by the better data analyzed for the branch operations of three major companies and over-all operations of 127 companies[2]), the reduction in the number of companies does not appear to have resulted in an increase in the size of the offices remaining.

Of greatest interest are the coefficients of the output variable, the average number of loans outstanding (NLO). These are consistently greater (though not significantly greater) than unity, indicating some diseconomies of scale.[3] Again, the evidence is contrary to the regulatory hypothesis that larger companies could operate at lower costs.

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1. See page 21a

2. See page 21a

3. See page 21a.

1. For example, Gerald Cope (Trustee to Richard Poulos, Referee in Bankruptcy) wrote to Rodney Scribner, Secretary of State, on January 20, 1971: "The reduction in the number of offices of small loan companies is explained from other circumstances to the exclusion of the 36 month rule. The cost factor of maintaining offices with small loan volumes became evident to the industry in the middle sixties and most companies had undertaken a concentration of their business in fewer offices prior to the enactment of the 36 month rule legislation."

2. Benston, Ibid.

3. Since all the data are in logarithms, the coefficients measure elasticities directly. For example, the 1960 coefficient of 1.18 indicates that a 10 percent increase in the number of loans outstanding might result in an 11.8 percent increase in operating expenses.

larger companies could operate at lower costs.

The average costs of making a loan, holding all variables constant at their geometric mean values, was calculated and is given in Table 5.[1] Since not all of the coefficients shown in Table 4 were significant, the regressions were computed with a step-wise regression routine and average costs were calculated with the coefficients that were significant at the .05 level of significance (one tail). These also are given in Table 5, together with a listing of the significant variables. Except for 1971, when only 11 companies are included in the sample, the differences between the two calculations are slight.

The data show generally increasing average costs per loan over the period. From 1960 through 1963, costs averaged about $56 a loan. From 1964 through 1967, when the 36 month limitation was enacted, they were about $70 a loan. For 1968 through 1970 they were about $82 a loan.[2] In part, the increasing costs mirror the changes in the price level. However, the ceiling rates under which the companies operate were not changed to reflect changes in nominal costs. Rather, in 1967, the annual ceiling rate on loans under $150 was reduced from 36 to 30 percent.

While it appears that 36 percent (or even 30 percent) is a very high rate, the average cost per hundred dollars on small loans is even higher.

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1. Since total expense = TE = $b_1 NLO^{b_2} (NLM/O)^{b_3} (NLL/M)^{b_4}$ etc.

$$\text{average cost} = TE/NLO = b_1 NLO^{b_2-1} \overline{(NLM/O)}^{b_3} \overline{(NLL/M)}^{b_4} \text{ etc.}$$

where bars denote geometric means.
Marginal costs can be calculated by multiplying average cost by b_2. Since b_2 is not significantly different from 1, these calculations are not presented.

2. It is interesting to note that the operating costs per loan in 1968, 1969 and 1970 estimated from data from 127 national companies averaged $62. (Benston, Ibid.)

Chart II shows the costs expressed as a percentage of dollars of loans, together with Maine's ceiling rates in effect before and after the 1967 law change. It seems clear that even under the higher rates allowed before 1967, loans under $150 probably were not profitable (recall that losses and interest are not included in the average costs). With the lower allowable rates and average costs, the finance companies do not appear able to cover operating costs for loans under $250 to $300. Why, then, did and do finance companies make these loans?

From Chart III, it appears that after the annual ceiling rate on loans under $150 was reduced from 36 to 30 percent, the companies practically ceased making loans of less than $100. Local companies, who made about 25 of their loans in this size range, reduced this type of loan particularly rapidly.[1] By 1969 this percentage dropped to 3 percent. However, lending in the next size category of $100 to $300 does not appear to have been affected much by the change rate ceiling.

An explanation of why finance companies make what appear to be unprofitable loans (except when the negative contribution margin becomes too great) may be derived from the model of loan company operations presented above. Unprofitable small loans may be made when the company expects that a portion of these customers will renew then at larger amounts, primarily by borrowing additional amounts before the loan matures. Also, the loan

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1. Table 4 shows that local companies reported costs are higher than those of national companies, cet. par. From interviews, I believe that nevertheless they tended to lend small amounts because they know their customers better and are able to take somewhat greater risks than do the national companies.

company is able to assess the risk of lending larger amounts by first lending a smaller sum. Thus, an initially unprofitable loan may result in a later profitable relationship. As is indicated by the model, the present value of the expected net cash flow from the customer is expected to be positive.

This explanation is consistent with the data. Loans larger than $300 to $400 appear profitable. While the 1967 reduction in rate ceilings for loans under $150 made these very unprofitable, the companies still found loans of between $100 and $300 worth making. However, the 36 month limitation deprived them of the opportunity of engaging a customer in a profitable long-term relationship. The effect on the average size of loans made by three major finance companies, shown in Chart IV, also is consistent with the implications of the model. Loans made to new and former borrowers were consistently smaller than those made to present borrowers. The average amount of all three types of loans increased over time as inflation reduced the real amount of funds borrowed and as increasing operating and money costs made smaller loans less profitable to the finance companies. In 1969, when the 36 month limitation became effective (and the particular companies whose data are reported realized that the law would not be repealed), the average size of new loans made increased sharply from $482 in 1967 and $528 in 1969 to $712 in 1968. In comparison, the average size of loans made to present borrowers was $758 in 1967, $778 in 1968 and $822 in 1969. As Chart IV shows, by 1970 and 1971, the average size of loans made to new, present and former borrowers were about the same. For comparison, the average size of loans made by 35 fairly large companies from all parts of the United States (some national, some regional and some limited to one or two states) in 1968, 1969

and 1970 was $755 for new borrowers, $578 for former borrowers and $970 for present borrowers.[1]

Another factor that makes the 36 month limitation particularly difficult for the finance companies is shown by monthly payments schedule for a loan that provides the borrower with about $600.[2] At the present ceiling rate of 26 percent add-on, the monthly payment amount for a 12 month loan is $58, for a 24 month loan $32, and for a 30 month loan, $28. For about an $800 loan the rate is a bit more than 24 percent and the monthly repayments are $80 for a 12 month loan, $44 for a 24 month loan and $36 for a 30 month loan. The take-home family income of the average borrower in Maine who would qualify for these loans is between $475 and $550 a month. While the borrower can make the required payments, a small disaster, such as illness or job layoff, might make it difficult for him to keep up to date. The loan companies recognize the possibility and usually "work with" the borrower by allowing him to extend his payments, often lending him additional funds to "tide him over." Possibly because of this practice, the loss rate actually experienced had been relatively low. Measured as charge-offs or increases to allowances for bad debts less recoveries divided by average dollars of loans outstanding, the net loss rate averaged 2.22 percent from 1960 through 1967. (The low was 1.87 in 1962 and the high 2.62 in 1967.) In 1968 the net loss rate was 3.25 percent and in 1969, 4.10 percent.

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1. Benston, Ibid.

2. The actual proceeds are adjusted up or down to make the monthly payments equal, even dollar amounts.

The operating cost and loss rate data reported provide evidence contrary to the hypothesis that the finance companies make loans in the expectation that some borrowers will default their loans. The high operating costs measured and low loss rate make this "strategy" particularly foolish; consequently, it is doubtful if the companies would follow it.

With the 36 month limitation in effect, if the finance companies extend a borrower's payments, they not only must incur the additional expense of counseling and "working with" the borrower -- the funds they have loaned bear a rate of only 8 percent. As Table 5 and Chart II show, the operating costs alone are greater than 8 percent for most loans. Thus, it appears that the necessity of extending loans when the borrower is unable to pay on time, the reduction of revenue from which operating and other costs could be paid, together with the impossibility of maintaining a long-term customer relationship were important factors in the decision of finance companies to cease operations in Maine.

Profitability of Finance Companies

Those who urged passage of the 36 month limitation and the reduction in ceiling rates argue that the companies could easily absorb the lower revenue. As Governor Curtis said in 1969, "Indeed, our small loan regulating laws are, and they remain, favorable to small loan concerns." To provide a test of this contention, the annual yield on assets was computed for each finance company whose data are given above for the years 1960 through 1971. Because the data do not permit an unambiguous measure of yield, two rates were computed. (1) Net small loan business operating income before income taxes and interest as a percent of average loans outstanding: income taxes are omitted because they need not reflect current operations and because they are often allocated arbitrarily by national companies. Interest also often is allocated arbitrarily by national companies and is largely a function of the type of financing (debt vs. equity, primarily) used. (2) Net total operating income from all sources before income taxes and interest expense as a percentage of average assets "used and useful," which includes working capital, furniture and fixtures, etc., and other assets in addition to loans receivable. While the returns on equity would have been preferable numbers, the data (particularly that of national companies and unincorporated local companies) do not allow meaningful measures.

Tables 6 and 7 present the percentages computed. The data were disaggregated because some critics of the finance companies believe that national companies shift profits from life, accident and disability insurance to an affiliated or owned insurance company and hence understate the income data

Table 6
Table 7

reported to the Bank Commissioner. Mean percentage rates of return on assets are given for local and national companies, for the companies grouped according to asset size (under $300,000; $301,000 to $1,000,000; and over $1,000,000) and for the total. High and low percentages for each group also are given. Chart V presents some of these data graphically.

Without some standard of comparison, one can only draw definitive conclusions about the data that show a negative rate of return. Nevertheless, unless the reports filed are fraudulent, it is clear that the net income before income taxes and interest expense of most finance companies in Maine after 1969 (when the 1967 law began to take effect) was inadequate to support continued operation. For all companies, the small loan percentage had dropped from 10.8 in 1960 to 6.0 in 1967 to 4.6 in 1969 and 1.7 and .08 in 1970 and 1971. The reduction was similar for the total net operating income and for local and national, small, medium and large size operations.

Turning (with less certainty) to the period before the law, it appears that the finance companies' return on assets was reasonably good, considering that they are relatively highly levered. However, even before the 1967 law was enacted, their yields were trending down, as Chart V graphically shows. In part, the reduced percentages are explained by the increasing operating costs shown in Table 5. Average costs per loan increased from $55.72 in 1960 to $66.68 in 1967. Interest on the funds they borrowed also increased over the period.[1] But the maximum rates the companies could charge did not increase.

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1. The annual average rate of finance company paper placed directly, 3 to 6 months, was (from 1954) 1.42, 1.97, 3.06, 3.55, 2.12, 3.82, (1959), 3.54, 2.68, 3.07, 3.40, 3.83, 4.27 (1965), 5.42, 4.89, 5.69, 7.16, 7.23 (1970), 4.91. [Federal Reserve Bulletin, various issues.]

It appears, then, that their rapid exodus from the state was due to worsening returns made impossible by the 36 month limitation and, in some measure, by the reduction in the rate ceiling and maximum loan size, compounded by greater bad debt losses. Thus Mr. Cope's statement (quoted in footnote 1, page 21a), that the finance companies were experiencing cost difficulties before 1967 appears correct (although his explanation "economies of scale" is not supported). But the data do not support Governor Curtis' belief that Maine's laws "...are, and they remain, favorable to small loan companies."

Effect of Decline of Finance Companies Lending on Aggregate Consumer Personal Loans

In testimony before the Business Legislation Committee of the Maine Senate on March 3, 1971, Bank Commissioner Elmer W. Campbell stated:

Figures are available by the small loans companies (probably given at this hearing) indicating that the reduction of their loans is catastrophic. It is true that there is a large reduction in the total of their loans but that does not necessarily indicate that the public is suffering from their inability to obtain loans.

Other sources are available and it is amazing to see the great increase in credit union loans in comparative periods.

From Dec. 31, 1966 to Dec. 31, 1969 loans of small loan companies decreased $11,000,000.

During this same period credit unions in Maine increased their loans by $29,540,000.

During 1970 it is estimated that credit unions increased their loans by an additional $13,000,000.

These figures seem to prove that consumers are properly provided with credit even with the decrease in small loan companies and the consumer has the advantage of much lower interest rates.

The department of banks and banking has received no complaints from the public concerning the closing of small loan companies and it is the belief of the commissioner that the public is able to obtain proper loans.

Commissioner Campbell's figures are not adjusted for the increases in prices that occured since the late 1960's. Chart VI graphs for 1955 through 1971 year end total consumer cash loans (and total loans per capita) at commercial and mutual savings banks, state and federal credit unions, industrial banks and finance companies in 1971 dollars (deflated by the gross national product deflator, 1971 = 100). Loans at credit unions and finance companies, similarly deflated, also are graphed. It is clear that total loans have increased since 1967, although loans made by finance companies decreased. Credit unions show a steady increase over the 17 year period, with a slightly greater rate of increase after 1967. Loans outstanding at finance companies increased hardly at all through

Chart VI

the early 1960's and then decreased sharply after 1967. As a proportion of total loans, credit union loans increased from 20.2 percent in 1954 to 49.6 percent in 1971 compared to the finance companies' proportions of 43.4 percent and 4.8 percent in 1971. (The market share of commercial and mutual savings banks increased from 32.6 to 40.5 percent and that of the industrial banks from 3.8 to 5.1 percent over this period). These data are consistent with Tables 6 and 7 and Chart IV, which also indicate that the finance companies were not in as good a position as the Maine legislature might have believed when they passed the restrictive legislation in 1967.

The increase in credit union loans after 1967 in absolute amount and as a percentage of the total, mentioned by Commissioner Campbell and shown in Chart VI, requires some explanation. Credit unions can obtain the funds they lend (with minor exceptions) only from their members.[1] Unlike finance companies, they cannot borrow from banks or from the general public. How, then, did they obtain the increased funds? Mr. Ted Desveaux of the Maine Credit Union League believes the increase was due to an extensive advertising campaign by the credit unions.[2] Their decision to expand predated the 1967 legislation, which they did not expect to be enacted. Thus the growth of the credit unions was coincident with but essentially independent of the decline of the finance companies.

While it is clear that credit unions' (and to a lesser extent, the other institutions') share of the market increased, it is not clear that

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1. In 1969, federal credit unions in Maine had "notes payable" of $3.2 million and total assets of $82.3 million while state credit unions had borrowings of $.4 million and total assets of $22.1 million.

2. This belief is supported by evidence presented by Ryland A. Taylor, "The Demand for Credit Union Shares: A Cross-Sectional Analysis," Journal of Financial and Quantitative Analysis, VII (June 1972), 1749-56.

the amount of loans supplied equaled the amount demanded. To determine whether total loans after 1967 were at the level they would have been had not the 36 month rule been enacted, a theoretically valid supply and demand model must be constructed, specified and tested for the period before 1968. The following model was developed for this purpose.

(8) $$LD = f(RL, G, P, UR, Y)$$

(9) $$LS = g(RL, P, RB, C)$$

(10) $$LD = LS, \text{ where}$$

LD = total consumer installment cash loans demanded,

LS = total consumer cash loans supplied,

RL = rate charged on loans,

G = goods purchased with consumer credit,

P = population,

UR = unemployment,

Y = personal disposable income,

RB = borrowing rate of lenders (gross opportunity cost of lending), and

C = operating cost and risk of lending.

According to this model, consumers' demand for loans is a function of the rate they pay and their need for borrowing as determined by their purchases, unemployment and income. The amount of funds lenders supply is a function of the rate they earn and the cost of obtaining and lending funds. Population serves to account for the scale of demand and supply.

