

FINDINGS:

The Higher Prices Facing Lower Income Consumers



I. BASIC FINANCIAL SERVICES

Low- and moderate-income consumers are more likely to buy high-priced basic financial services than higher income households.

Lower income families are more likely than other households to pay high prices for basic financial services like check cashing, short-term loans, tax preparation, and transmitting money. Depending on what products they purchase, the extent of their demand, and where and from what type of establishment they make their purchases, lower income families can pay as much as several thousand dollars every year in extra costs for these services.⁵⁵

*Lower income consumers are much more likely than higher income consumers to pay high prices to cash checks and take out short-term loans.*⁵⁶

Depending on where lower income families live and the types of services they consume, these costs can range from a few dollars more to over \$2,000 every year in extra costs for these basic financial services.⁵⁷

Lower income consumers pay more because of their greater reliance upon alternative, high-priced financial service companies, including check cashers, payday lenders, pawnshops, and auto-title

lenders. For instance, survey evidence indicates that most check casher customers earn annual incomes below \$30,000. Similarly, most payday-lending customers earn between \$15,000 and \$60,000 per year, and over 65 percent of pawnshop customers earn under \$25,000.⁵⁸ All these types of busi-



nesses tend to charge a higher price for a comparable service or product sold by a bank or a credit union, thus indicating that the lower income consumers who frequent them are more likely than higher income households to pay high prices for basic financial services.

Exactly how much more lower income consumers pay depends on what products they consume, the extent of their demand, along with where and who they are buying the product from. For instance, cashing

a check *generally* costs substantially more every year at a check-cashing establishment than at a bank, but exactly how much more varies across the country.⁵⁹

Prices charged at check cashers range from approximately one percent of the face value of a check in West Virginia to no limit in 19 states.⁶⁰ Across the 12 metropolitan areas in our sample, maximum check-cashing fees generally range between 1.6 percent of the face value of a check in New York to up to 10 percent for personal checks cashed in Maryland.⁶¹ Although there is no information about the exact prices charged at establishments in these areas, recent research suggests that fees are generally fixed at the maximum allowed rate.⁶²

Thus, a family with a net income of \$30,000 a year would pay about \$18.46 every two weeks to cash a check in New York, or about \$480 over the course of a year. In contrast, that same family would pay \$1,500 to cash checks from a private company if they lived and worked in Atlanta.

At least in theory, the family need not pay anything to cash

Exactly how much more lower income consumers pay depends on what products they consume, the extent of their demand, along with where and who they are buying the product from.



The maximum allowable fee for check cashing services varies widely among the states

Select Geographies	Description of maximum fee allowed by state regulations
California (Los Angeles and San Francisco)	For government and payroll checks, fees may not exceed 3% of the value of the check with customer I.D., and 3.5% or \$3 (whichever is greater) without I.D. Fees may not exceed \$15 for bounced checks. A one-time fee to set up an account may not exceed \$10.
Colorado (Denver)	Not regulated
Connecticut (Hartford)	Fees may not exceed 1% of the face value of government and payroll checks, and may not exceed 2% of the face value of all other checks.
District of Columbia (Washington)	Check cashers may not charge an additional fee for verification, handling, and documentation processing totaling more than \$5 on a personal check with a face value of up to \$250; no more than \$10 on a personal check with a face value of \$250.01-\$500; no more than \$15 on a personal check with a face value of \$500.01-\$750; and no more than \$20 on a personal check with a face value of \$750.01-\$1,000.
Georgia (Atlanta)	Fees may not exceed 3% of the face value of government checks, 10% of personal checks, and 5% of all other checks.
Illinois (Chicago)	Fees may not exceed 1.4% of the face value plus \$0.90 for checks under \$500, and 1.85% of the face value for checks greater than \$500.
Indiana (Indianapolis)	Fees may not exceed 10% of the face value of the check.
Maryland (Baltimore)	Fees may not exceed 3% of the face value of government checks, 5% of payroll checks, and 10% of personal checks.
New York (New York)	Fees may not exceed 1.58% of the face value of the check or \$1, whichever is greater.
Pennsylvania (Pittsburgh)	Fees may not exceed 2.5% of the face value of government checks, 3% of payroll checks, and 10% of personal checks. One-time fee to investigate credit of consumer may not exceed \$10.
Washington (Seattle)	No limit

Sources: California Department of Financial Institutions; Colorado Department of Regulatory Agencies; State of Connecticut Department of Banking; District of Columbia Department of Insurance, Securities and Banking; Georgia Department of Banking and Finance; State of Illinois Department of Financial and Professional Regulation; Indiana Department of Financial Institutions; Maryland Department of Labor, Licensing, and Regulation; State of New York Banking Department; Pennsylvania Department of Banking; Washington State Department of Financial Institutions

checks, because they could do so through a banking account. Although no inventory exists of banking products offered by every bank and credit union in the metropolitan areas in this analysis, recent industry reports suggest that a growing number of banks have started offering accounts with no maintenance fees, no minimum balance requirements, and no check-cashing fees.⁶³ Although the

banking industry has traditionally lost money on checking accounts (even with monthly maintenance fees), banks and credit unions now widely view these accounts as a gateway to the other, more profitable services they offer.⁶⁴ In turn, competition for checking customers means that a growing number of banks are offering accounts that lower income consumers could rationally use as a substitute for

paying fees to a check casher.

Lower income consumers also are more likely than higher income consumers to pay higher prices for short-term loans because they rely on alternative, high-priced lenders. As with the premium for cashing checks, just how much more they pay for short-term loans also varies across the country; the amount is also partially dependent upon what type of business sells the lower

The maximum allowable fee for payday lending services varies widely among the states

Select Geographies	Description of Maximum Fee Allowed by State Regulations
California (Los Angeles and San Francisco)	Maximum Charge = 15%; Maximum Loan Amount = \$300
Colorado (Denver)	Maximum Charge = May not exceed 20% of the first \$300 loaned plus seven and one-half percent of any amount loaned in excess of \$300; Maximum Loan Amount = \$500
Connecticut (Hartford)	Prohibited
District of Columbia (Washington)	Maximum Charge = 10% of face amount + fee of \$5: \$0–\$250; \$10: \$251–\$500; \$15: \$501–\$750; \$20: \$751–\$1000; Maximum Loan Amount = \$1,000
Georgia (Atlanta)	Prohibited
Illinois (Chicago)	Maximum Charge = \$15.50 per \$100 ; Maximum Loan Amount = \$1,000 or 25 percent of a borrower's gross monthly income, whichever is less
Indiana (Indianapolis)	Maximum Charge = 15%: \$0–\$250; 13%: \$251–\$400; 10%: \$401–\$500; Maximum Loan Amount = \$500
Maryland (Baltimore)	Prohibited
New York (New York)	Prohibited
Pennsylvania (Pittsburgh)	Prohibited
Washington (Seattle)	Maximum Charge = 15%: first \$500; 10%: remaining portion of the loan in excess of \$500 up to the \$700 maximum; Maximum Loan Amount = n.a.

Source: National Conference of State Legislatures, Consumer Federation of America (www.paydayloaninfo.org)

income consumer an alternative short-term loan.

