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Research impact

Changing the payday loan landscape

A major report by the School of Economics underpinned a landmark reform of the controversial payday loan sector.

Payday lending has been a source of increasing controversy in recent years. Stories of small loans escalating into massive debts, APRs reaching 5000% and under-pressure borrowers struggling to cope with ever-spiralling charges have brought mounting pressure for a significant regulatory crackdown.

"Payday loan companies have grown used to being able to do whatever they want," says John Gathergood, an Associate Professor of Economics. "They have been the villains of recession Britain, offering loans that in many cases have served as the last step on a descent into financial ruin rather than the first rung on a ladder to better forms of credit."

As a leading researcher in the field of household financial behaviour, Dr Gathergood co-authored a major report into payday loan companies for the Financial Conduct Authority (FCA). His findings underpinned the FCA's subsequent ruling that payday lenders would be limited in what they could charge, with interest and charges capped at a maximum of 0.8% of the loan principal per day.

The decision was announced in November 2014 and effectively gave payday lenders eight weeks to adapt their practices before the new regulations officially came into effect.

"The FCA has offered these companies a chance to reform," says Dr Gathergood, who is affiliated with the school's Granger Centre for Time Series Econometrics and Centre for Finance, Credit and Macroeconomics. "All payday lenders will see their profits fall sharply. The cap is going to squeeze even the biggest landers, and many of them simply won't be able to survive. They have to show they can provide products and services for the good of the customer – or else risk annihilation."

The Financial Conduct Authority, the UK's financial watchdog, has suggested only a handful of Britain's payday lenders will be able to continue operating under the new regulations and that only those that are able to prove themselves "ethical" will be allowed to profit. The Chancellor, George Osborne, described the new regulatory regime as "part of a long-term economic plan to have a banking system that works for hardworking people".

John Gathergood

Lecturer in Economics

"Over recent decades financial innovation has made available to consumers a wide range of financial and insurance products and instruments, such as mortgages and credit cards. There's much to be learned about how these are used and what the proper role for regulation should be."

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