The demand equation may be written in the following linear form:

$$(11) \qquad LD_t = a_1 P_t + \sum_{h=t-n}^{t} a_h RL_h + \sum_{i=t-n}^{t} a_i G_i + \sum_{j=t-n}^{t} a_j UR_j + \sum_{k=t-n}^{t} a_k Y_k + U_t$$

where U_t is a random disturbance term and other variables are as defined above. Loans demanded at time t (LD_t), then, are a linear function of the pouplation (P) and present and past rates of charge (RL), purchases of goods, (G), unemployment (UR), and income (Y). Assuming that total loans with respect to population is homogeneous in degree one (as Chart VI shows), $a_1=1$ and all variables can be stated in terms of loans, goods purchased, etc., per capita. Assuming further that the effects on loans of past goods purchases, unemployment and income are impounded in the beginning level of loans outstanding (for each period, loans supplied = loans demanded), equation (11) can be rewritten, either in total or per capita form, as:

$$(12) \qquad LD_t = a_o LO_{t-1} + a_1 \Delta RL + a_2 \Delta G_t + a_3 \Delta UR_t + a_4 \Delta Y_t, \text{ where}$$

LO_{t-1} = loans outstanding at the end of the previous period, and

Δ = change.

The supply equation (9) also can be written in linear form (in total or per capita) as:

$$(13) \qquad LS_t = \sum_{h=t-n}^{t} b_h RL_h + \sum_{i=t-n}^{t} b_i RB_i + \sum_{j=t-n}^{t} b_j C_j + V_t$$

where V_t is a random disturbance term and other variables are as defined above.

The amount of loans supplied, then, is a linear function of past and present lending rates, borrowing rates and lending costs. As is assumed for the demand equation, past rates and costs are impounded in past levels of lending, so that equation 13 can be rewritten as:

$$(14) \qquad LS_t = b_o LO_{t-1} + b_1 \Delta RL_t + b_2 RB_t + b_3 C_t + V_t.$$

Using two stage least squares, the equation can be solved for the common endogenous "price" variable, ΔRL_t, and then for LD_t. Unfortunately, this planned procedure could not be effected because data on RL_t are not available for banks. Further, the data on gross loan income which are available for finance companies and credit unions do not adequately measure current period charges. Consequently, the simultaneous supply and demand model had to be abandoned. Considering that simultaneous equation models rarely provide much different estimates than are given by single equation models, this limitation may not be very serious.[1]

As an alternative, the demand for consumer loans can be extended on the reasonable assumption that lenders supply the loans demanded to the class of borrowers whom they serve.[2] The rates charged borrowers differ

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1. For an example related to consumer loans, see Walter Nicholson, "A Simultaneous Model of the Demand for Consumers' Durable Goods and Consumer Credit," unpublished paper presented at the Winter Meetings of the Econometric Society, New York, December 23, 1969.

2. See Maw Lin Yee, "An Analysis of Installment Borrowing by Durable Goods Buyers," Econometrica, 30 (October 1962), 770-87; Helen M. Hunter, "A Behavioral Model of the Long Run Growth of Aggregate Consumer Credit in the United States," Review of Economics and Statistics, May 1966, 124-140; Horace J. DePodwin and Howard N. Ross, The Supply and Demand for Personal Credit in New York State, 1950-1970, Savings Bank Association of New York State (New York, 1965); and James F. Smith, The Demand for Consumer Credit Since 1948: A Dynamic Stock-Adjustment Approach, unpublished dissertation, Southern Methodist University, May, 1971.

for banks, credit unions, industrial banks, and finance companies but, except when the legal ceiling changes, usually are at the ceiling. Lenders, then, provide funds to borrowers at this rate in the amounts demanded, so long as the borrowers are within the risk class (or better) served by the lender. Thus, the volume of loans is demand determined and the rate charged, RL, being constant, is dropped from the equation. The following demand equation then was estimated:[1]

$$(15) \qquad LO_t = c_o LO_{t-1} + c_1 \Delta RV_t + c_2 \Delta UR_t + c_3 \Delta Y_t, \text{ where}$$

RV = registered vehicles, used as a proxy for goods purchased for which cash loans are taken, since cars are the single most common good purchased with the proceeds of these loans.

Since the linear form need not be the best specification, equation (14) also was estimated in logarithmic form.[2]

Equation (15) and its logarithmic counterpart were estimated with annual data for 1954 (the first year for which complete data on total consumer cash installment loans are available) through 1967. (Quarterly data are not available). The equations were specified with total and per capita amounts, but, as Chart VI indicates, there was almost no difference in the coefficients. Hence only the total loan equations are reported.

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1. A forecasting model, in which both supply and demand factors were included, could not be specified, since annual data on consumer loan costs at commercial banks in Maine are not available.

2. Equation (15) also was stated in terms of changes, in an attempt to reduce the problem of autocorrelation of the residuals. However, this form proved to have a lower Durbin-Watson statistic and higher first order autocorrelation of residuals, as well as a worse fit to the data.

The coefficients (standard errors) and t values estimated are as follows:

(15') $$LO_t = 1.109\ LO_{t-1} + .66\ \Delta RV_t - 941\ \Delta UR_t - 41.25\ \Delta Y_t$$

	(.027)	(.78)	(1602)	(41.09)
	40.78	.84	.58	1.00

$R^2 = .99$

Durbin-Watson Statistic = 1.22

First order autocorrelation of residuals = .39

(16) $$\ln LO_t = 1.013\ \ln LO_{t-1} + .13\ \Delta \ln RV_t - .11\ \Delta \ln UR_t - 2.01\ \Delta \ln Y_t$$

	(.003)	(.21)	(.10)	(1.00)
	380.8	.62	1.13	2.02

$R^2 = .98$

Durbin-Watson statistic = 1.25

First order autocorrelation of residual = .27

Only the lagged loans outstanding are significant at the .05 level in either the original or logarithmic form. Considering a less rigorous definition of "significance," the equations with variables whose coefficients are at least as great as their standard errors are:

(15'') $$LO_t = 1.089\ LO_{t-1}\ ; \quad R^2 = .98$$

(.029)

40.78

(16') $$\ln LO_t = \underset{(.002)}{1.012\ LO_{t-1}} - \underset{(.68)}{1.15\ \Delta Y_t}\ ; \quad R^2 = .98$$
$$423.9 \qquad 1.70$$

Omitting the "non-significant" variables affects the R^2 and coefficients hardly at all. Thus, it appears that loans outstanding are best stated as a function of the previous balance outstanding and possibly, in the logarithmic form, of changes in personal income.

The coefficients thus estimated with data over the period 1954-1967 were used to "predict" loans outstanding in the post-1967 years. Table 8 shows the actual and the predicted amounts of total loans for each of the four equations whose coefficients are given above. With the exception of equation 15' for 1971, the predicted amounts are greater than actual for all models and years. However, the estimated amounts are not, in all cases, significantly greater than the actual loans outstanding. "Actual" is two standard deviations or more less than "predicted" for the 1968 and 1970 original data models and the "good" 1971 original data model. The less stringent one standard deviation difference shows significantly less than predicted loans in all years for the original data models (except the 1971 all variables equation) and the "good" logarithmic equation. Thus, there is some evidence that the 36 month limitation may have resulted in a lesser amount of loans outstanding.

Table 8

However, the aggregate data and the models specified really are not adequate or sufficient to determine the effect of the radical reduction in lending by finance companies on the availability of credit to consumers.

People can borrow from many sources besides commercial and mutual savings banks, credit unions, and industrial banks -- such as trade credit, auto finance companies, second mortgage lenders, friends, loan sharks and others whose data are not available on a state wide basis. Consequently, it is not possible to conclude, as did Commissioner Campbell, that "these figures seem to prove that consumers are properly provided with credit..." or the reverse, as the demand models indicate. Rather, at the least, one must go to the individuals affected to determine the effect of the 36 month limitation.

Survey of Lenders

Commercial bankers and credit unions officials were interviewed and a survey mailed to determine whether and how the reduction in lending by finance companies affected them. While some of the bankers believed the restrictive legislation was good for consumers, most thought it unwise. Of greatest interest was their almost universal belief that they had "picked up" very little new business that they thought was formerly served by the finance companies. Bank charge cards, they said, generally would not be granted to these customers because charge cards, with which a holder can borrow on demand, present a bank with greater risk than installment loans. However, they thought that many people who borrow at finance companies could qualify for bank installment loans, if they would apply. Mr. Desveaux of the Maine Credit League believed that many former finance company customers were now served by credit unions, but he said that there were no data available to support or deny this belief. However, since credit unions can lend only to members, people who are not employed by companies with credit

unions, attend a charch that has a credit union or live in a neighborhood served by an area credit union, cannot be served.

Survey of Borrowers -- The Data

To determine directly the effect of the reduction in finance company lending on their customers, a large sample of borrowers was interviewed. In November and December, 1971, four major consumer finance companies who were shrinking and/or discontinuing their operations in Maine were asked to supply the names, telephone numbers, addresses and other information on former or present customers who had wanted to take out or increase loans (roughly) during the past year, but whose requests were refused because the company was not extending or making loans. In all cases, these were people to whom the companies would have been pleased to lend had they not decided to reduce or eliminate their operations in Maine.

Table 9 gives the composition of the sample. Names, addresses and telephone numbers of 771 borrowers were received over a period of several months. All borrowers for whom valid telephone numbers could be found were contacted.[1] In all, 436 persons were contacted at this stage of the survey.

The telephone interviews proved very satisfactory, in part because the interviewers were very good at establishing rapport. The principal interviewer was a graduate student at the University of Maine who was familiar with much of the state. After some experimentation, he developed the technique of conducting an apparently unstructured conversation of from

1. Initially, borrowers were sent a letter that informed them of the study and that they would be contacted by telephone, assured them that they would not be "sold anything," that the information gathered would be kept confidential and that the study might benefit them. The letters appeared to be ignored completely. Consequently this procedure was abandoned.

four to six minutes, during which he avoided leading the borrowers to answers, yet managed to get replies to most of the questions. When an interviewee wouldn't give information unless he or she were asked too specific questions (i.e., "Why did you want to borrow money?" No reply until the interviewer had to say -- "To buy a car?") and then seemed to be answering to please or get rid of the interviewer, the interview was marked "refused to respond." Most in this group include people who simply wouldn't speak to the interviewer. Of the 436 people contacted, 58 (13.3 percent) refused to answer and 378 (76.6 percent) gave the requested information. The interviewers believe that they received valid answers to their questions, with one exception -- "What percentage amount of loan was outstanding when you attempted to renew your loan?" Many interviewees gave vague replies which indicated that they either really did not know the amount or did not understand the question.

The 436 borrowers contacted represent 56.6 percent of the sample. It would be potentially misleading to assume that the persons not contacted are like those contacted; their not having locatable telephone numbers might be an indication that inability to borrow additionally from the finance companies put them in a particularly difficult financial situation. Consequently, a sample of 82 (24.2 percent) of the 335 borrowers not contacted was selected. (The sub-sample comprised all borrowers in several towns). The last known home and work addresses of these borrowers was obtained, from which they were located (eventually) and interviewed. All of these borrowers were interviewed (although this proved quite time consuming). Thus a control against the 253 persons not contacted was established.

The principal question asked the borrowers was whether or not they were able to obtain the funds for which they had gone to the finance companies. To ascertain which characteristics were associated with ability or inability to get funds, data on the borrowers was obtained from the finance companies, as follows: occupation, weekly gross salary, age, marital status, number of dependents, number of years the borrower was continually in debt to the finance company, and number of previous loans the borrower had with the finance company.

The data first are used to determine whether or not the 67.2 percent of the sample contacted are representative of the entire sample. Tables 10 through 14 give the percentages of each sample in the subcategories for which information was gathered. The number of observations for which valid data were available also is given, as are the number and percentages of each sample for which data were not available. Table 15 gives the chi square statistics (which measure the probability that the differences are not due to chance) computed from two way comparisons of the samples. The chi square statistics show no significant[1] differences in any of the characteristics measured between the poeple who answered the initial telephone survey (A) and those who refused (R), between those who answered the initial telephone survey (A) and those who were contacted by field interviews (C), and

Table 10
Table 11
Table 12
Table 13
Table 14
Table 15

1. A measured chi square statistic as large or larger than that at the five percent level of significance indicates that the relationship measured could have occured by chance no more than five times in a hundred. Thus, in Table 15, the measured chi square for occupation between the A vs. R. samples of 2.48 compared to the chi square at the 5 percent level of 11.10 is considered evidence of an "insignificant" difference in the occupations of borrowers in the two groups.

between those not initially reached by telephone who later were contacted (C) or not contacted (N). Only those who answered the initial survey (A) and those not contacted (N) showed significant differences in several respects. The most striking of the differences are as follows: those not contacted include a slightly higher percentage of unskilled and much higher percentage of professional workers (see Table 10), they earn somewhat less (see Table 11), and have a higher percentage of single persons and fewer dependents (see Table 13). Of greatest interest for this study, they do not differ much in number of years in debt or previous loans. Consequently, it is concluded that the 460 borrowers interviewed, on which the balance of this and the next two sections are based, represent the entire sample of 771 well.

Ability to Borrow and Source of Funds of Individuals Surveyed

Table 16 shows that almost exactly half the borrowers were able to obtain funds (A) from other sources and half were unable to obtain new funds (U). This table and Table 18 report on differences between the two groups to ascertain why some borrowers could get funds and others not. Considering the reason for borrowing first, Table 16 shows that a greater percentage of those able to obtain funds wanted the money to consolidate debts (54.5 vs. 48.9 percent) or buy a used car (19.5 vs. 12.7), while the percentage of those wanting to purchase furniture and household items was highest for the "unable to obtain funds" group (10.0 vs. 5.6 percent). The percentages of what some might view "socially acceptable purposes," -- to pay medical bills, make home improvements and pay school expenses -- were about the same for each group. At the least, there seems no evidence that those unable to obtain funds wanted the money for obviously "less worthy" purposes.

Table 18 gives the chi-square statistics for each of the seven characteristics reviewed above as well as for the percent of loan unpaid at the time the borrower wanted additional funds (5 categories) and reason for borrowing. (Groups other than the able (A) vs. unable (U) to obtain funds groups are discussed below). Chi square statistics rather than the underlying data are reported since the only significant difference between those who were able (A) and unable (U) to obtain funds is the "reason for borrowing," which is detailed in Table 16. Thus (contrary to expectations), the explanation of why some borrowers could and some could not obtain funds is not discernable from the data collected. The interviewers were unable to say

whether the people who could not borrow tried to borrow but were refused, could not find another institution in their area from whom to borrow (such as a credit union from which they were eligible to borrow), gave up trying after being told that the finance company would not advance them funds ("if they wouldn't lend to me, who would?"), or bought more goods on credit but did not consider this "borrowing."

Those able to obtain funds were queried about the source of their borrowings. The greatest proportion (39.8 percent) shifted their debt to another finance company, which shows that the 36 month rule was not entirely effective. Banks provided loans to 22.9 percent, 20.8 percent borrowed from a credit union and the balance of 6.5 percent from other sources. None admitted borrowing from a loan shark. Recalling that few of the bankers interviewed and surveyed thought that they had gotten much new business from former finance company borrowers, it may be that these people were considered by bankers to be sufficiently good risks to be not classified as "finance company clients."