For the 31 million lower income households that have a checking account, millions of them turn every year to payday lenders for short-term loans.⁶⁵ In fact, about 81 percent of the customers that buy high-priced payday loans earn less than \$50,000 a year.⁶⁶

Payday lenders typically provide a two-week loan in exchange for a personal check that the lenders will cash on the borrower's payday. State departments of banking regulate rates charged by payday lending businesses, which means that rates vary widely across the country.⁶⁷

Across the country, fees for payday loans range from nothing (because the industry is banned) to

higher than 15 percent of a loan's value in Colorado, Delaware, South Dakota, and other states.⁶⁸ In Washington, for instance, total fees and interest cannot exceed 15 percent of a loan for \$500 or less (a 390 percent APR). Similarly, Illinois allows payday lenders to charge \$15.50 for every \$100 borrowed (a 403 percent APR).

The 9 million lower income households that don't have a checking account can turn to one of 14,000 pawnshops or one of the growing number of car-title lenders.⁶⁹ Prices for pawnshop loans range from no limit (in Arkansas, Iowa, Idaho, Maryland, North Dakota, Nebraska, South Dakota, Utah, and West Virginia) to 2 percent or less in Indiana and Missouri.⁷⁰ Across our sample of 12

metropolitan areas, pawnshop loan rates range from a low of 2.5 percent in the California metro areas for loans up to \$225, to 20 percent in Chicago for the exact same loan amount. Similarly, recent evidence indicates that auto title loans bear an APR around 400 percent.⁷¹

There is no information about the prices actually charged at establishments in these areas, but recent research suggests fees are generally set at the maximum allowed rate.⁷² Assuming this research is generalizable, a Seattle family in which one salaried worker earns a net income of \$30,000 a year would pay about \$270 to borrow \$300 six times year from a payday lender. In Chicago, that same family would pay about \$280 to borrow the same amount of money.

The maximum allowable fee for pawnshop loans varies widely among the states

Geography	Description of Monthly Fees Allowed (Includes Interest and Other Fees)
California (Los Angeles and San Francisco)	2.5% per month on the amount up to \$225; 2% on the portion over \$225 up to \$900; 1.5% on the portion over \$900 up to \$1,650; 1% on the portion over \$1,650. Service charge may range from \$1 on any loan for not more than 90 days in amount of less than \$15, to \$140 on any loan for not more than 90 days in amount of \$2,100-\$2,500; plus a \$3 loan setup fee for loans smaller than \$50, or a setup fee of \$5 for loans greater than \$50; plus a \$5 storage fee for items larger than 1 cubic foot, \$10 for items larger than 3 cubic feet, \$20 for items larger than 6 cubic feet, and \$1 for each additional cubic foot of space.
Colorado (Denver)	20% per month for loans smaller than \$50; 10% per month for loans greater than \$50
Connecticut (Hartford)	5% per month for loans smaller than \$15; 3% per month for loans between \$14.01 and \$50; 2% per month for loans greater than \$50
District of Columbia (Washington)	2% per month for loans smaller than \$200; 1% per month for loans greater than \$200 but less than \$1,000; 0.67% per month for loans greater than \$1,000
Georgia (Atlanta)	For the first 90 days, 25% per month at a minimum of \$10 per month. After 90 days, 12.5% per month at a minimum of \$5 per month.
Illinois (Chicago)	20% per month
Indiana (Indianapolis)	2% per month for loans smaller than \$960; 1.75% per month for loan amounts between \$960 and \$3,200; 1.25% per month for amounts greater than \$3,200. May charge an additional fee of up to 20% per month for storage, setup fees, etc.
Maryland (Baltimore)	No specified limits
New York (New York)	3% per month
Pennsylvania (Pittsburgh)	3% per month, plus a \$1 charge per pledge
Washington (Seattle)	Sliding scale from \$1 for loans smaller than \$10 to 3% for loans of \$100 or more; plus a one-time fee ranging from \$0.50 for loans smaller than \$5 to \$90 for loans of \$4,500 or more.

Source: Tenney, Glen. "The Effects of Government Regulation on Competition and Supply in the Pawn Industry: A Quantitative and Qualitative Study." 2004.

As with check-casher fees, lower income families that pay these costs could avoid them by purchasing the same services from mainstream companies in the form of credit cards, home equity loans, and overdraft protection plans, among other products. One 2005 survey measuring 146 different credit card products sold by 47 different companies found that the average APR was 12.6 percent, and

industry reports suggest that the typical APR on a home equity loan is even lower.⁷³ These rates are just a fraction of those charged by payday lenders and other alternative loan vendors.

This does not hold true, however, when consumers overdraw their checking accounts, effectively using them as a source of short-term loans, and incur overdraft fees.⁷⁴ Although no industry-wide assess-

ment measures the average rate banks charge for fees, several reports suggest that they can be quite high.⁷⁵ For instance, one major company charges \$31 per overdraft.⁷⁶ Used once per month, six times a year, the Seattle low-income family that pays \$270 to borrow \$300 six times year from a payday lender would pay about \$186 at this bank for that same loan amount.⁷⁷ If that family splits that overdraft fee between two bounced checks, however, these fees can quickly outpace charges levied by alternative sources.

Together, lower income consumers rely more on alternative, high-priced check-cashing and short-term loan companies than do higher income households. The annual cost of this reliance can range from a few extra dollars to several thousand dollars for lower income families.

Lower income consumers are also more likely than higher income consumers to pay high fees to get their tax returns quickly.

Lower income consumers are about as likely as higher income consumers to pay for tax preparation services. Nationwide, about 57 percent of lower income tax filers used for-profit tax preparation services in 2003, compared to about 61 percent of non lower income tax filers.⁷⁸

However, when lower income families use for-profit tax preparation firms, they are much more likely than high-income consumers to buy refund anticipation loans (RALs), which are essentially advance payments made to filers

based on the refund check from the IRS that they expect to receive. Because the IRS can take several weeks to cut a refund check, these loans have a stronger appeal to lower income families, who, by definition, are on more limited budgets.

Nationwide, about five percent of middle and higher income tax filers take out RALs, compared to about 15 percent of the lower income market.⁷⁹ Our sample of metropolitan areas reflects this trend: among middle and higher income households, demand for refund anticipation loans ranged from a low of 3.2 percent of filers in San Francisco to a high of nearly 8 percent in Atlanta. Among lower income filers, however, demand for RALs was much higher in every

metropolitan area we sampled, ranging from a low of 6 percent in San Francisco to a high of over 21 percent in Atlanta.

Though no nationwide or metropolitan estimate of the cost of RALs exists, one recent study suggests that a major tax preparation firm typically charges about 250 percent.⁸⁰ Other widely cited studies suggest that rates can range from 70 to more than 1,800 percent.⁸¹ This can add up to over \$100 in fees for short, two-week loans—a cost, again, that lower income consumers are much more likely than higher income consumers to incur.

Lower income tax filers are much more likely than higher income tax filers to buy refund anticipation loans

Metropolitan Area	Proportion of Tax Filers That Buy Refund Anticipation Loans (2003)	
	Lower Income Households	All Other Households
San Francisco	5.9%	3.2%
Pittsburgh	8.4%	3.4%
Hartford	8.6%	3.3%
Denver	9.7%	4.2%
Seattle	10.3%	5.2%
Los Angeles	10.4%	4.1%
New York	11.0%	4.4%
Washington, DC	12.2%	5.2%
Chicago	14.5%	6.2%
Baltimore	16.2%	5.4%
Indianapolis	18.6%	7.7%
Atlanta	21.2%	8.0%

Source: Unpublished IRS data from Alan Berube and Porsha Cropper, The Brookings Institution

Lower income consumers are likely to pay fees to wire funds to foreign countries, fees less likely to be incurred by higher income households.

