

The Daily Dish

Turning Unaffordable Into Unavailable

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Senator Elizabeth Warren, the likely chair of the Senate Banking Committee in the next Congress, has announced her intention of legislating a 10-percent cap on credit card interest rates. The putative goal is "affordability." Credit card debt outstanding is roughly $1.3 trillion, with 6.87 percent going delinquent. The latter is presumably evidence of unaffordability of some sort and the blame is placed on credit card interest rates, which now average 19.7 percent. Simply cap the rate at 10 percent, the argument goes, and *voila* – affordability stretches out as far as the eye can see.

The problem, of course, is that interest rates reflect the riskiness of borrowers. Lenders are willing to extend those final dollars of credit because the average of 19.71-percent interest offsets the costs from delinquencies, defaults, collection costs, and so forth. When the interest rate gets cut to 10 percent, the math no longer adds up. Credit will be cut off for the now-unprofitable lending.

And who will that be? The riskiest, marginal, less affluent borrowers. That is, those whom "affordability policy" is supposed to help. Instead of unaffordable, credit cards will simply become unavailable. Presumably advocates of the cap are comforted by the fact that payday loans, loan sharks, and the mob will still be in business.

Stepping back, the credit card line of business will now be less attractive overall, and funds will instead be funneled toward more attractive alternatives – auto loans, mortgages, commercial lending, etc. The irony is that the cap helps every borrower except the credit card borrowers.

Price-fixing never works, and this is a predictable failure. A heads up that this is a bad idea is President Trump's support for the idea in January; the president is a notoriously prolific and unwise price-fixer (see, for example, his most-favored nation drug pricing policies). All

sides, and more importantly the public, would be well-served to drop the interest rate cap idea entirely.