Those unable to obtain funds took one of three actions. Most continued to pay regularly (77.3 percent) while almost all of the balance missed some payments but paid off the loan (22.3 percent). Only one person (.4 percent) declared bankruptcy.

Borrowers' Feelings about Not Having Been Granted a Loan by the Finance Company

The people interviewed also were asked how they felt about no longer being able to borrow from the finance company. Questions of this sort always must be treated with skepticism and interpreted with great care, since feelings are difficult to measure and people often answer according to how they

think they should feel. This caveat is especially necessary when interpreting feelings about borrowing. Borrowers, no less than law makers, often regard being in debt (particularly from "lenders of last resort") as "bad." A good illustration of this is provided in an interview study of 101 people who were at that time borrowers from small loan companies.[1] the interviewers did not know this fact and, during the course of the interview, asked how many cash loans and installment purchases the interviewee had outstanding at the time of the interview (unfortunately, the two types of debt were grouped). Eleven percent of those interviewed said they had no loans, 23 percent said they had one, 28 percent said they had three, etc. Thus at least 11 percent (and possibly 34 percent) reported no loans outstanding although they were then in debt to a finance company.

In the present study, the interviewers put the answers as to "feelings" into the categories reported in Table 17. Of those able to obtain funds, Table 17 74.1 percent felt better off, primarily because they established credit with a "better quality" financial institution (80.2 percent of the 74.1 percent). Most of the balance felt better off because they were "rid of the burden of the finance company." It is easily understandable that people who find that they can borrow for a lower interest charge at an institution with more "class" feel better. It is interesting that most of the few who felt worse off even though they did find funds elsewhere (7.0 percent) said that they still found themselves under the burden of a financial institution --

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1. John B. Lansing, Gerald P. Ginsburg, and Kaisa Braaten, "A Pilot Study of Characteristics of People who Borrow Cash from Small Loan Companies," Survey Research Center, Institute for Social Research, University of Michigan, December 1957, mimeographed.

that debt was too easy to get. The remaining 19.1 percent who were able to obtain funds said they felt about the same, half because they still were in debt and a little less than half because they borrowed from another finance company.

It is interesting to find that 36.3 percent of those who were unable to obtain funds said they felt better, primarily because they were "rid of the burden of the finance company." The balance declared that finance companies are a "necessary evil," so having paid off their debt, they felt better. Most of those who felt worse blamed their condition on having borrowed from a finance company in the first place, which required them to pay off the loans. Only 11.4 percent of those who were unable to obtain funds (5.7 percent of the total) felt worse because there were no other alternatives available to them.

The characteristics (occupation, salary, age, marital status, number of dependents, years in debt, number of previous loans, percent of loan unpaid and reason for borrowing) of those who felt better (B), worse (W) or the same (S) were compared to ascertain if any of these were related to the feeling expressed. Table 18 gives the chi square statistics computed for these groups. Age for the B vs. W comparison is the only characteristic that is significantly different between the groups. The principal difference is that the B group is older; 3.3 percent are between 18 and 24 compared to 15.9 percent for the W group.

Table 18

Chi square statistics that measure the significance of differences in the characteristics of those who were able to obtain funds who felt better (B), worse (W) or the same (S) are given in Table 19. Only salary in the B vs. S comparison, occupation in the W vs. S comparison, and source of

Table 19

funds in the B vs. W and B vs. S comparisons are significantly different. The difference in salaries between the B and W groups is in the lowest category -- $0 - $80 a week. The B group had 9.9 percent of its valid observations in this category compared to 30.8 percent for the W group. With respect to occupation, a greater percentage of those who felt worse (W) are white collar workers (30.8 compared to 2.6) and a greater percentage of those who felt about the same (S) are unskilled (39.5 compared to 7.7). The other differences in occupation indicate that "higher status" workers were less content with the changed situation than were those with "lower status" jobs. Thus the people who felt worse off even though they were able to obtain funds otherwise appear to be lower paid white collar workers.

The source of the very large chi square differences with respect to source of funds are analysed further in Table 20. Not surprisingly, the significant chi square statistic is due to the fact that 93.8 percent of the borrowers who felt worse off borrowed predominantly from another finance company while 67.8 of the borrowers who felt better off obtained funds from banks or credit unions.

<Table 20

Table 21 gives the chi square statistics for differences in the characteristics (occupation, salary, age, etc.) of those who were unable to obtain funds according to their feelings about the situation. The only significant differences are in comparisons of years in debt of those who felt better (B) vs. worse (W) and action taken of B vs. W and W vs. S (felt the same). The major differences with respect to years in debt are in the proportions who were in debt three or fewer years. However, the pattern of difference is erratic. The percentages for 1, 2 and 3 years in debt for the B vs. W groups are: 2.8 vs. 17.6, 50.7 vs. 37.8 and 24.9 vs. 16.2. Considering

<Table 21

that 77.4 vs. 71.7 are the B vs. W percentages for 3 years and under, it is doubtful if the differences are meaningful.

The feelings of those who were unable to obtain funds is analysed with respect to their actions in Table 22. Most of those who felt better (81.9 percent) continued to pay on their loan, compared to 62.7 percent of those who felt worse and 90.5 percent of those who felt the same. That 37.3 percent of those who felt worse missed payments but paid off the loan probably indicates the difficulty they experienced in repaying their debt -- hence their negative feelings. Overall, 77.3 percent of those who could not obtain funds continued to pay regularly while 22.3 percent missed some payments but paid off the loan. Only one person declared bankruptcy.

How should the data on "feelings" be interpreted? First it should be recalled that the borrowers were interviewed at about the time when they had managed to repay their loans to the finance companies. After perhaps much struggle and privation, some were out of debt for the first time in years. At this point, they are likely to be pleased that they were unable to have borrowed a year or two ago. Second, many borrowers, particularly those from the New England state of Maine, may be somewhat ashamed of being in debt, particularly from lenders whom they and others regard as higher cost lenders of last resort. Third, it should be recalled that the borrowers interviewed were finance company customers in good standing. People who had not previously been customers of the companies but who wanted to take out loans were not interviewed because records on them are not available. Consequently, nothing is known about their feelings about not having the alternative of borrowing from a finance company. For these reasons (and others given below), I interpret the predominent belief of borrowers that they "felt

better" (Table 17), not as support for closing down small loan companies, but as an indication of the relief that many borrowers feel in being out of debt or at borrowing at lower than previous rates. The implications of this and alternative interpretations are considered further below.

The "hard data" revealed by the survey allow firmer conclusions to be drawn. Half of the former finance company borrowers were unable to obtain funds elsewhere and 20.0 percent simply borrowed from another finance company. Only 27.0 percent of the former borrowers were able to obtain funds at lower rates than they otherwise would have paid (30.0 percent if loans from relatives and friends are included). Thus, it appears that not all those unable to borrow from finance companies were otherwise accomodated.

Characteristics of Long and Short Term Borrowers

The 36 month limitation was enacted in the belief that long term borrowers need protection from the finance companies and from themselves. In-depth psychological, economic, and sociological studies of long term borrowers would be desirable to determine whether the legislation is, in fact, wanted by and helpful to them. Unfortunately, such studies not only are very expensive to make, but difficult to interpret. However, the economic and other measurable characteristics of long term borrowers can be compared to those of shorter-term borrowers to determine what characterizes people presumed to be in need of protection. Data on the sample of borrowers surveyed, described above, is used for this analysis.

Table 23 shows the occupations of borrowers who were in debt to a finance company continuously for 1, 2-4, 5-8, 9-12 and 13+ years or who had 1, 2-4, 5-8 or 9+ previous loans. The data are presented as percentages of

<Table 23

the total number of each grouping of years in debt or previous loans (1, 2-4, etc.). However, since there are an uneven number of borrowers in the different occupation categories (a greater proportion of finance company customers are skilled and semi-skilled or unskilled workers than are white collar workers, etc.), the percentages should be compared to the percentage distribution of the sample (given in the first column).[1] Table 23 shows that unskilled workers comprise a greater percentage of short term (one year in debt or one previous loan) borrowers than would be expected by their numbers in the sample. Relatively more skilled and semi-skilled workers are longer term borrowers. Borrowers in the other occupation groups do not exhibit any particularly marked relationship to term of indebtedness. Taken as a whole, the chi square statistics computed indicate that the relationships between occupation and number of years of continuous indebtedness and number of previous loans are not significantly different (at the 5 percent level) than would be expected by chance.

Table 24 presents a similar analysis for five categories of weekly gross salary. With respect to number of years continuously in debt, the percentages show a slight tendency for the borrowers with incomes of $81 to $120 a week to be longer term borrowers, while those making $161 to $200 a week appear to be shorter term borrowers. However, the overall relationship between salary and years in debt is not strong, as indicated by the non-significant, rather low value of the chi square statistic. With respect to the number of previous loans, poorer borrowers (those making less than $80

1. The percentage distributions of the sample are weighted averages of the percentages in the number of years or loans rows, the weights being the percentage of each number of years or loans grouping to the total. These percentages are given at the foot of the columns.

a week) had a much higher than proportionate percentage of only one previous loan. In contrast, the highest paid group (those making $200 a week or more) had a somewhat greater proportion of previous loans.[1] The middle salaried groups show no special relationship to number of previous loans. Consequently, the chi square statistic indicates that, on the whole, salary is not significantly related to number of previous loans.

In contrast, age and previous indebtedness to the finance company is highly significantly related, as indicated by the large chi square statistics reported in Table 25. This relationship hardly is surprising, since young borrowers cannot have been in debt for very long. As Table 25 shows, relatively few borrowers in the 18 to 24 age bracket had been in debt more than four years or had more than one previous loan. Borrowers in the next age bracket (25-34), who represent about a quarter of the sample, also were in debt relatively fewer years than the older borrowers. The long term borrowers are those between 45 and 64 years of age. These data indicate that long term borrowers started with the loan company in their thirties, perhaps after they found it difficult to manage their finances otherwise.

Table 25

It would seem that married people would tend to be longer term borrowers than those who are single, divorced or widowed, since their need for funds is greater. However, as Table 26 shows, such is not the case. While the relationship between marital status and previous indebtedness is not significant, it appears that married people have a proportionately greater share

Table 26

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1. It is interesting to note that this group is not characterized by a much greater number of years in debt than expected, which indicates that they may have rewritten their loans more often.

of one year debt and one previous loan than do the others.

The relationship between the number of dependents and previous borrowings/is consistent with that of marital status. shown in Table 27 Borrowers with no dependents comprise a far greater proportion of long term debtors (13+ years previously in debt or 9+ loans) and those with three or more dependents a lesser proportion than do the others. The overall relationship, however, is not significant. Thus, it appears that short term debtors are more likely to be single or married people with three or more dependents. <Table 27

Table 28 shows the relationship between the borrower's primary reason for borrowing and his/her previous indebtedness. <Table 28 Borrowers who wanted funds to consolidate debts were proportionately more heavily represented in the 13+ previous loan group, but do not have a much different than expected number of previous loans. Those who wanted money for a used car or school related expense do not show any special pattern of previous indebtedness. Both groups of borrowers tend to have much lower than expected percentages of more than nine previous loans or years in debt. In addition, borrowers who wanted money for medical bills show higher than the expected proportion of one year in debt and one previous loan. These data are consistent with the common sense belief that borrowers who want money for immediate needs are shorter term debtors than those who want money for longer term purposes.

Finally, previous indebtedness is related to the borrowers' feelings about not having been able to borrow from the finance company. As Table 29 shows, less than a proportionate number of very short term (one year in debt, one previous loan) borrowers tended to feel better off, perhaps indicating

that they were pleased with their new relationship with the finance company. However, as the chi square statistics indicate, the relationship over all is not significant.

In summary, long term borrowers (those continually in debt for 9 or more years = CD, or those who had 9 or more previous loans = PL) tend to be skilled workers (CD and PL), people who make $200 or more per week (PL), in age between 45 and 64 (CD and PL), people with no dependents (CD and PL), and borrowers who wanted the money to consolidate debts (PL). The long term borrowers appear not to be professional workers (CD), people making less than $80 a week (PL), and those under 34 years of age (CD and PL). Very long term debtors (those in debt continuously for 13 or more years) particularly include fewer than expected borrowers with three or more dependents and those who wanted money for medical bills and furniture and home improvements. Short term debtors (those continuously in debt for less than four years = CD, or with one previous loan = PL) tend to be unskilled workers (CD and PL), people earning less than $80 a week (PL), those under 24 (CD and PL, 34 for CD), married borrowers (CD and PL), people with five and over dependents (CD and PL), and those whose primary reason for borrowing was to pay medical bills (CD and PL). Short term borrowers appear not to be skilled and semi-skilled workers and white collar workers (CD and PL), people making over $161 a week (PL), those between 45 and 64 years of age (CD and PL), unmarried people, and those with one or no dependents (CD and PL).

The portrait of the long term borrower that emerges from the data reviewed is not consistent with the view that they are of a homogeneous group who are ill equipped to handle their financial affairs. Rather their occupations,

salaries, marital status, number of dependents, and stated reasons for borrowing show that they are diverse. Only age is significantly (and obviously) related to previous indebtedness. Further, the relationship between the borrowers' characteristics and whether they are short or long term borrowers that are shown by the data are consistent with the portrait of borrowers as rational consumers whose debts reflect their economic and family positions and need for credit. As a further test of whether long term indebtedness is "bad" for consumers and/or society, the relationship between such borrowing and bankruptcies is considered next.

Long Term Borrowing and Bankruptcy

Concern over the number of personal bankruptcies filed in Maine was an important reason for the enactment of the 36 month rule. In a speech supporting the legislation on April 5, 1967, Senator Peter Mills said:

> The real question, however, is why do people become so indebted that they cannot meet their monthly payments and, therefore, are compelled to file bankruptcy. The main reason for this is the:
>
> (a) high cost of credit
> (b) on unreasonable large indebtedness
> (c) for long periods of time. [capitals in original a, b and c]

Referee in Bankruptcy Poulos also considers long term indebtedness an important cause of bankruptcies,[1] perhaps because he comes in direct and frequent contact with those who declare bankruptcy and their creditors.

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1. See last sentence of quote on page 2 above.

Aside from the important philosophical (and empirical) question of whether bankruptcy is detrimental to consumer welfare, the preliminary question to be answered is whether long term indebtedness is associated with (or a causal factor of) bankruptcies. Some data on this question were gathered by Referee Poulos from 351 bankruptcy cases on file as of June 13, 1972, in which a particular finance company was the principal creditor. Referee Poulos' staff analysed the files available to them and determined the number of times the loan in question had previously been rewritten (with or without an additional cash advance). This determination could be made for 90 of these loans. Table 30 gives the number and percentage of the number of rewrites of this total compared to similar data, from the same company, of borrowers who were included in the sample described above. It is clear from Table 30 that the people who declared bankruptcy had renewed their loans far fewer times than those who were considered good customers by the finance company and who, when credit was cut off, did not declare bankruptcy. Thus the available data are contrary to the belief that long term indebtedness is associated with bankruptcy and hence is unlikely to be a causal factor of bankruptcy. Rather, as several studies have shown, bankruptcy appears related to harsh wage garnishments and unexpected costly medical problems, job losses and marriage failures.[1]

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1. See David T. Stanley and Marjorie Girth, Bankruptcy: Problem, Process, Reform, The Brookings Institution (Washington, D. C., 1971); and Philip Shuchman and Gerald R. Jantscher, "Effects of the Federal Minimum Exemption from Wage Garnishments on Nonbusiness Bankruptcy Rates," Commercial Law Journal, November 1972, 360-3.