Evidence also suggests that lower income consumers are more likely than higher income consumers to buy remittance products. These services allow immigrants to send money back to their country of origin, nearly always for some type of fee. According to a recent analysis by Bendixen and Associates, 80 percent of U.S. buyers who send remittances to Latin America—the most common destination by far—earn annual incomes below \$30,000.⁸² This points to the much higher demand among lower

income households for this basic financial service.⁸³

Prices for remittances vary widely across markets, companies, and by the destination for the remittance. According to one recent study, sending a remittance to Mexico costs about 7.32 percent of the amount of money sent.⁸⁴ To send \$200 every other week over the course of a year, then, would amount to about \$320 in fees for that year. Given that 35 percent of immigrants in 2002 earned less than \$20,000 a year, and 68 percent earned less than \$35,000, hundreds of dollars spent on fees for remittance products can have a significant effect on the budget of a regular, lower income user.⁸⁵



IMPLICATIONS

The dense concentration of businesses that sell high-priced financial services in lower income neighborhoods can serve to limit the choices of poorer consumers.

Nearly all of the high-priced, basic financial service companies we discuss in this section—alternative check cashers and short-term loan providers, tax preparation firms, and wiring companies—tend to be much more densely concentrated in lower income neighborhoods than higher income neighborhoods. Overall, however, the majority of these establishments are located in moderate-income neighborhoods, suggesting that the saturation of lower income markets has provided an incentive for these companies to move into higher income neighborhoods. We review the evidence on each of these types of businesses below.

Check Cashing and Short Term Loans

The highest, per-capita concentration of alternative check cashing and short-term loan providers are found in the lowest income neighborhoods of metropolitan areas.⁸⁶ Take Denver, for instance. According to our data, there are approximately 334 core alternative

financial service providers in the metro area. In Denver neighborhoods with median incomes below \$30,000, there is one of these establishments for every 3,196 residents. As the median income in a Denver neighborhood increases, the number of alternative providers of financial services per person decreases: neighborhoods with

Alternative check cashers and short-term loan providers are densely concentrated in lower income neighborhoods

Population Per Alternative Check Casher and Short-Term Loan Provider, by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Seattle metro	2,330	6,888	38,244	n.a.	n.a.
Denver metro	3,196	4,755	22,957	27,416	n.a.
Atlanta metro	4,230	5,297	19,019	66,154	33,702
Indianapolis metro	4,357	6,385	20,434	n.a.	n.a.
Baltimore metro	4,901	14,270	68,083	147,356	n.a.
Los Angeles metro	5,873	8,856	28,110	155,864	n.a.
San Francisco metro	5,899	11,938	39,071	74,456	n.a.
Hartford metro	5,985	28,849	55,624	n.a.	n.a.
Washington, DC metro	6,369	7,199	21,994	49,505	218,405
New York metro	9,314	15,303	32,203	116,847	108,350
Pittsburgh metro	10,825	23,392	218,803	n.a.	n.a.
Chicago metro	17,661	16,621	28,845	40,045	40,781
Metro Average	7,130	10,061	29,663	77,366	133,221
Seattle city	3,560	11,565	62,219	n.a.	n.a.
San Francisco city	3,655	13,179	68,810	n.a.	n.a.
Baltimore city	4,724	12,589	33,918	n.a.	n.a.
Indianapolis city	4,769	5,568	15,355	n.a.	n.a.
Denver city	5,054	7,281	66,690	10,528	n.a.
Atlanta city	6,363	16,804	n.a.	30,879	11,737
Los Angeles city	6,822	11,570	27,902	66,113	n.a.
Oakland city	7,861	12,084	n.a.	n.a.	n.a.
Hartford city	7,919	33,659	n.a.	n.a.	n.a.
Washington, DC city	8,833	8,086	10,156	5,553	n.a.
New York city	9,410	14,271	13,550	19,242	10,050
Pittsburgh city	9,891	132,560	n.a.	n.a.	n.a.
Chicago city	20,781	28,436	8,928	14,731	n.a.
City Average	7,600	10,915	15,410	26,465	32,929

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

Most alternative check cashers and short-term loan providers are located in moderate-income neighborhoods

Distribution of Alternative Check Cashers and Short-Term Loan Providers by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Washington, DC metro	8%	65%	23%	3%	0%
Chicago metro	11%	67%	19%	2%	1%
Atlanta metro	12%	77%	10%	1%	0%
Denver metro	12%	79%	8%	1%	0%
Seattle metro	16%	77%	7%	0%	0%
Indianapolis metro	18%	75%	8%	0%	0%
San Francisco metro	18%	61%	19%	3%	0%
Los Angeles metro	32%	62%	6%	0%	0%
New York metro	33%	51%	15%	1%	0%
Baltimore metro	43%	49%	7%	1%	0%
Hartford metro	43%	40%	17%	0%	0%
Pittsburgh metro	44%	55%	1%	0%	0%
Metro Average	22%	62%	14%	1%	0%
Denver city	18%	80%	1%	1%	0%
Indianapolis city	21%	72%	7%	n.a.	0%
Chicago city	25%	54%	20%	1%	0%
Washington, DC city	26%	55%	12%	8%	0%
Seattle city	28%	69%	4%	0%	0%
Oakland city	38%	62%	0%	0%	0%
New York city	42%	45%	12%	1%	0%
San Francisco city	43%	48%	9%	0%	0%
Los Angeles city	53%	43%	4%	0%	0%
Atlanta city	65%	33%	0%	2%	0%
Baltimore city	68%	31%	1%	0%	n.a.
Hartford city	86%	14%	n.a.	n.a.	n.a.
Pittsburgh city	92%	8%	0%	0%	n.a.
City Average	38%	53%	8%	1%	0%

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

median incomes between \$30,000 and \$60,000 have one store for every 4,755 residents; those with median incomes between \$60,000 and \$90,000 have one storefront for every 22,957 residents; and so on. This points to the very high relative density of alternative providers of check cashing and short-term loan services in lower income neighborhoods.

While concentration is highest in lower income communities, the bulk of alternative financial service sector storefronts are found in moderate-income neighborhoods with median incomes between \$30,000 and \$60,000. In Chicago, for instance, although the city's lowest-income neighborhoods are home to a much higher per-capita number of vendors of alternative financial services, more than two-thirds of these establishments in the metro area are located in neighborhoods with moderate incomes.

This trend is replicated in nearly every metro area in our sample: While alternative check cashing and short-term loan providers are much more highly concentrated in cities' lowest-income neighborhoods, most of the establishments are located in neighborhoods with more moderate incomes.

Tax Preparation Firms

Tax preparation establishments tend to be the most densely concentrated in moderate-income neighborhoods with median incomes between \$30,000 and \$60,000, rather than in lower- and higher-income neighborhoods. Moderate-income neighborhoods within the Chicago metropolitan area, for instance, have one tax preparation establishment for every 5,011 residents. That compares to about 8,200 people in a lower income neighborhood, 5,716 people in neighborhoods with median incomes between \$60,000 and \$90,000, 6,204 people per-establishment in a neighborhood with a median income between \$90,000 and \$120,000, and so on.

Our sample does include exceptions to this trend, however. Tax preparation firms in Denver, Pittsburgh, San Francisco, and Seattle are most highly concentrated in the lowest-income neighborhoods of those cities. In Seattle, for instance, there is one tax establishment for every 3,035 residents of neighborhoods with median incomes under \$30,000. Neighborhoods with median incomes between \$30,000 and \$60,000, on the other hand, have one establishment for every 4,009 residents, and neighborhoods with median incomes between \$60,000 and \$90,000 have one tax preparation firm for every 8,172 residents.



For-fee tax preparation firms are densely concentrated in moderate income neighborhoods

Population Per Tax Return Preparation and Filing Establishment, by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Atlanta metro	5,091	3,331	4,934	12,028	n.a.
Baltimore metro	5,945	4,363	7,360	10,525	n.a.
Chicago metro	8,200	5,011	5,716	6,204	8,739
Denver metro	4,021	5,022	5,483	12,745	5,289
Hartford metro	5,205	4,282	5,115	15,467	n.a.
Indianapolis metro	5,559	4,713	10,547	17,179	n.a.
Los Angeles metro	4,201	3,357	4,240	5,720	6,785
New York metro	8,182	6,557	6,005	7,387	11,405
Pittsburgh metro	3,796	6,440	6,078	5,268	n.a.
San Francisco metro	2,282	2,937	3,688	4,856	3,375
Seattle metro	3,035	4,099	8,172	91,781	n.a.
Washington, DC metro	6,369	3,657	5,206	8,736	12,134
All Metros	5,434	4,367	5,357	7,057	10,336
Atlanta city	7,635	7,202	7,428	30,879	n.a.
Baltimore city	6,239	7,601	16,959	5,493	n.a.
Chicago city	8,906	6,995	4,310	29,462	n.a.
Denver city	5,686	7,374	16,673	5,264	n.a.
Hartford city	7,309	11,220	n.a.	n.a.	n.a.
Indianapolis city	5,621	5,197	16,890	n.a.	n.a.
Los Angeles city	4,987	4,943	5,131	6,010	16,879
New York city	8,964	8,378	6,606	6,791	30,149
Pittsburgh city	7,253	44,187	21,956	n.a.	n.a.
San Francisco city	2,335	3,533	6,036	2,490	n.a.
Oakland city	2,246	4,711	20,432	8,296	n.a.
Seattle city	3,337	4,755	5,656	n.a.	n.a.
Washington, DC city	9,298	4,299	8,309	4,165	5,791
All Cities	6,269	5,267	5,265	6,107	11,622

Source: Author's analysis of data from InfoUSA

Wiring Services

Like the tax preparation firms, nearly all of the core providers of remittance services are located in neighborhoods with median incomes of less than \$60,000. In 2005, over 84 percent of the establishments were located in these neighborhoods.

Again, however, these services are most densely concentrated in the lowest-income neighborhoods of all but two of the metropolitan areas in our sample. Chicago is typical of this general trend. There is about one business that sells wiring services for every 18,367 residents of Chicago's lowest income neigh-

A substantial number of neighborhoods in each of the metros have no financial service establishments and no mainstream establishments in particular.

borhoods. As income rises, the density of these businesses drops. For instance, neighborhoods with a median income between \$60,000 and \$90,000 have about one wiring service for every 60,505 residents.

What's more, the concentration of these businesses varies systematically with the density of immigrants across our sample of 12 metropolitan areas. In particular, Chicago, Los Angeles, and New York, all with substantially larger numbers of foreign born citizens relative to all of the other areas in our sample, have greater density of these services in their lower income neighborhoods, reflecting higher potential demand among consumers in those communities.⁸⁷

Banks and credit unions have footholds in place to compete with these higher-priced sellers of basic financial services.

About 29 percent of the lower income neighborhoods in our sample has at least one bank or credit union. Moreover, over 75 percent of the lower income neighborhoods we analyze are adjacent to a neighborhood with a bank or credit union.

This points to another important trend in the data: a majority of these alternative, high-priced check cashing and short-term loan businesses are meeting the demand for these basic financial services among lower income households literally down the street from mainstream banks and credit unions. In fact, of the 3,278 neighborhoods in our sample that included an alternative checking and short-term loan provider, 49 percent of these neighborhoods also had a bank or a credit union, and nearly 80 percent of these neighborhoods were adjacent to a neighborhood with a bank or credit union.

Still, a substantial number of neighborhoods in each of the metros have no financial service establishments and no mainstream establishments in particular.

In Atlanta, for instance, less than half of the lower income neighborhoods in the metro area are home to a bank or a credit union, compared to 100 percent of the neighborhoods with median incomes above \$120,000. Clearly, while a large infrastructure for mainstream financial services is already in place, geographic gaps remain.

Wire transfer/remittance firms are densely concentrated in lower income neighborhoods

Population Per Remittance/Wire Transfer Service, by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Chicago metro	18,367	31,900	60,505	220,249	122,343
Los Angeles metro	19,124	49,629	94,871	311,729	n.a.
Denver metro	31,160	89,318	642,801	109,663	n.a.
Seattle metro	32,625	92,648	956,105	n.a.	n.a.
New York metro	39,901	43,385	105,151	160,664	433,400
Hartford metro	39,902	109,628	n.a.	n.a.	n.a.
Atlanta metro	42,906	37,399	235,838	88,206	n.a.
San Francisco metro	48,376	74,885	117,214	n.a.	n.a.
Pittsburgh metro	83,509	122,360	218,803	n.a.	n.a.
Indianapolis metro	161,206	247,430	n.a.	n.a.	n.a.
Baltimore metro	181,319	93,306	136,166	n.a.	n.a.
Washington, DC metro	203,797	55,192	85,108	198,019	n.a.
Metro Average	30,422	49,517	109,663	215,809	599,495
Seattle city	13,349	42,791	124,438	n.a.	n.a.
Los Angeles city	17,509	45,543	74,406	132,226	n.a.
Chicago city	17,812	23,544	20,832	n.a.	n.a.
Denver city	22,745	71,895	66,690	n.a.	n.a.
Hartford city	31,674	67,317	n.a.	n.a.	n.a.
Oakland city	36,686	277,936	n.a.	n.a.	n.a.
San Francisco city	42,031	42,833	68,810	n.a.	n.a.
New York city	43,350	47,571	88,077	n.a.	n.a.
Atlanta city	76,353	75,617	74,280	30,879	n.a.
Pittsburgh city	108,799	132,560	n.a.	n.a.	n.a.
Indianapolis city	157,382	207,882	n.a.	n.a.	n.a.
Baltimore city	330,681	204,416	n.a.	n.a.	n.a.
Washington, DC city	n.a.	55,603	30,467	33,319	n.a.
City Average	30,154	44,495	66,524	158,788	n.a.