Summary and Recapitulation

This study analyses the arguments for and against allowing finance companies to lend originally or extend a loan for more than 36 months without incurring the severe penalty of having the interest rate charged on the unpaid balance limited to 8 percent simple. Maine passed such a law in 1967, in large measure because the legislators and others ("regulators") believed that long term indebtedness to high interest rate lenders resulted in a form of "economic slavery." The regulators' arguments are based on a belief that borrowers either are not good judges of the future effect of their present action of borrowing and/or are enticed into long term, high rate borrowing by finance companies, from which they cannot extricate themselves. Those opposed to the legislative ("anti-regulators") beleive that consumers can and do make rational borrowing decisions and that, in any event, the finance companies simply respond to rather than create demands for credit. Aside from this basic perceptual disagreement, the regulators and anti-regulators disagree about the effect of the legislation on the availability of credit in the state.

There is no doubt that the number of finance companies and offices operating in Maine declined drastically since the 36 month rule was passed in 1967, as shown by Chart I and Tables 1 and 2. The Chart also provides a test of the regulators' hypothesis that national companies left the state deliberately to show other states what would happen should they pass a law such as that enacted in Maine. The equivalent decline in the number of local companies and offices (who could not benefit from such an action) and national companies and offices is contrary to the hypothesis.

The virtual elimination of finance companies as lenders in Maine is explained best with an analysis of their operations and costs. In deciding whether to lend to a potential customer, the companies consider the profitability of the entire relationship. The net cash flow from subsequent as well as the first loan is discounted. To an extent (smaller than expected), lending to new borrowers is more costly than lending to present or former borrowers. The major advantages in a long term relationship seem to rest on a reduction in losses by permitting a customer to extend payments and in the fact that longer-term borrowers generally have larger outstanding balances than new borrowers. The finance companies provide customers with "personalized" service: the loan office managers know their clients individually and learn to judge how much debt the clients can carry. When a borrower gets behind in payments, perhaps because he has lost his job or had an unexpected expense, the manager can reduce the required payment by extending the debt. He also may lend the borrower an additional amount, to "tide him over." With the 36 month limitation in effect, such extensions become prohibitively unprofitable and losses mount.

The other aspect of finance company operations is that loans to new and one time borrowers often are not profitable. The companies' operating costs are a function primarily of the number rather than the amount of loans they service; thus making and processing a $400 loan costs about as much per year as a $700 loan. Consequently, the rate ceilings allowable in Maine (particularly since the ceiling on loans under $150 was lowered in 1967) do not provide enough revenue to make loans of less than $300 to $400 profitable. But new customers generally borrow less than present customers who increase and/or

extend their loans. In 1966, new loans in Maine averaged $447 compared to $718 for loans to present borrowers. Hence, a customer relationship often is profitable only if the companies can expect that a fairly large percentage of new customers will borrow additional amounts in the future. With the 36 month limitation in effect, this expectation is removed.

The data analyzed are consistent with these explanations. The loss rate in Maine averaged 2.2 percent before the 36 month limitation was enacted in 1967: in 1968 it was 3.25 and in 1969 (the latest year for which these data are available), 4.10 percent. The average cost per loan computed was $56 in the early 1960's, $70 in the middle 1960's and $82 in the later 1960's (Table 5). As Chart II shows, these costs make loans under $240 unprofitable without consideration of interest, losses, income taxes, and return on capital. Further evidence is derived from the fact that when the ceiling rate on loans under $150 was dropped from 36 to 30 percent in 1967, the companies virtually ceased making loans under $100 in size (Chart III). Also, the average size of a new loan made in Maine after 1967 was about equal to the size of a loan made to a present customer (Chart IV).

It has been claimed, on the one hand, that the companies were sufficiently profitable to absorb the costs of the ceiling rate reduction and the 36 month limitation and, on the other, that they would have left Maine anyway since the size of office they could operate was not economical (economies of scale are assumed). Calculation of the companies' rate of return on assets (Chart V and Tables 6 and 7) show that they hardly could be described as "very profitable." Nor do the data give any evidence of

economies of scale (Table 4). However, the data do show that the companies' share of the market and amount of loans was declining before 1967 (Chart VI). A major reason for this decline was the increase in their operating costs and in the cost of money and the rigid ceiling on interest rates they could charge, which resulted in a decline in their rate of return. Thus, the effect of the 36 month limitation together with the ceiling rate reduction (and perhaps the actions of the Referee in Bankruptcy, Mr. Poulos, in reducing their income from insurance and recoveries of bad debts) resulted in a decline in profitability that forced the companies to reduce and eventually cease operations in Maine.

The effect of the reduction in finance company lending, in the aggregate, appears to be reflected in a lower amount of loan dollars supplied relative to the amounts demanded, particularly in 1968, 1969 and 1970 (Table 8). Much of the apparent increase in the amount of loans supplied is due to changes in the price level since 1967 that inflate the figures. Nevertheless, the increase in loans made by credit unions (and, to a much lesser extent, by banks), do offset loans not made by finance companies, in the aggregate. However, the aggregate data are not adequate to determine whether those who otherwise would have borrowed at finance companies were served by other lenders. Therefore, a survey of these people was undertaken.

Four hundred sixty people, good customers of finance companies who wanted to borrow but to whom the companies would not lend because of reduced operations in Maine, were surveyed. Half were unable to obtain funds elsewhere. Of the other half, 40 percent borrowed from other finance companies, 33 percent from banks, 31 percent from credit unions, and 6 percent from other sources. (None admitted borrowing from loan sharks.)

Those who could and could not otherwise obtain funds did not differ significantly in such characteristics as occupation, salary, age, marital status, number of dependents, percent of loan unpaid at the time, and years in debt and previous loans to the finance company (Table 18). The only statistically significant difference was in the reason for borrowing: a higher percentage of those who were able to obtain funds wanted them to consolidate debts or buy a used car while relatively more of those who could not obtain funds wanted money to buy furniture and household items (Table 16). Thus, there do not appear to be any obvious (or at least, tested for) reasons for half of those surveyed having been able to borrow compared to the half who couldn't.

The sources of funds for the half who could obtain them were other finance companies (40 percent), banks (23 percent), credit unions (21 percent) and others (6 percent). No one admitted borrowing from loan sharks. Most (77 percent) of the half who couldn't obtain funds paid off their loans regularly, while the balance (except for one person who declared bankruptcy), missed some payments in paying off their loans.

When asked their feelings about the situation (Table 17), 55 percent of the people surveyed said they "felt better," primarily because they were "rid of the burden of the finance company" or were borrowing from a "better institution." Twenty-two percent said they felt worse and 23 percent said they felt about the same. Of the total only 6 percent said they felt worse because "there was no other alternative available." Tests of differences among the interviewees according to their feelings about not being able to borrow from the finance company revealed no significant differences (Table 18). In interpreting these findings, one should recognize that

people who borrow from what they know to be high cost "lenders of last resort" are not proud of their situation. They were surveyed at about the time that they had managed to pay off their loans or made other, often preferable, arrangements. The pain of repayment was past and the pleasure of freedom from debt prevailed.

The occupations, salaries, age, marital status, number of dependents, and reason for borrowing of long and short term debtors were compared to determine whether long term borrowers are a group that appears in need of state protection. No statistically significant differences were found in these comparisons (Tables 23-29). The differences that did emerge show long term borrowers to be a diverse group whose period of indebtedness seems to reflect rationally their economic and family positions and need for credit.

Finally, the belief of regulators that long term indebtedness results in bankruptcy was tested. The number of loans previously made to people who subsequently declared bankruptcy was compared to the number made to customers of the same company whom they considered to be good risks (none of whom, in fact, went bankrupt when the company did not extend further credit to them) (Table 30). The percentage of long term borrowers was far greater among those who did not compared to those who did declare bankruptcy. In fact, the majority of bankrupts were relatively new customers of the company.

Policy Conclusions

It seems clear that, regardless of its intended purpose, the 36 month limitation was a prime causal factor of most finance companies leaving the state of Maine. Their leaving appears to be the result of the rate ceiling

imposed by the state, which makes the revenue derivable from small loans less than the associated operating costs, and on the 36 month limitation, which makes a compensating long term relationship impossible. As a consequence, many people who want to borrow small amounts are not served and loans under $100 are rarely made. Half of the borrowers surveyed who previously were considered good customers of the finance companies were unable to obtain funds when they wanted them.

"But," regulators might argue, "on balance this is a good situation. Even most of those who could not obtain funds felt better off." In part this objection is valid and in part not. First, people who had not been good borrowers from finance companies were not surveyed. The companies usually serve people who, because of their occupation, salary, age, race, and lack of previous credit record, are not considered good credit risks. The data show that the companies' cost of operations are very high, primarily because they much "work with" people who are not very good at amanging their financial affairs by themselves. To an important extent, companies provide their clients with personal financial management, for which they charge what appear to be high interest rates. Where will these potential borrowers go should the finance companies not be in business? Banks cannot afford to provide this service; credit unions may, if the borrowers are members. The ability of credit unions, though, to provide service at lower cost than finance companies depends on their limiting their clientele to qualified members. Unlike finance companies, credit unions can benefit from volunteer help and donated quarters to reduce operating costs and the social pressure

of a close affinity group and/or automatic deductions from wages to encourage repayment. What of those to whom credit union membership is not available?

Collaterally, would even the 27 percent of the former finance company customers surveyed who were able to borrow the funds they wanted from banks and credit unions been accepted by these institutions had they not established good credit records by previous borrowing from a finance company? The law that "forced" these borrowers to go to lower cost lenders probably benefited most of them, since otherwise they might have continued to borrow at much higher rates at the finance companies in the belief that banks and credit unions wouldn't give them credit, even though some of these people may find the alternative institutions not as flexible or personal in meeting their needs as they might wish. However, the banks and credit unions are unlikely to offer credit to new borrowers who appear to lack the discipline or ability to handle credit. How will these people be able to establish a favorable credit rating? How can they "graduate" from finance companies to lower cost lenders if the finance companies don't exist?

Second, is the 36 month rule really effective? The data show that most companies in Maine did cease or reduce and change their operations as a result. But some others seem to have evaded the law. Of those former finance company customers surveyed who were able to obtain funds, 40 percent borrowed from other finance companies. Many interviewees said they were told to give their present company a check to repay their loan on one day and borrow the next day from company X. They needn't worry about the

check "bouncing," since the first company wouldn't "get around" to depositing it for several days. This trading of customers between companies effectively nullifies the 36 month limitation, though at some cost and risk to the companies and, therefore, to their clients.

It should be emphasized, however, that the decline in the number of finance company dollars of loans outstanding indicates that the evasion was quite limited in scope. Two factors may explain the general inability or unwillingness of finance companies to evade the law. One is the fear of being caught; Mr. Poulos, the Referee in Bankruptcy, is an able and tenacious supporter of the law whom the finance companies have reason to fear. The other is the past competitive nature of the industry which makes it difficult for rival companies to "cooperate" in sending each other their good customers. However, if the situation in Maine in the future follows the pattern of regulations in most states, the zealous supporters of legislation will shift their attention to other concerns and companies will overcome their past rivalry in favor of collusion.

Third, will people who have paid off loans or not made them remain out of debt if finance companies do not exist to serve them? One should recall that small loan legislation was passed in 1916 to allow lenders to provide money at higher than the usual usury rates when it finally became obvious that people were borrowing from loan sharks who exacted a far higher toll than would have been charged by legal lenders. While no evidence of loan sharking was found in the survey done for this study, the experience of other states and times speaks otherwise. But even if illegal lenders do not take the place of the finance companies, people still will have to pay for the credit they demand. Studies of the effect of severe

usury laws on prices and credit provide evidence of what happens when laws make normal lending impossible. Arkansas has a rigidly enforced 10 percent simple usury law, with no provision for small loans (the Small Loan Act was repealed in 1954). A very careful study of the effect of this law by George C. Lynch[1] shows clearly and conclusively that, as a result, non-locally produced goods cost more in Arkansas than in comparable out-of-state areas since retailers raise their prices to compensate for excess credit costs. Consequently, people who pay cash for goods are penalized, as are retailers located in towns near other states where other retailers can offer lower prices to cash customers. If people who borrow do so because they wish to buy goods or services or meet what they consider to be necessary obligations, the absence of finance companies cannot prevent merchants from raising their prices. Cash customers must pay for credit they don't want and people who want credit must purchase goods from a specific merchant: both groups pay more.

Finally, what of the argument that finance companies keep people in debt by "forcing money on them"? No doubt this claim is true for some people and some lenders. People who are impulse buyers, who must achieve instant gratification, or who cannot withstand temptation can be taken advantage of. Unfortunately, perhaps, prohibition never before has been a successful remedy for similar maladies. Drunks rarely are reformed for

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1. George C. Lynch, "Consumer Credit at Ten Percent Simple: The Arkansas Case," Law Forum, University of Illinois, 1968, pp. 592-618.

long by closing the bars and liquor stores. Nor does it seem fair to penalize those who can handle credit for the shortcomings of those who can't.

Several salutory changes can be made, however. First, the 36 month limitation should be repealed. Second, the ceiling rate on small loans should be restated to allow lenders a return that makes providing small loans worthwhile. The ceiling should be stated as an amount per loan to cover operations costs plus a rate per dollar to cover interest, risk and capital costs. The data presented in this study suggest about $80 to $90 per loan and, perhaps, 12 to 15 percent per dollar. Since renewals are somewhat less expensive for lenders and if emphasis on loan renewals by finance companies is not to be encouraged, the allowable amount for a renewal might be $70 to $80. These amounts should be tied to and automatically adjusted by a price level index (such as the GNP deflator) and and an interest rate index (such as the rate on finance company loans reported in the Federal Reserve Bulletin). Third, some possible abuses should be corrected. One is that the creditors' defense of fraud in bankruptcy proceedings might be disallowed, as suggested in a comprehensive study by Philip Shuchman.[1] Another is removal of the limitation that a consumer can declare bankruptcy only once in six years. The present limitation makes it desirable for lenders to extend possibly improvident loans to people who have just completed bankruptcy.[2] These changes (and the

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1. Philip Shuchman, "The Fraud Exception in Consumer Bankruptcy," Stanford Law Review, 23 (April 1971), 735-73.

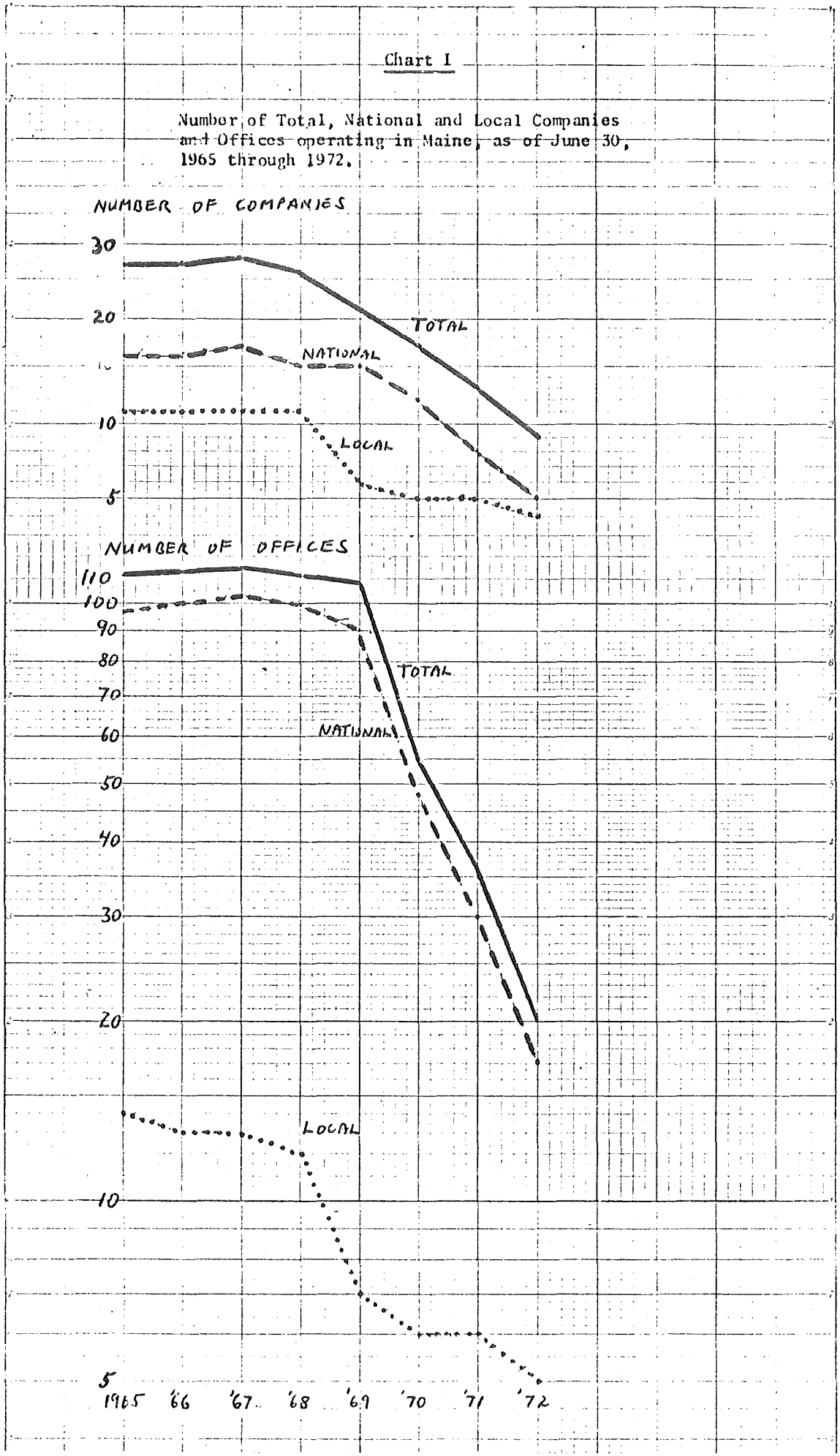
2. See analysis and proposals by Conrad K. Cyr, Referee in Bankruptcy, Bangor, Maine, "Single Claim Jurisdiction for the United States Court of Consumer Affairs: An Interim Proposal for Relevant Regulation of Consumer Credit," unpublished, undated paper.

others recently enacted that eliminated debtors prison and holder in due course defenses) should make it easier for borrowers to be relieved of debts that they cannot carry and put creditors on notice that over-burdening debtors is not profitable. But, creditors also should be allowed to have the debtor voluntarily agree to automatic loan repayments by means of payroll deductions, such as are available to credit unions. At the same time, credit unions should be allowed to offer loans to much wider groups. This competition among lenders can serve to provide borrowers with better and less expensive servite.

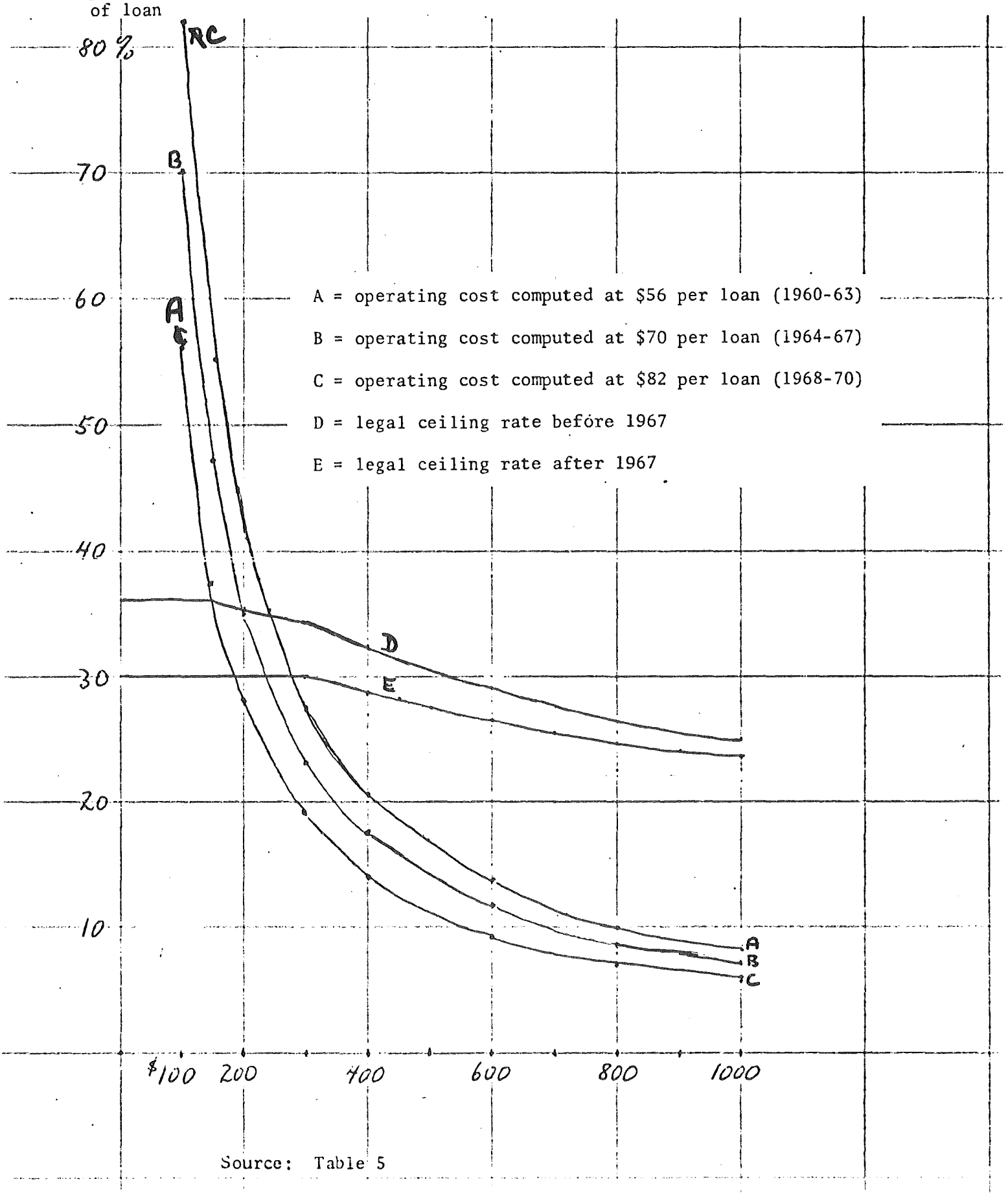
Finally, those people who are unable to manage their affairs need help, much as do alcoholics. Organizations such as the Credit Counseling Centers should be encouraged and supported. Other direct aid to the poor and ignorant, such as education about the costs of borrowing and the value of saving might be offered by government. But, in a free society, this type of help and the fair enforcement of laws should be the extent and limit of governmental "concern."

Chart I

Number of Total, National and Local Companies and Offices operating in Maine, as of June 30, 1965 through 1972.



Average Operating Costs and Legal Ceiling Rates per Dollars of Loans

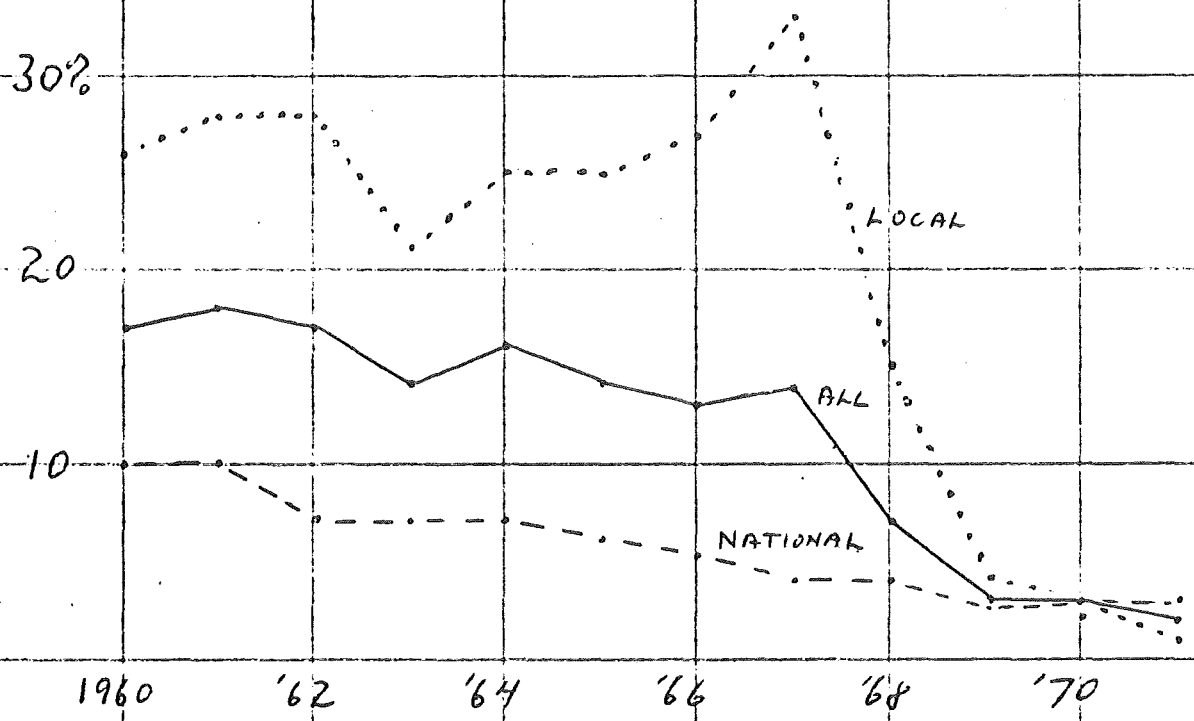


Source: Table 5

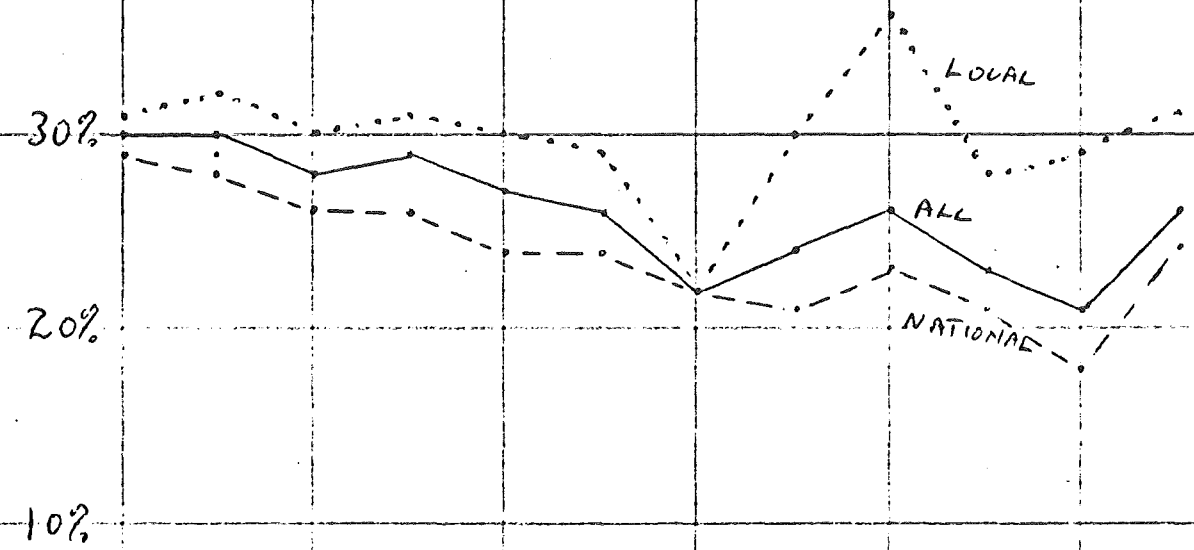
Chart III

Percentage of Number of Small Loans to Total Loans Made

A. Loans Size under $100



B. Loans Size $100 to $300



For number of observation in each year, see Table 3.