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

On average, 30 percent of lower income neighborhoods across the 12 selected metro areas have at least one bank or credit union

Proportion of Neighborhoods with a Bank or Credit Union, by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
New York metro	18%	23%	29%	20%	19%
Chicago metro	23%	49%	67%	72%	59%
Los Angeles metro	30%	30%	26%	20%	15%
Baltimore metro	31%	60%	64%	52%	0%
Atlanta metro	41%	58%	73%	56%	88%
Hartford metro	41%	68%	56%	13%	100%
Washington, DC metro	41%	54%	60%	53%	43%
San Francisco metro	43%	44%	46%	42%	23%
Indianapolis metro	44%	65%	76%	80%	100%
Seattle metro	50%	39%	30%	20%	33%
Pittsburgh metro	55%	52%	52%	40%	100%
Denver metro	57%	48%	47%	54%	40%
Metro Average	29%	40%	44%	36%	31%
New York city	22%	30%	41%	52%	67%
Chicago city	24%	48%	71%	64%	67%
Baltimore city	28%	50%	50%	50%	n.a.
Oakland city	29%	33%	33%	47%	50%
Los Angeles city	32%	38%	48%	33%	12%
Washington, DC city	38%	43%	57%	63%	44%
Atlanta city	39%	56%	57%	67%	100%
Hartford city	41%	59%	n.a.	n.a.	n.a.
Indianapolis city	43%	68%	74%	0%	100%
Pittsburgh city	44%	38%	44%	100%	100%
Denver city	52%	50%	76%	67%	0%
San Francisco city	58%	47%	40%	70%	0%
Seattle city	93%	54%	43%	0%	50%
City Average	29%	40%	49%	50%	39%

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

Why are financial services more costly for lower income consumers?

This section has shown that lower income families are generally much more likely than higher income families to buy costly basic financial services. This is reflected both by survey evidence and by the location of these businesses, which generally tend to be more densely concentrated in lower income neighborhoods than higher income neighborhoods.

To bring down these higher costs, policymakers will have to grapple with the myriad factors that drive lower income consumers to buy these high priced products.

First, banks and credit unions face both real and perceived higher costs of doing business with lower income consumers.

Today, for instance, over 23 percent of lower income households do not have a checking account, and another 64 percent do not have a savings account.⁸⁸ To be sure, these millions of lower income consumers represent an unmet market demand. While there is some banking presence in many lower income neighborhoods, many consumers do not use them either because of negative perceptions or lack of products to meet their needs.

Lower income consumers need financial products that make sense for them. That means banks need to offer no, or very low, minimum balance requirements, an affordable overdraft protection plan, and no, or very low, maintenance fees. Not all banks offer these services; those that do not face product development and marketing costs to bring these products into the market. Together, these market dynamics drive both real and perceived higher costs of doing business in lower income neighborhoods.

Second, unscrupulous business practices drive up prices in lower income markets.

In some cases, this means that regulatory protections are insufficient. As this section has noted, for instance, companies can charge APRs of 400 to 500 percent for check-cashing services, short-term loans, and refund anticipation loans in some of the areas in this analysis. States that pass laws allowing those astronomical rates keep high-priced providers in business.

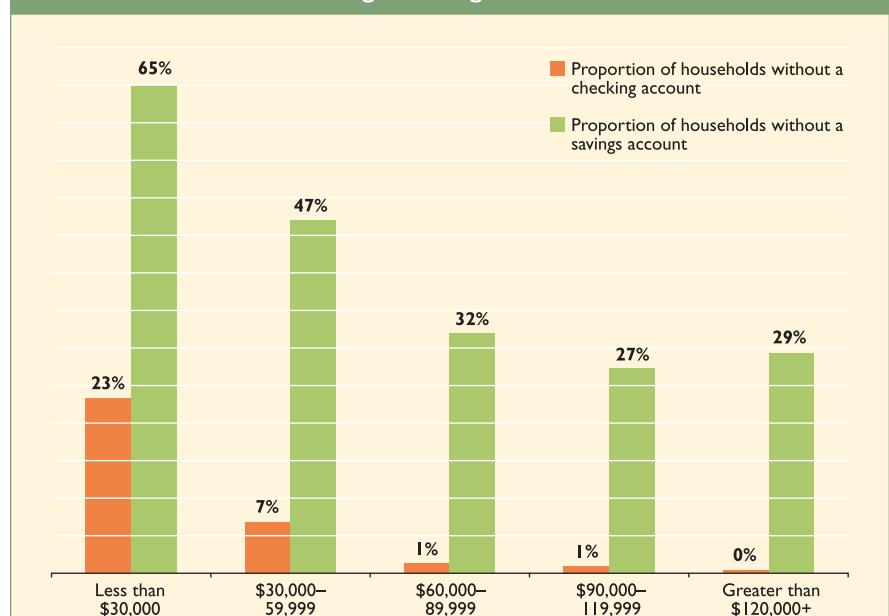
In other cases, regulatory complacency is reflected by the insufficiency of information given to regulated institutions. For instance, some experts report that there is widespread misunderstanding in the banking community about the

paperwork requirements required for opening accounts.⁸⁹ Regulators can help banks move into these markets by more widely disseminating information about which specific types of identification are considered acceptable and not acceptable for banks to use when opening up bank accounts.

Finally, consumers lack information about banking services.

Numerous studies point to misperceptions lower income consumers hold about banks, possibly stemming from bad experiences or lack of interaction with banks or credit unions.⁹⁰ Studies also show that the lower a consumer's income, the less financial knowledge he or she is likely to have: for instance, some lower income families may not know that a checking account can often be a better financial deal than check cashers.⁹¹ Finally, language barriers, along with cultural obstacles, can steer lower income families toward high-priced financial services.⁹²

Lower income households are much less likely than higher income households to own a checking or savings account



Source: Author's analysis of the 2004 Survey of Consumer Finances



II. CARS

Lower- and moderate-income consumers are more likely than higher income households to pay higher prices for car-related products.

Lower income families consistently spend more to purchase cars and take out auto loans than do higher income families. On average, lower income households pay between \$50 and \$500 more in car prices and an extra two percentage points on an auto loan. Together, these higher prices can add up to over \$1,000 every year, depending on the specific combination of products purchased.⁹³

There is also evidence suggesting that lower income families tend to pay higher auto insurance prices, although insurance industry disclosure laws are too restrictive to reliably quantify the exact value of that premium. We do find, though, that it is generally much more expensive to insure a car in lower income neighborhoods within metropolitan areas than in higher income neighborhoods.

Consumers from lower income neighborhoods typically pay between \$50 and \$500 more for the same car as consumers from higher income neighborhoods.

The typical lower income car buyer pays more for a car than a higher income counterpart. While a number of studies have attempted to capture this dynamic, probably the best recent research is by Fiona Scott Morton and her colleagues, who recently analyzed a national sample of 650,000 car purchases.⁹⁴ After controlling for a number of factors that influence car prices, including the make and model of cars, the neighborhood income of the car buyer—their proxy for the

income of the car buyer—had a significant effect on the final price of a car. They also found that race, and a number of characteristics associated with household income, like educational attainment and renter status, have a strong effect on the price of a car.

What these effects mean is that two customers who buy the exact same car will pay different prices

that vary systematically based on certain characteristics. We can see the power of these effects by comparing two hypothetical car buyers.⁹⁵ The first is white, has a high school diploma, owns a house, and lives in a neighborhood with a median income of \$80,000. The second customer is black, dropped out of high school, rents, and lives in a neighborhood with a median income of \$20,000. According to the analysis by Morton and her colleagues, the second customer will pay about \$500 more than the first customer for the exact same car.