CHART IV

Average Size of Loans Made to New, Present and Former Borrowers, 1960 - 71

Means of Averages at Three Major inance Companies

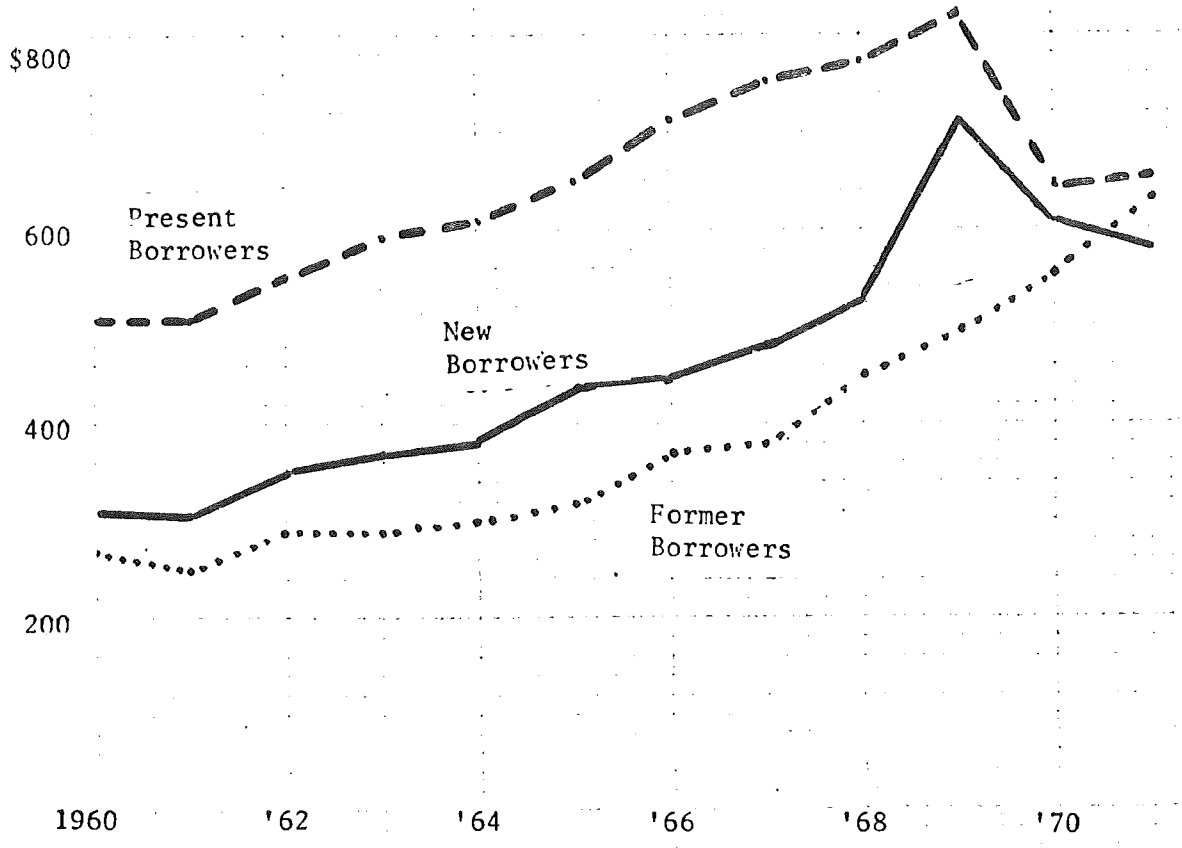
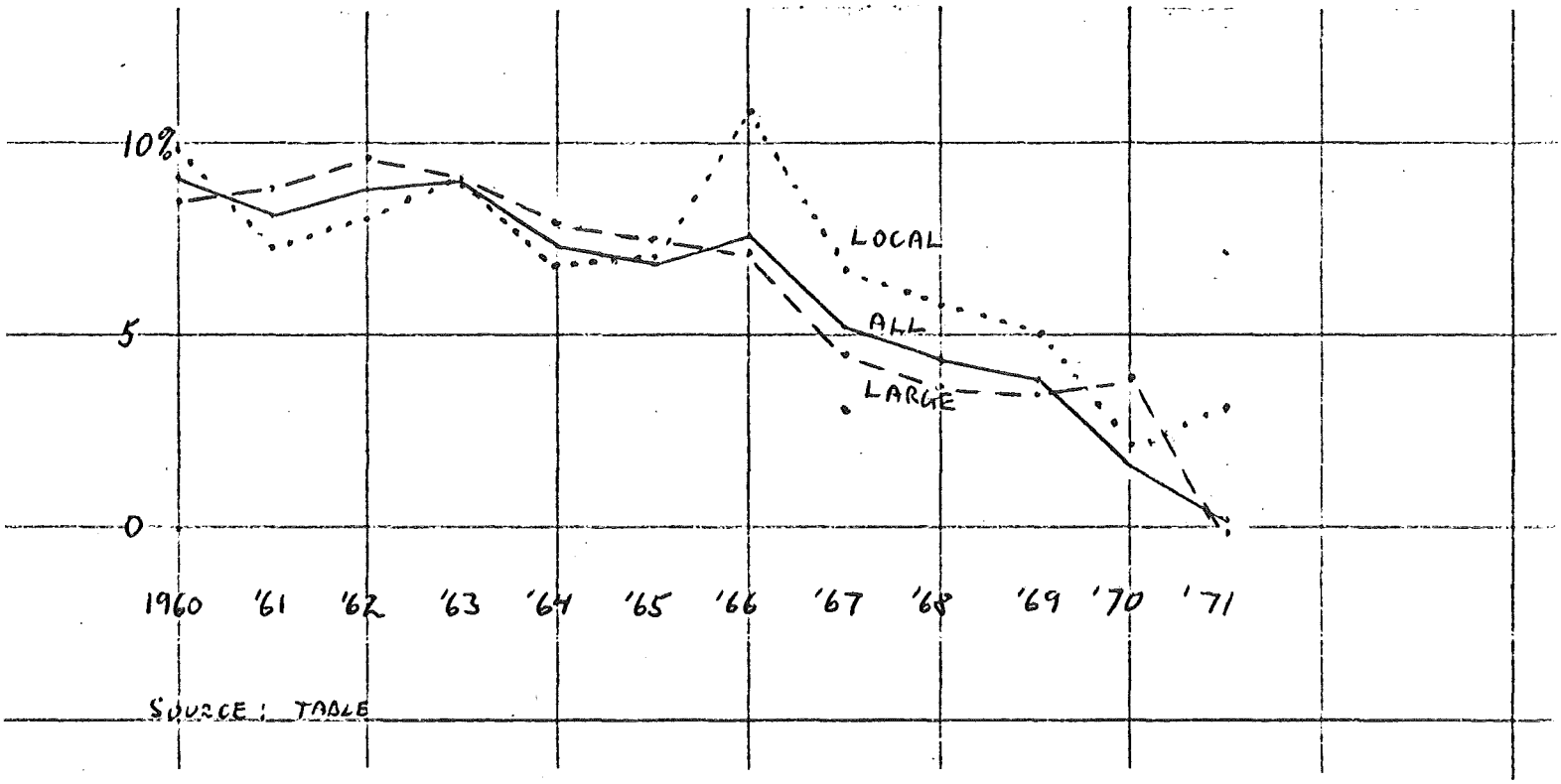


CHART V

Net Income Before Income Taxes and Interest Expense
All Local and Large (Assets over $1 Million) Companies

A. Small Loan Net Income as Percentage of Average Loans Outstanding



B. Total Net Income as Percentage of Average Assets "Used and Useful"

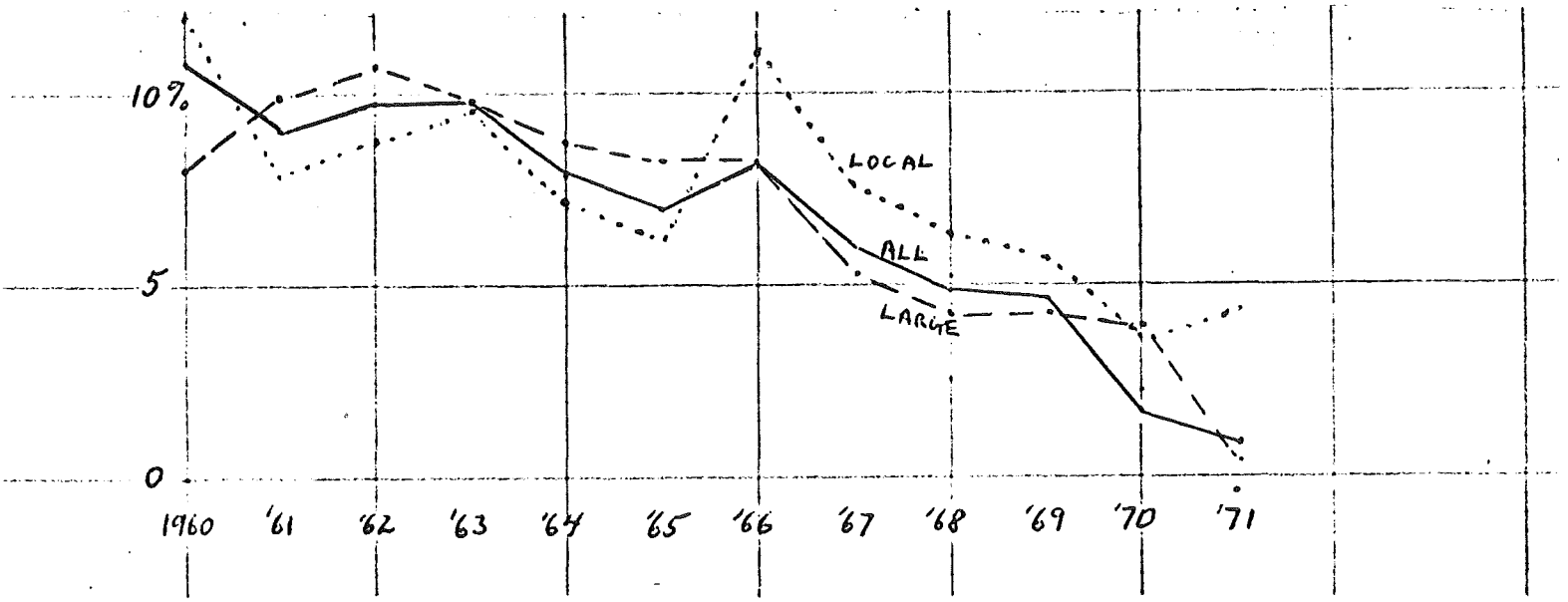
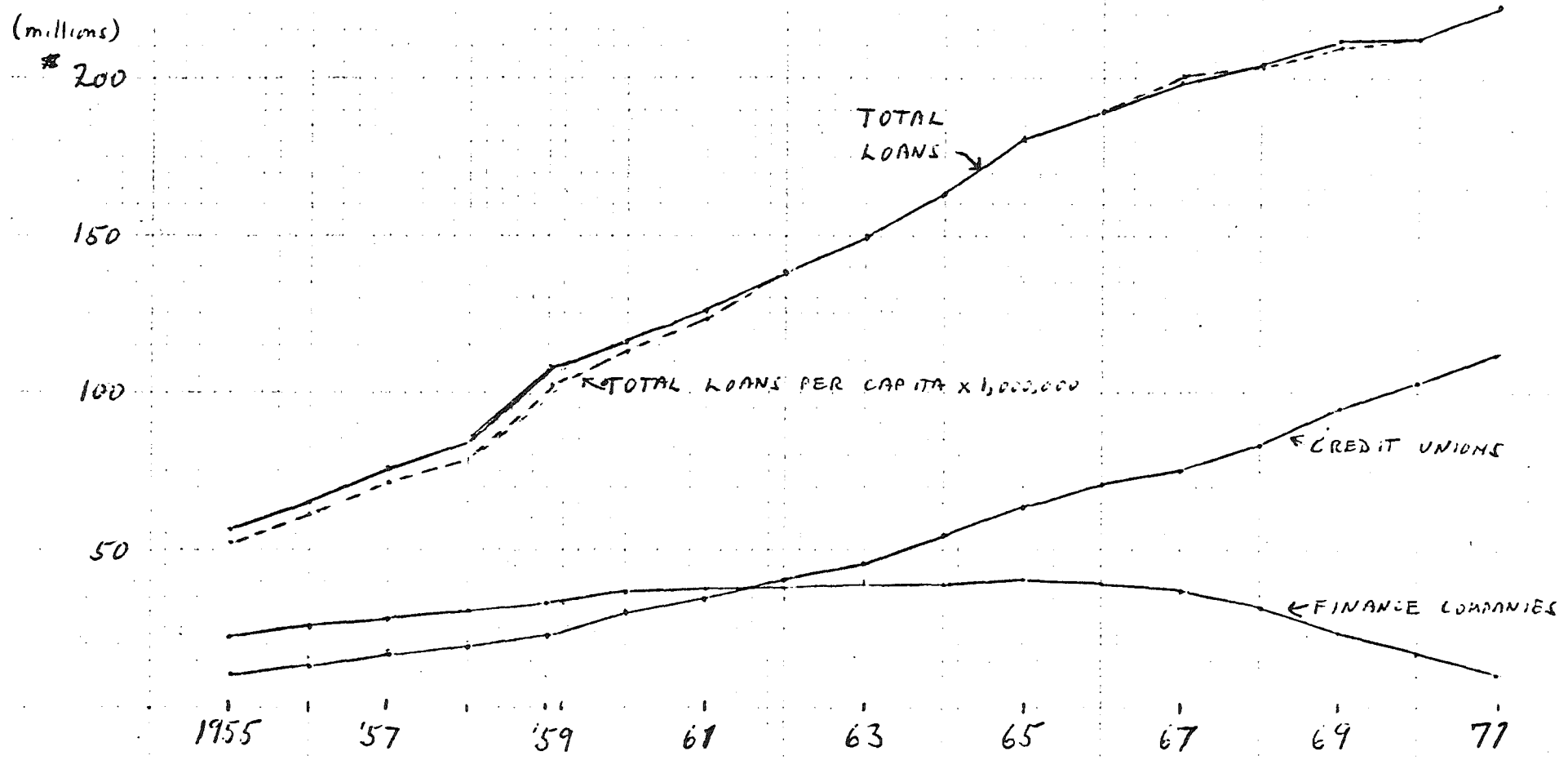


CHART VI

Total and Per Capita, Credit Union and Finance Company Personal Cash Installment Loans in 1971 Dollars, 1955 through 1971



Sources: Commercial and mutual savings banks, FDIC, Assets and Liabilities - Commercial and Mutual Savings Banks, annual (Washington, D. C.).
Finance Companies, industrial banks and state credit unions: Report of the Bank Commission of the State of Maine, bi-annual (Augusta, Maine).
Federal Credit Unions: Annual Report of the Bureau of Federal Credit Unions, annual (Washington, D. C.).

Deflated by GNP deflator, 1971=100.

TABLE 1

Number of Local and National Companies Operating in Maine by Asset Size (in Million $) of Company[a]

Type and Asset Size	Number as of June 30							
	1965	1966	1967	1968	1969	1970	1971	1972
Local								
$0-$300	7	7	7	6	3	2	2	1
301-1000	2	2	2	2	1	1	1	1
1001 +	2	2	2	2	2	2	2	2
total	11	11	11	11	6	5	5	4
National								
$0-$300	2	2	2	1	2	1	0	0
301-1000	3	3	4	3	3	3	1	0
1001 +	11	11	11	11	10	8	7	5
total	16	16	17	15	15	12	8	5
$0-$300	9	9	9	7	5	3	2	1
301-1000	5	5	6	5	4	4	2	1
1001 +	13	13	13	14	12	10	9	7
total	27	27	28	26	21	17	13	9

[a] As of later of December 31, 1965 or second year of operation.

TABLE 2

Number of Offices Operated by Local and National Companies in Maine by Asset Size (in Millions $) of Company[a]

Type and Asset Size	Number as of June 30							
	1965	1966	1967	1968	1969	1970	1971	1972
Local								
$0-$300	7	7	7	6	3	2	2	1
300-1000	3	2	2	2	1	1	1	1
1000 +	4	4	4	4	3	3	3	3
total	14	13	13	12	7	6	6	5
National								
$0-$300	3	3	3	1	7	1	0	0
300-1000	7	9	12	10	9	5	2	0
1000 +	87	88	88	88	74	42	28	15
total	97	100	103	99	90	48	30	15
All								
$0-$300	10	10	10	7	10	3	2	1
300-1000	10	11	14	12	10	6	3	1
1000 +	91	92	92	92	77	45	31	18
total	111	113	116	111	97	54	36	20

[a] As of later than December 31, 1965 or second year of operation

TABLE 3

Number and Type of Observations Used for Analyses in Tables 4, 5, 6 and 7

	Type of Companies			Size of Companies		
Year	Local	National	Total	Under $300	$300-$1000	Over $1000
1960	10	12	22	5	5	12
1961	11	14	25	6	5	14
1962	12	14	26	7	5	14
1963	12	14	26	7	5	14
1964	12	11	23	7	3	13
1965	11	15	26	6	6	14
1966	9	15	24	4	6	14
1967	8	16	24	5	5	14
1968	4	13	17	2	3	12
1969	4	13	17	2	3	12
1970	4	12	16	2	3	11
1971	3	8	11	1	1	9

Determinants of Total Operating Expenses
Regression Coefficients[a], (Standard Errors)[b], t Values[c]
(all variables in common logarithms)

Dependent variable: total expenses before income taxes, interest and losses

		Independent Variables (see description below)					
Year	NLO	NLM/O	NLL/M	DEL60+	NLO/OF	LOCAL	CONST
1960	1.18[a]	.65	.20	-.11	.26	.22	.30
	(.14)[b]	(.62)	(.16)	(.16)	(.19)	(.12)	(.19)
	8.59[c]	1.04	1.24	.67	1.37	1.80	1.60
1961	1.16	d	.07	.12	.38	.17	.60
	(.10)		(.09)	(.11)	(.12)	(.08)	(.15)
	11.46		.83	1.13	3.12	1.97	.65
1962	1.22	1.03	.61	.60	-.02	.22	--
	(.11)	(.43)	(.10)	(.13)	(.15)	(.10)	
	12.71	2.39	6.35	4.53	.12	2.14	
1963	1.10	.74	.44	.38	.27	.22	--
	(.12)	(.36)	(.10)	(.11)	(.16)	(.11)	
	8.90	2.07	4.44	3,39	1.76	1.98	
1964	1.15	--	.35	.16	.24	.30	.20
	(.27)		(.18)	(.19)	(.34)	(.23)	(.30)
	4.22		1.99	.85	.72	1.28	.66
1965	1.30	1.30	.67	.23	-.20	.43	.38
	(.14)	(.31)	(.12)	(.19)	(.21)	(.11)	(.18)
	9.29	4.17	5.55	1.18	.99	3.69	2.15
1966	1.29	.21	.37	.33	--	.36	.23
	(.10)	(.28)	(.17)	(.22)		(.15)	(.27)
	13.14	.74	2.12	1.48		2.38	.82
1967	1.28	.52	.77	.15	-.09	.39	.15
	(.14)	(.26)	(.18)	(.15)	(.22)	(.15)	(.21)
	8.88	1.96	4.35	1.00	.40	2.70	.70
1968	1.10	.46	.41	-.05	.49	--	.10
	(.06)	(.35)	(.17)	(.09)	(.12)		(.32)
	17.45	1.33	2.42	.60	4.07		.31
1969	1.07	.20	.50	-.19	.42	.13	.16
	(.14)	(.16)	(.31)	(.14)	(.25)	(.16)	(.17)
	7.73	1.22	1.59	1.39	1.68	.82	.90
1970	1.19	--	.55	-.04	.09	.45	.50
	(.26)		(.48)	(.25)	(.45)	(.34)	(.31)
	4.55		1.14	.16	.19	1.35	1.60
1971	1.06	-.20	.16	-.057	.057	.027	1.47
	(.13)	(.16)	(.23)	(.090)	(.15)	(.11)	(.36)
	8.47	1.29	.71	.63	.32	.26	4.13

R^2 for any year's regressions are no less than .96. See Table 3 for number of observations.

d - F value too small for inclusion.

Description of independent variables:

NLO = number of loans outstanding (year beginning + year end)/2
NLM/O = number of loans made/NLO
NLL/M = number of large (over $1,000) loans made/total number made
DEL60+ = dollars of loans delinquent 60 days or more
NLO/OF = NLO/number of offices
LOCAL = 10 if company is local, 1 if company is national ($\log_{10} 10 = 1$, $\log 1 = 0$)
CONST = constant term

Table 5

Average Operating Cost Per Loan
(Income taxes, interest and losses not included)

Year	All Variables Included	Significant Variables Only Included[a]	
		Amount	Variables
1960	55.72	53.15	NLO, NLO/OF
1961	54.73	53.44	NLO, NLO/OF, LOCAL
1962	62.89	62.92	NLO, LOCAL, NLM/O, LL?NLM, DEL60+
1963	62.81	62.08	NLO, LOCAL, NLM/OF, LL/NLM, DEL60+
1964	66.48	64.63	NLO, LOCAL, LL/NLM
1965	76.79	72.46	NLO, LOCAL, LL/NLM, NLM/O
1966	75.11	71.44	NLO, LOCAL LL/NLM
1967	66.68	65.14	NLO, LL/NLM, NLO/OF
1968	96.25	96.55	NLO, LL/NLM, NLO/OF
1969	78.23	75.97	NLO, NLO/OF
1970	82.08	73.54	NLO, NLO/OF
1971	105.32	68.33	NLO, CONST

Source: All variables evaluated at geometric mean values against coefficients given in Table 4. See Table 3 for number of observations.

[a]Variables included in regression that "explain" the variance of the dependent variable the most, whose t values are significant at the .05 level.

TABLE 6

Small Loan Business Net Operating Income before Income Taxes and Interest Expense
As Percentage of Average Loans Outstanding

Arithmetic Mean (Range: low - high)

Year	Local	National	Total	Under $300	$300-1000	Over $1000
1960	12.0 (4 - 29)	9.8 (7 - 15)	10.8 (4 - 29)	14.2 (4 - 29)	10.3 (9 - 13)	9.6 (7 - 15)
1961	7.8 (-11 - 18)	9.9 (4 - 14)	9.0 (-11 - 18)	6.8 (-10 - 18)	9.0 (5 - 13)	9.9 (6 - 14)
1962	8.6 (-5 - 18)	10.6 (4 - 15)	9.7 (-5 - 18)	7.2 (-5 - 18)	10.5 (9 - 13)	10.7 (6 - 15)
1963	9.5 (1 - 17)	9.8 (6 - 13)	9.7 (1 - 17)	9.6 (1 - 17)	9.4 (7 - 11)	9.8 (5 - 13)
1964	7.1 (-8 - 18)	8.7 (3 - 14)	7.9 (-8 - 18)	6.2 (-8 - 18)	7.5 (3 - 12)	8.8 (6 - 14)
1965	6.3 (-10 - 20)	7.5 (-5 - 12)	7.0 (-10 - 20)	4.6 (-10 - 20)	6.4 (-5 - 12)	8.3 (3 - 12)
1966	11.0 (6 - 19)	6.4 (-9 - 24)	8.1 (-9 - 24)	11.8 (6 - 19)	5.5 (-9 - 24)	8.2 (-4 - 16)
1967	7.6 (-3 - 23)	5.2 (-9 - 12)	6.0 (-9 - 23)	7.8 (-3 - 23)	6.7 (-6 - 12)	5.2 (-9 - 11)
1968	6.3 (3 - 13)	4.5 (-7 - 11)	4.9 (-7 - 13)	(a)	4.9 (a)	4.3 (-7 - 11)
1969	5.6 (-3 - 15)	4.3 (-9 - 11)	4.6 (-9 - 15)	(a)	1.4 (a)	4.5 (-9 - 11)
1970	3.6 (-2 - 11)	1.0 (-21 - 8)	1.7 (-21 - 11)	(a)	-8.6 (a)	4.0 (-2 - 8)
1971	4.4 (a)	-0.5 (-8 - 5)	0.8 (-8 - 10)	(a)	(a)	0.4 (-8 - 5)

number of observations: see Table 3

a. Too few observations

TABLE 7

Total Net Operating Income before Income Taxes and Interest Expense as Percentage or Average Total Assets Used and Useful

Arithmetic Mean (Range: low - high)

Year	Local	National	Total	Under $300	$300-$1000	Over $1000
1960	9.8 (4 - 15)	8.6 (5 - 13)	9.2 (4 - 15)	10.5 (4 - 15)	9.3 (7 - 12)	8.5 (5 - 13)
1961	7.4 (-9 - 16)	8.7 (4 - 12)	8.1 (-9 - 16)	6.7 (-9 - 16)	8.9 (5 - 11)	8.8 (4 - 12)
1962	8.0 (-4 - 16)	9.5 (5 - 15)	8.8 (-4 - 16)	7.0 (-4 - 16)	9.2 (6 - 11)	9.6 (5 - 15)
1963	9.1 (1 - 18)	8.9 (6 - 12)	9.0 (1 - 18)	9.7 (1 - 18)	8.3 (6 - 11)	8.9 (5 - 12)
1964	6.8 (-7 - 18)	7.8 (0 - 13)	7.3 (-7 - 18)	6.6 (-7 - 18)	5.8 (2 - 8)	8.0 (3 - 13)
1965	7.2 (-1 - 20)	6.6 (-4 - 11)	6.9 (-4 - 20)	7.0 (-1 - 20)	5.3 (-4 - 8)	7.5 (3 - 11)
1966	10.8 (4 - 21)	5.7 (-8 - 22)	7.6 (-8 - 22)	13.1 (4 - 21)	5.0 (-8 - 22)	7.2 (-5 - 15)
1967	6.7 (-5 - 18)	4.5 (-8 - 12)	5.2 (-8 - 18)	7.2 (-5 - 18)	5.4 (-6 - 10)	4.5 (-8 - 11)
1968	5.8 (3 - 12)	3.9 (-6 - 11)	4.4 (-6 - 12)	(a)	4.9 (a)	3.7 (-6 - 10)
1969	5.0 (-3 - 13)	3.6 (-12 - 9)	3.9 (-12 - 13)	(a)	1.4 (a)	3.5 (-12 - 9)
1970	2.1 (-3 - 8)	1.4 (-15 - 10)	1.6 (-15 - 10)	(a)	-7.2 (a)	3.8 (-2 - 10)
1971	3.2 (a)	1.0 (-8 - 4)	0.2 (-8 - 6)	(a)	(a)	-0.2 (-8 - 4)

number of observations: see Table 3

a. Too few observations

TABLE 8

Actual vs. Predicted Total Loans, 1968 - 1971
Based on Coefficients Estimated with Data from 1954 - 1967

(millions of constant dollars, 1971=100)

		1968	1969	1970	1971
Actual (A)		204	211	213	225
Predicted (P), Standard Error[a] (SE), and Predicted less Actual (P-A)					
Original Data:					
Equation 14' (all variables)	P	222	220	230	223
	SE	8	8	8	8
	P-A	18	9	17	-2
Equation 14" ("good" variables)	P	222	226	234	236
	SE	7	7	7	7
	P-A	18	15	21	11
Logarithmic Data					
Equation 15 (all variables)	P	217	221	234	241
	SE	15	18	18	19
	P-A	13	10	21	16
Equation 15'	P	220	228	235	244
	SE	13	16	16	17
	P-A	16	17	22	19

[a]Standard error(s) is corrected for extrapolation as follows:

$s = (X_i[\hat{b}_i\hat{b}_j]X_j^{-1} + s^2_{y\cdot x})^{-1/2}$ where X_j is a vector of independent variable values for 1968, 1969, 1970 and 1971, $\hat{b}_j$ computed regression coefficients and $[\hat{b}_i\hat{b}_j]$ is the variance covariance matrix of the coefficients, and $s^2_{y\cdot x}$ is the variance of the regression equation.

TABLE 9

Composition of Sample of Borrowers

		Number		Percentage
Borrowers contacted:				
Successful contact with initial survey		378		49.0
Follow-ups		82		10.6
Total complete information		460		59.6
Refused to answer		58		7.6
Total contacted		518		67.2
Borrowers who couldn't be contacted with initial survey:				
Total	335		43.4	
Follow-ups (included above)	-82		-10.6	
Total not contacted		253		32.8
Total sample:		771		100.0

TABLE 10

Occupation of Borrowers

	Not Contacted by First Survey		Contacted by First Survey	
	Not Contacted (N)	Included in Study: Contacted (C)	Included in Study: Answered (A)	Refused to Respond (R)
Percentage of Valid Observations				
unskilled	28	34	24	1
skilled and semi-skilled	31	42	39	38
service workers (manual, janitor, etc.)	3	1	3	4
white collar (sales, office, government, etc.)	9	9	13	1
professional (teacher, executive, proprietor, doctor, etc.)	19	9	9	13
other	10	5	12	11
total valid observations	100	100	100	100
unknown	41	3	22	10
Number of Observations				
total valid	180	80	310	53
unknown	73	2	68	5
total	253	82	378	58

TABLE 11

Weekly Gross Salary of Borrowers

	Not Contacted by First Survey		Contacted by First Survey	
	Not Contacted (N)	Included in Study Contacted (C)	Answered (A)	Refused to Respond (R)
Percentage of Valid Observations				
$0 - 80	14	21	10	6
81 - 120	50	43	44	7
121 - 160	27	21	28	7
161 - 200	5	10	12	9
200 +	4	5	6	4
total known	100	100	100	53
unknown	69	3	22	10
Number of Observations				
total valid	175	80	310	53
unknown	78	2	68	5
total	253	82	378	58

TABLE 12

Age of Borrowers

	Not Contacted by First Survey		Contacted by First Survey	
	Not Contacted (N)	Included in Study Contacted (C)	Answered (A)	Refused to Respond (R)
Percentage of Valid Observations				
18 - 24	11	5	6	8
25 - 34	27	29	25	26
35 - 44	26	21	31	17
45 - 54	22	19	22	37
55-64	12	24	14	15
65 +	2	2	2	0
Total valid	100	100	100	100
Unknown	58	3	51	26
Number of observations				
Total valid	146	80	250	46
Unknown	107	2	128	12
Total	253	82	378	58

TABLE 13

Marital Status and Dependents of Borrowers

	Not Contacted by First Survey		Contacted by First Survey	
	Not Contacted (N)	Included in Study Contacted (C)	Answered (A)	Refused to Respond (R)
Percentage of Valid Observations				
Marital Status				
married	71	70	80	77
other	29	30	20	23
total valid	100	100	100	100
unknown	78	2	68	5
Number of Dependents				
none	36	32	21	26
one	14	15	19	10
two	17	14	20	13
three	16	13	16	17
four	9	16	15	15
five and over	8	10	9	19
total valid	100	100	100	100
unknown	69	3	22	10
Number of Observations				
total valid	175	80	310	53
unknown	78	2	68	5
total	253	82	378	55

TABLE 14

Number of Years Borrower was Continually in Debt
and Number of Previous Loans before Refusal

	Not Contacted by First Survey		Contacted by First Survey	
	Not Contacted (N)	Included Contacted (C)	in Study Answered (A)	Refused to Respond (R)
Percentage of Valid Observations	12	18	12	23
Number of Years in Debt to Finance Company:				
1	12	18	12	23
2 - 4	41	36	43	34
5 - 8	22	18	20	14
9 - 12	16	12	17	19
13 +	9	16	8	10
total valid	100	100	100	100
unknown	82	5	65	5
Number of Previous Loans:				
1	16	25	22	17
2 - 4	38	34	34	35
5 - 8	22	25	21	31
9 +	24	16	23	17
total valid	100	100	100	100
unknown	68	7	21	10
Number of Observations				
total valid	171	77	313	53
unknown	82	5	65	5
total	253	82	378	58

TABLE 15

Differences between Samples of Interviewed and Not Interviewed Borrowers, Chi Square (χ^2) Tests

Characteristics[a]	χ^2 at 5% Level	Survey Groups: Chi Square Values A vs R	A vs C	A vs N	C vs N
Occupation	11.10	2.48	6.76	15.14*	8.91
Salary	9.49	2.83	7.99	10.23*	5.29
Age	11.10	7.06	6.25	3.97*	7.64
Marital Status	3.84	.13	3.66	5.53*	.00
Number of Dependents	11.10	7.89	5.74	13.39*	3.69
Years in Debt	9.49	5.85	6.75	.40	4.88
Number of Previous Loans	7.81	3.28	2.49	2.50	4.38

Notes

a. See Tables 10 through 14 for description of categories within categories.

b. Groups: A = answered initial survey

R = refused to respond to initial survey

C = contacted in follow up field interviews

N = not contacted in follow up interviews

* = Significant at least at the 5 percent level. See Tables listed in a for degrees of freedom.