Income only accounts for a small share of this direct effect because Morton and her colleagues control for a number of other car-buyer characteristics. But, income covaries with many of the other independent variables in this analysis, so the total effect of income adds



up to more than just the direct effect of income. For instance, the much larger effect is race, which accounts for over \$300 more, on average, in additional costs, not charged to a white car buyer. Educational attainment and renter status also have significant effects, bringing the total effect to about \$500 in extra charges for this hypothetical consumer.

On average, lower income consumers pay two percentage points more for auto loans than higher income consumers.

Every year, about 4.5 million lower income consumers pay a higher than average APR for their auto loans.⁹⁶ In 2004, the average annualized rate of interest paid by lower income households was about 9.2 percent. In contrast, households that earned between \$30,000 and \$60,000 a year paid an average rate of about 8.5 percent; households earning between \$60,000 and \$90,000 paid an average rate of about 7.2 percent; households earning between \$90,000 and \$120,000 paid about a 6.3 percent rate; and households that earned more than \$120,000 paid about a 5.5 percent rate. Auto loan prices have a nearly perfect, linear relationship with household income.

This relationship has implications that go beyond what a typical household in each income category might pay for an auto loan. To see this, we analyzed the middle 50 percent of all households in each income category—those that fall between the 25th and 75th percentile—in terms of what APRs they paid. This captures a much bigger section of the population

than does an analysis of the central tendency.

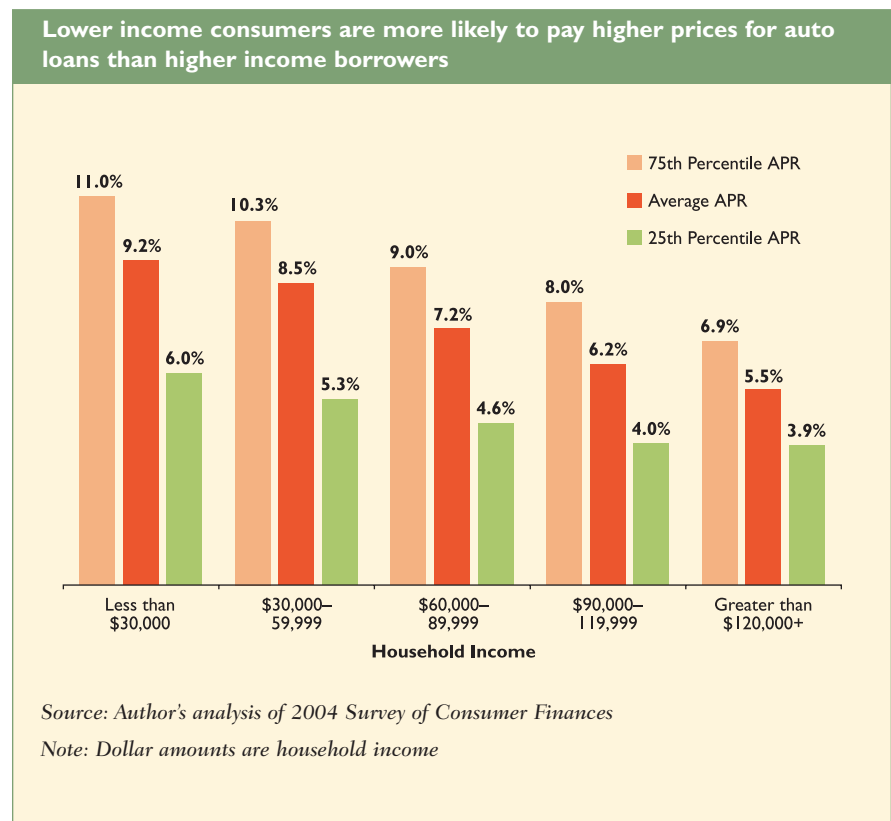
According to this analysis, the middle 50 percent of lower income households pay between 6.0 and 11.0 percent interest for their auto loans. That range systematically falls as household income increases. On the other side of the distribution, for instance, half of the households that earn more than \$120,000 a year pay between 3.9 and 5.3 percent interest on their auto loan—both a smaller range and a much less expensive set of rates than those paid by lower income households.

The data also indicate that lower income households are much more likely to pay extremely high interest rates for auto loans, rather than just a higher average price. To see this, we considered the household

income of all of the households that paid a higher average APR than 75 percent of all of the other households in 2004. This isolated the households that pay unusually high rates to maintain their auto loans.

Consistent with other results, we found that almost 40 percent of all lower income households with auto loans pay these extremely high rates. In contrast, just 30 percent of households with annual incomes between \$30,000 and \$60,000 pay these high rates; along with 20 percent of households with annual incomes between \$60,000 and \$90,000; 13 percent of households that earn between \$90,000 and \$120,000 annually; and just 6 percent of all households with annual incomes above \$120,000.

Taken together, these data demonstrate conclusively that lower



income households tend to pay higher prices for auto loans than do higher income households. Just how much more varies widely across lower income consumers, but we can see how much more the typical lower income consumer pays for an auto loan. In particular, an auto loan of \$5,000—about the median value of the typical car owned by a lower income household—would cost \$1,256 in interest over the course of five years at a rate of 9.2 percent, the average charged to lower income borrowers. In contrast, a household earning more than \$120,000 a year is charged an average rate of 5.5 percent, and thus pays just \$730 in interest over five years. That represents a savings of over \$500 to the higher income household relative to what the lower income household pays.

Holding other factors constant, drivers from lower income neighborhoods pay between \$50 to over \$1,000 more per year in higher prices for auto insurance than higher income drivers.

Because disclosure laws in the insurance industry are so limited, it is difficult to reliably quantify the national average prices different drivers pay for the same insurance policy. But we can look at our sample of metropolitan areas—home to nearly a quarter of Americans—to estimate how these price differences vary across neighborhoods.

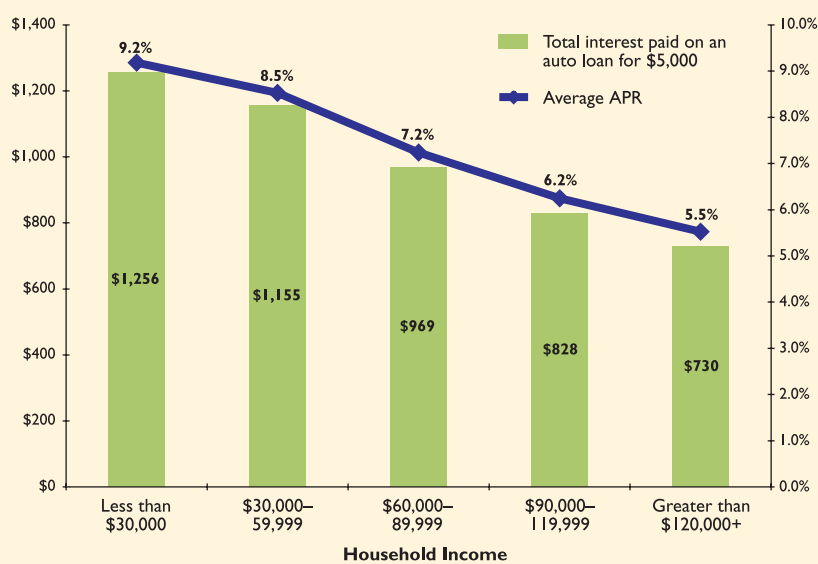
Across our sample of metropolitan areas, we find that the highest prices for auto insurance are in the lowest income neighborhoods. New York, Hartford, and Baltimore had the highest price differentials

across neighborhoods. In these three metros, 12 months of auto insurance in neighborhoods with median incomes of less than \$30,000 costs over \$400 more, on average, than in neighborhoods with median incomes between \$90,000 and \$120,000. New York has the highest price differential in our sample: it costs nearly \$1,000 more every year, on average, to insure the exact same car and driver in a lower income neighborhood than in a moderate-income neighborhood, with a median income between \$30,000 and \$60,000.

In lower income neighborhoods within the eight other metros, the price differential was more modest, generally adding up to \$50 to \$150 extra every year. Chicago, where we found that it costs between \$106 and \$138 more every year to insure a car in the lowest income neighborhoods of the metropolitan area, was typical of this trend. Similarly, car insurance customers from the lowest income neighborhoods of Indianapolis pay anywhere from a \$60 to \$90 premium compared to higher income neighborhoods.

Looking only at the central cities of these metropolitan areas, we saw the exact same trend play out in ten of the twelve cities: Purchasers in the lowest income areas paid the highest prices for auto insurance. New York, again, showed the highest price differential across neighborhoods. In neighborhoods where the median income is less than \$30,000, average prices for twelve months of insurance were between \$210 and \$670 more expensive than in higher income neighborhoods within the city. More typical

Higher auto loan prices for lower income households can add up to hundreds of dollars in extra costs



Source: Author's analysis of the 2004 Survey of Consumer Finances

Note: Average APR is taken from the 2004 Survey of Consumer Finances; loan amount is shown for illustrative purposes only

Auto insurance tends to be more expensive in lower income neighborhoods than higher income neighborhoods

Average Price of Car Insurance, by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Pittsburgh metro	\$356	\$356	\$348	\$330	n.a.
Indianapolis metro	458	384	392	366	366
San Francisco metro	604	542	538	508	496
Seattle metro	614	600	564	568	540
Chicago metro	628	522	490	492	500
Atlanta metro	662	554	566	574	n.a.
Denver metro	730	610	610	588	n.a.
Los Angeles metro	802	694	624	644	790
Washington, DC metro	806	594	552	550	566
Baltimore metro	944	616	544	520	n.a.
Hartford metro	1,268	800	720	750	n.a.
New York metro	1,660	1,110	678	854	848
Metro Average	\$831	\$660	\$678	\$680	\$724
Pittsburgh city	396	382	n.a.	n.a.	n.a.
Indianapolis city	458	428	426	n.a.	n.a.
Seattle city	596	620	548	n.a.	n.a.
Oakland city	610	594	578	n.a.	n.a.
San Francisco city	652	602	614	588	n.a.
Chicago city	664	612	522	552	n.a.
Atlanta city	726	640	594	602	n.a.
Denver city	730	686	670	n.a.	n.a.
Washington, DC city	822	822	822	822	822
Los Angeles city	826	776	746	798	790
Baltimore city	1,042	818	n.a.	n.a.	n.a.
Hartford city	1,336	1,336	n.a.	n.a.	n.a.
New York city	1,766	1,556	1,214	1,096	n.a.
City Average	\$1,064	\$927	\$834	\$802	\$790

Source: Author's analysis of data collected from three major insurance companies

Note: Averages are population weighted

across these ten cities was the gap in San Francisco, where buyers from the lowest income neighborhoods paid between \$38 and \$64 more for auto insurance than did those from the city's more expensive neighborhoods.

Prices could be even higher for lower income drivers because of a number of driver characteristics that are factored into pricing decisions made by insurance companies. Some of these factors, like credit scores, occupation, and education, are strongly associated with household income.⁹⁷ This suggests, though it certainly does not prove, that lower income drivers may systematically pay higher prices for auto insurance. But because there are so few disclosure laws in the insurance industry, there is not sufficient data to analyze the full impact of all of these factors. More than any other issue we discuss in this report, the dearth of good data impairs our understanding of the relationship between income and insurance prices.

Why are these auto and auto-related products more expensive for lower income households?

This section reviewed evidence of the higher prices lower income consumers tend to pay for cars, car loans, and car insurance. Three major causal factors exist for these higher prices.

First, sellers of these auto products face real and perceived risks of doing business in lower income neighborhoods.

Lower income consumers have proven more likely to miss loan payments and to live in areas where it is more expensive to insure drivers.⁹⁸ In addition to the real added costs these risks carry, they also foster a perception of higher costs of doing business with lower income consumers, particularly when measurements of these risks are not precise, such as with insurance pricing. Sellers pass on these higher costs—both real and perceived—to lower income consumers by charging them more. As we discuss in the recommendations section, there are both policy and market tools to lower these costs of doing business.

Second, unscrupulous businesses and business practices inflate the prices charged to lower income consumers for car-related necessities.

Some evidence suggests that car dealers may systematically discriminate against black car buyers when setting a sales price.⁹⁹ Also, the much higher interest rates lower income drivers pay for auto loans may be due to poor credit or payment histories but also may be due to unscrupulous businesses inflating prices. Because the rate of car ownership among lower income families has been growing at a much faster pace than among higher income families, the sheer volume of new purchasers for cars and related products suggests that a lot of these customers may not

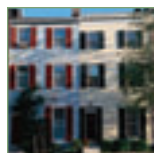


have the experience or knowledge to spot and avoid unscrupulous businesses that overcharge.¹⁰⁰

Finally, lower income consumers tend to be less well-informed than higher income consumers.

Lower income consumers are generally much less likely to compare prices before buying goods and services, which likely makes them more susceptible to bad deals. At the very least, this weakens the buyer's position when shopping for cars, car loans, and car insurance. Any customer who does not know, for instance, what price a dealer paid for a car, the various strategies dealers use to artificially inflate prices, or even that prices are negotiable, will be at a significant disadvantage when they want to purchase a car.

Similarly, lower income consumers are less likely to understand credit scores—an important factor in what sellers charge for loans and insurance—which may needlessly drive up the prices these consumers pay. For instance, one recent survey found that only 56 percent of the respondents with a low educational attainment, and 64 percent of respondents with a lower income, indicated that they knew that their credit rating weakened when they missed a credit card payment.¹⁰¹ Knowing less about this market product may make it more difficult for lower income consumers to bring up their credit scores.



III. HOMES

Lower- and moderate-income consumers are more likely than higher income households to pay higher prices for home-related products.

Lower income consumers are more likely than higher income households to buy higher-priced home furniture and appliances. Together, these extra costs can add up to thousands of dollars for lower income families, depending on what combination of products they consume.

Similarly, evidence suggests that it is generally more expensive to insure a home in a lower income neighborhood than in a higher income neighborhood, and that lower income home insurers may pay an additional premium, above and beyond the premium they pay for the neighborhood they live in.

Lower income homeowners paid, on average, a percentage point more than higher income households in mortgage interest and fees.

Nationwide, more than 4.2 million lower income homeowners pay a higher than average APR for their mortgage.¹⁰² In 2004, the average annualized rate of interest on a first mortgage for lower income households was about 6.9 percent.¹⁰³ By contrast, households that earned between \$30,000 and \$60,000 a year paid an average rate of about 6.5 percent; households earning between \$60,000 and \$90,000 paid an average rate of about 6.0 percent; households earning between \$90,000 and \$120,000 paid about a 5.9 percent rate; and households that earn more than \$120,000 paid a rate of approximately 5.5 percent. The much smaller second mortgage market shows a nearly identical pattern. Over the course of a loan, these

higher annual percentage rates paid by lower income households can add up to tens of thousands of dollars in additional charges.