TABLE 16

Primary Reason for Original Borrowing:
Borrowers Who Were Able and Unable to Obtain New Funds

Percentages	A	U
Consolidate debts	54.5	48.9
Used car	19.5	12.7
Medical bills	7.4	8.7
Furniture and household items	5.6	10.0
Home improvements	5.2	4.8
School related expenses	2.6	3.5
Miscellaneous	5.2	11.4
	100.0	100.0
Number of Borrowers	231	229
Chi square	12.78	
(at 5% level, 6 degrees of freedom = 12.60)		

TABLE 17

Effect of Not Being Able to Borrow from Finance Companies

Percentages -- 460 Observations

	Able to Obtain Funds		Unable to Obtain funds		Total
	Sub	Total	Sub	Total	Sample
Felt Better Off:					
Rid of "burden" of finance company	17.5		82.0		
Established credit with "better quality" financial institution	80.2				
Finance companies are a necessary evil			16.9		
No reason given	2.4		1.2		
Total felt better off	100.1	74.1	100.1	36.3	55.3
Felt Worse Off:					
Too easy to obtain money -- still under "burden" of financial institution	87.5				
No other alternative available			31.4		
Burden of high interest rates lead to difficulty in paying off loan			68.7		
No reason given	12.5		0		
Total felt worse off	100.0	7.0	100.1	36.3	21.6
Felt About the Same:					
Still borrowing from a finance company	40.9				
Still borrowing from some financial institution	50.0				
Doesn't matter where one borrows			71.4		
No reason given	9.1	19.1	28.6	27.6	23.3
	100.0	100.2	100.0	100.2	100.1
Percentage of Total		50.2		49.8	

TABLE 18

Differences Between Borrowers, Chi Square Tests
Those Able and Unable to Obtain Funds and According to Feelings About
Situation (Regardless of Ability of Obtain Funds)

Characteristics[a]	χ^2 at 5% Level[c]	Borrower Groups: Chi Square Values[b]			
		A vs U	B vs W	B vs S	W vs S
Occupation	11.10	1.35	8.11	5.18	9.04
Salary	9.49	1.86	3.51	2.82	1.08
Age	11.10	5.14	16.88*	2.30	7.50
Marital Status	3.84	2.08	2.75	.25	.61
Number of Dependents	11.10	8.47	5.60	7.58	4.00
Years in Debt	9.49	5.71	3.62	.95	1.75
Number of Previous Loans	7.81	4.35	1.32	2.23	1.71
Percent of Loan Unpaid	9.49	5.58	4.22	4.34	7.30
Reason for Borrowing	12.60	12.78*	3.70	6.85	3.14

Notes

a. See Tables 10 through 14 and 16 for descriptions of categories within characteristics.

b. Groups: A = able to obtain funds
U = unable to obtain funds
B = felt better off, all borrowers
W = felt worse off, all borrowers
S = felt about the same, all borrowers

Chi squares based on number of valid observations, as follows:

occupation, salary, marital status, dependents, years in debt, number of loans: A = 192, U = 198, B = 214, W = 85, S = 91

age: A = 162, U = 168, B = 184, W = 69, S = 77

percent unpaid, reason for borrowing, action taken: A = 229, U = 231, B = 254, W = 99, S = 107

c See tables labeled in a for degrees of freedom.

* Significant at least at the 5% level.

TABLE 19

Differences According to Feelings, Chi Square Tests
Borrowers Who Were Able to Obtain Funds

Characteristics[a]	χ^2 at 5% Level[c]	Feelings: Chi Square Values[b]		
		B vs W	B vs S	W vs S
Occupation	11.10	9.94	7.24	14.65*
Salary	9.49	5.67	10.94*	4.35
Age	11.10	8.90	1.80	2.81
Marital Status	3.84	.03	.11	.06
Number of Dependents	11.10	2.44	4.07	4.00
Years in Debt	9.49	.58	3.42	2.27
Number of Loans	7.81	3.87	2.69	2.20
Percent of Loan Unpaid	9.49	1.96	4.10	1.72
Reason for Borrowing	12.60	6.36	7.37	1.29
Source of Funds	11.10	33.24*	47.90*	2.22

Notes

a. See Tables 10 through 14 and 16 for description of categories within characteristics.

b. Feelings: B = felt better off
W = felt worse off
S = felt about the same

Chi squares based on number of valid observations, as follows:

occupation, salary, marital status, dependents, years in debt, number of loans: B = 141, W = 13, S = 38

age: B = 121, W = 12, S = 35

percent unpaid, reason for borrowing, source of funds: B = 171, W = 16, S = 44

c. See tables listed in a. for degrees of freedom.

* Significant at least at the 5% level.

TABLE 20

Source of Funds, in Percentages, of Those Able to Obtain Funds, By Feelings About Inability to Borrow at Original Finance Company

Source of Funds	Feelings[a]			
	Total	B	W	S
Another finance company	39.8%	24.6%	93.8%	79.5%
Bank	32.9	42.7	0	6.8
Credit union	20.8	25.1	6.3	9.1
Relative	4.3	5.3	0	2.3
Friends	1.3	1.2	0	2.3
Own funds or sale of property	.9	1.2	0	0
	100.1%	100.1%	100.1%	100.0%

a. B = felt better off
W = felt worse off
S = felt about the same

Chi-square statistics (significantly different from 0 if > 11.10, 5 degrees of freedom):

B vs. W	33.24
B vs. S	47.90
W vs. S	2.22

TABLE 21

Differences According to Feelings, Chi Square Tests

Borrowers Who Were Unable to Obtain Funds

Characteristics[a]	χ^2 At 5% Signif.[c]	Feelings: Chi Square Values[b]		
		B vs W	B vs S	W vs S
Occupation	11.10	9.44	1.17	4.38
Salary	9.49	3.96	7.53	4.19
Age	11.10	10.25	3.88	8.58
Marital Status	3.84	.66	.01	.38
Number of Dependents	11.10	3.96	4.19	8.63
Years in Debt	9.49	10.55*	3.23	2.44
Number of Loans	7.81	2.52	1.15	.89
Percent of Loan Unpaid	9.49	1.13	5.66	9.40
Reason for Borrowing	12.60	6.29	3.90	3.45
Action Taken	5.99	9.56*	2.47	13.22*

Notes

a. See Tables 10 through 14 and 16 for description of categories within characteristics.

b. Feelings: B = felt better off

W = felt worse off

S = felt about the same

Chi squares based on number of valid observations, as follows:

occupation, salary, marital status, dependents, years in debt, number of loans: B = 73, W = 72, S = 53

age: B = 63, W = 57, S = 42

percent unpaid, reason for borrowing, action taken: B = 83, W = 83, S = 63

c. See tables listed in a. for fer degrees of freedom.

* Significant at least at the 5% level.

TABLE 22

Action Taken, In Percentages, by Those Who Couldn't Obtain Funds, By Feelings About Inability to Borrow at Finance Company

Percentages	All	Better	Worse	Same
Continued to pay	77.3%	81.9%	62.7%	90.5%
Missed payments but paid off loan	22.3	16.9	37.3	9.5
Declared bankruptcy	.4	1.2	--	--
	100.0%	100.0%	100.0%	100.0%

TABLE 23

Occupation of Borrowers According to Previous Indebtedness to Finance Company In Percentages, 383 Observations[a]

Occupation	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
Unskilled	26	46	28	14	18	19
Skilled and Semi-Skilled	40	26	38	42	52	46
Service Workers	2	4	2	3	2	3
White Collar	13	8	11	16	13	14
Professional	9	6	11	12	5	5
Other	10	10	9	13	10	14
Totals	100	100	99	100	100	101
Total Number of Years	100	13	42	20	16	10

Chi square statistic = 27.31 (31.40 at 5 percent level of significance).

		Number of Previous Loans			
		1	2-4	5-8	9+
Unskilled	26	35	28	25	13
Skilled and Semi-Skilled	40	33	40	40	50
Service Workers	2	2	3	1	2
White Collar	13	9	13	15	12
Professional	9	8	11	9	9
Other	10	13	6	11	15
Totals	101	100	101	101	101
Total Number of Loans	100	23	35	21	28

Chi square statistic = 18.33 (25.00 at 5 percent level of significance.)

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

TABLE 24

Salary of Borrowers According to Previous Indebtedness to Finance Company

In Percentages, 383 Observations[a]

Weekly Gross Salary	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
$ 0-$80	12	14	13	9	10	14
81- 120	44	44	42	41	49	49
121- 160	26	22	28	30	23	24
161- 200	12	18	12	11	12	5
200+	6	2	5	9	7	8
TOTALS	100	100	100	100	101	101
Number of Years	101	13	42	20	16	10

Chi square statistic = 9.67 (26.29 at 5 percent level of significance).

		Number of Previous Loans			
		1	2-4	5-8	9+
$ 0 - $80	12	20	10	11	9
81 - 120	44	44	38	51	46
121 - 160	26	26	29	24	26
161 - 200	16	7	17	10	10
200+	6	3	6	5	10
TOTALS	100	100	100	101	101
Number of Loans	100	23	35	21	21

Chi squares statistic = 17.16 (21.00 at 5 percent level of significance).

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

TABLE 25

Age of Borrowers According to Previous Indebtedness to Finance Company
In Percentages, 323 Observations[a]

Age	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
18-24	6	12	9	3	0	0
25-34	26	44	27	27	13	7
35-44	28	22	30	40	24	11
45-54	21	6	16	22	38	41
55-64	17	12	16	7	22	41
65+	2	4	2	0	2	0
Totals	100	100	100	99	99	100
Total Number of Years	99	15	44	18	14	8

Chi square statistic = 64.28 (31.40 at 5 percent level of significance.)

Age	Distribution of Sample	Number of Previous Loans			
		1	2-4	5-8	9+
18-24	6	19	3	2	0
25-34	26	29	30	28	10
35-44	28	26	34	28	22
45-54	21	12	17	25	36
55-64	17	13	13	15	32
65+	2	1	4	2	0
Total	100	100	101	100	100
Total Number of Previous Loans	100	26	35	21	18

Chi square statistic = 64.11 (25.00 at 5 percent level of significance.)

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

TABLE 26

Marital Status of Borrowers According to Previous Indebtedness to Finance Company In Percentages, 383 Observations[a]

Marital Status	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
Married	79	86	75	82	80	73
Other	21	14	25	18	20	27
Total	100	100	100	100	100	100
Total Number of Years	101	13	41	20	16	10

Chi square statistic = 3.76 (9.49 at 5 percent level of significance.)

Marital Status	Distribution of Sample	Number of Previous Loans			
		1	2-4	5-8	9+
Married	79	87	72	78	80
Other	21	13	28	22	20
Total	100	100	100	100	100
Total Number of Previous Loans	100	23	35	21	21

Chi square statistic = 7.43 (7.81 at 5 percent level of significance.)

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

TABLE 27

Number of Dependents of Borrowers According to Previous Indebtedness to Finance Company In Percentages, 383 Observations[a]

Number of Dependents	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
None	23	14	22	29	16	38
One	18	14	18	18	18	24
Two	19	20	21	9	21	19
Three	15	16	18	14	16	5
Four	16	22	11	23	18	8
Five and over	9	14	10	6	10	5
Total	100	100	100	99	99	99
Total Number of Years	101	13	42	20	10	10

Chi square statistic = 25.99 (31.40 at 5 percent level of significance.)

Number of Dependents	Distribution of Sample	Number of Previous Loans			
		1	2-4	5-8	9+
None	23	19	23	18	32
One	18	12	20	20	20
Two	19	22	15	21	18
Three	15	17	18	12	12
Four	16	15	15	21	12
Five and over	9	15	9	7	6
Total	100	100	100	99	100
Total Number of Previous Loans	100	23	35	21	21

Chi square statistic = 16.36 (25.00 at 5 percent level of significance)

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

TABLE 28

Primary Reason for Original Borrowing According to Previous Indebtedness of Borrowers to Finance Company

In Percentages, 389 Observations[a]

Primary Reason for Borrowing	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
Consolidate debts	51	52	49	47	49	66
Used car	16	15	19	13	15	16
Medical bills	8	13	9	9	5	3
Furniture and household	8	8	6	13	8	3
Home improvements	8	6	9	9	10	5
School related expense	3	2	4	3	3	3
Miscellaneous	5	4	4	5	10	5
Total	99	100	100	99	100	101
Total Number of Years	101	13	42	20	16	10

Chi square statistic = 6.30 (36.41 at five percent level of significance)

Primary Reason for Borrowing	Distribution of Sample	Number of Previous Loans			
		1	2-4	5-8	9+
Consolidate debts	51	54	51	45	54
Used car	16	17	14	19	16
Medical bills	8	11	9	8	5
Furniture and household	8	3	11	8	6
Home improvements	8	6	7	12	8
School related expense	3	3	3	2	4
Miscellaneous	5	6	4	5	7
Total	99	100	99	99	100
Total Previous Loans	100	23	35	21	21

Chi square statistic = 11.96 (28.86 at five percent level of significance)

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

Table 29

Borrowers' Feelings About Not Being Able to Borrow from Finance Company According to Previous Indebtedness to Company

In Percentages, 389 Observations[a]

Borrowers' Feelings	Distribution of Sample	Number of Years Continuously in Debt				
		1	2-4	5-8	9-12	13+
Felt better off	54	48	56	59	51	50
Felt worse off	22	31	20	20	23	26
Felt about the same	23	21	24	21	26	24
Totals	99	100	100	100	100	100
Total number of years	101	13	42	20	16	10

Chi square statistic = 4.26 (15.50 at five percent level of significance)

Borrowers' Feelings	Distribution of Sample	Number of Previous Loans			
		1	2-4	5-8	9+
Felt better off	54	48	55	57	57
Felt worse off	22	25	21	25	19
Felt about the same	23	27	24	18	24
Totals	99	100	100	100	100
Total Previous Loans	99	23	34	21	21

Chi square statistic = 3.32 (12.60 at five percent level of significance)

[a]All those of the sample of 460 for whom data on salary and previous indebtedness are available.

TABLE 30

Number of Times Loan was Previously Rewritten
at a Large Finance Company

Number of Rewrites	Cases in Bankruptcy		Sample of Good Customers	
	Number	Percentage	Number	Percentage
0	2	2.2	0	0.0
1	59	65.6	17	14.0
2	13	14.4	18	14.9
3	2	2.2	11	9.1
4	1	1.1	4	3.3
5	3	3.3	9	7.4
6	1	1.1	6	5.0
7	1	1.1	4	3.3
8	1	1.1	6	5.0
9	1	1.1	3	2.5
10	1	1.1	7	5.8
11	2	2.2	1	.8
12+	3	3.3	35	28.9
	90	99.8	121	100.0
No information	261	290.0	116	95.9
	351		237	