Higher mortgage prices have implications for more than just the typical household with a mortgage in each income category. To see this, we analyzed the middle 50 percent of all households in each income category—those that fall between the 25th and 75th percentile—in terms of what APRs they paid. This illustrates the rates that the middle 50 percent of each income category pay for mortgages, which captures a much bigger section of

the population than an analysis of the central tendency.

According to this analysis, the middle 50 percent of lower income households paid between 5.4 and 7.8 percent interest for their mortgages in 2004. That range systematically shrinks as household income increases. On the other



Lower income households pay higher prices for home loans than higher income households

Typical APR on First Mortgage, by Income Group

Typical APR on First Mortgage, by Income Group			
Household Income	25th Percentile	Mean	75th Percentile
Less than \$30,000	5.4%	6.9%	7.8%
\$30,000–59,999	5.5%	6.5%	7.0%
\$60,000–89,999	5.3%	6.0%	6.5%
\$90,000–119,999	5.1%	5.9%	6.3%
Greater than 120,000+	4.9%	5.5%	6.0%
Total	5.3%	6.2%	6.8%
Typical APR on Second Mortgage, by Income Group			
Household Income	25th Percentile	Mean	75th Percentile
Less than \$30,000	7.0%	9.2%	10.0%
\$30,000–59,999	5.8%	7.9%	10.0%
\$60,000–89,999	4.5%	7.1%	8.5%
\$90,000–119,999	4.5%	6.4%	8.0%
Greater than 120,000+	4.5%	6.0%	6.5%
Total	4.8%	7.2%	8.8%

Source: Author's analysis of the 2004 Survey of Consumer Finances

side of the distribution, for instance, half of the households that earn more than \$120,000 a year pay between 4.9 and 6.0 percent interest on their mortgage loans. That range is smaller, and the rate much lower, than that paid by lower income households.

The data also indicate that lower income households are much more likely to pay *extremely* high rates for mortgages. To see this, we analyzed all of the households that pay a higher average APR than 75 percent of all other households in the sample. This isolated the households that pay unusually high rates to maintain their home loans. Consistent with other results, we find that over 54 percent of all lower income households with a

mortgage pay these extremely high rates. By contrast, 46 percent of households with an annual income between \$30,000 and \$60,000 pay extremely high rates; along with about 36 percent of households with an annual income between \$60,000 and \$90,000; 35 percent of households between \$90,000 and \$120,000; and just 19 percent of all households with an annual income above \$120,000.

Data from our sample of metropolitan areas reflects these nationwide trends. In 2004, among all home mortgage borrowers in nine of the 12 metro areas in our sample, lower income households were more likely than any other income group to purchase a high-cost mortgage.¹⁰⁴ And, in five of our 12 met-

ropolitan areas, households earning less than \$30,000 represented the largest market share for high-cost mortgages among all of the income groups. Both statistics point to the much greater likelihood that lower income borrowers will buy a higher priced mortgage product than higher income households.

These overall trends belie important differences across the metropolitan areas in our sample, however. Lower income borrowers in the metro areas of Atlanta, Baltimore, Indianapolis, and Pittsburgh show particularly high demand for high-cost loans: in those four metros, more than one in five mortgage borrowers earning less than \$30,000 a year purchased high-cost mortgages. In Atlanta and Indianapolis, more than one in four lower income homeowners purchased a high cost mortgage.

To put that in perspective, consider the other side of the distribution. In high-cost areas like San Francisco and Seattle, for instance, only between 10 and 12 percent of all lower income mortgage borrowers in each area purchased a high-cost mortgage. Lower income borrowers are still among the most likely income group in these two metros to purchase a high-cost mortgage, but that probability was substantially lower than the four areas detailed above.

Although lower income borrowers do tend to be the most likely home buyers to purchase a high-cost loan, it is important to point out that the market for high-cost loans consists of many more middle and higher income households than lower income households. In fact, lower income borrowers comprised

Across the 12 metro areas, lower income households are much more likely than higher income households to buy high-cost mortgages

Proportion of High-Cost Loans, by Household Income and Metro Area

Metro Area	Household Income						
	\$0–30,000	\$30,000–45,000	\$45,000–60,000	\$60,000–75,000	\$75,000–90,000	\$90,000–105,000	\$105,000+
San Francisco	11%	8%	8%	9%	10%	9%	6%
Seattle	12%	14%	14%	14%	12%	10%	8%
Los Angeles	12%	13%	14%	15%	14%	13%	9%
New York	12%	13%	14%	16%	16%	15%	10%
Denver	13%	16%	16%	15%	13%	10%	7%
Washington, DC	15%	17%	17%	16%	14%	12%	7%
Hartford	17%	18%	18%	16%	13%	11%	8%
Chicago	20%	21%	21%	19%	16%	14%	9%
Baltimore	23%	21%	19%	16%	14%	12%	8%
Pittsburgh	25%	21%	16%	13%	10%	8%	6%
Atlanta	25%	23%	21%	20%	16%	14%	11%
Indianapolis	25%	22%	19%	15%	13%	11%	9%

Source: Author's Analysis of 2004 Home Mortgage Disclosure Act Data.

Note: High Cost Loans are defined by the Federal Reserve; this table says, for instance, that

25 percent of the loans originated to a household in Atlanta with a median income between \$0-30,000 were high cost.

more than a fifth of the high-cost mortgage market in each of the metropolitan areas in our sample. In eight of the 12 metros, borrowers earning less than \$30,000 a year accounted for less than five percent of the total high-cost mortgage market in 2004.

Similarly, in nearly all of the metropolitan markets in our sample the largest portion of the high-cost mortgage market in 2004 earned considerably more than \$30,000 a year. And, in Los Angeles, New York, and San Francisco, a majority of the high-cost mortgages were sold to borrowers with household incomes more than \$105,000.

Because middle- and higher income households account for the majority of the market for high-cost mortgages, we can state that the demand for and supply of these

products does not depend on low-income households. In fact, in nearly all of the metropolitan areas in our sample, these borrowers account for a very small portion of this high-cost market.

Holding other factors constant, homeowners in lower income neighborhoods can pay as much as \$300 more for home insurance than those in higher income neighborhoods.

Because disclosure laws in the insurance industry are so limited, it is difficult to reliably quantify the national average prices homeowners in different income groups pay for the same insurance policy. But we can estimate these price differences by examining our sample of metropolitan areas—where nearly one out of every fourth person in

this country lives.

In seven of the nine metropolitan areas where we could obtain home insurance quotes, homeowners in lower income neighborhoods paid the highest prices for insurance.

Chicago, where the average quote for a year of home insurance in the city's lowest income neighborhoods was about \$1,043, had the sharpest price differentials across income groups. The next highest average quote in our sample was for households in neighborhoods with a median income between \$30,000 and \$60,000, for whom a year of home insurance would cost \$755. This trend holds across most of the metropolitan areas in this sample, suggesting that home insurance premiums tend to be more expensive in lower income neighborhoods.

Lower income households represent a small share of the market for high cost loans in these 12 metros

Distribution of Market Demand for High-Cost Loans, by Household Income and Metro Area

Metro Area	Household Income						
	\$0–30,000	\$30,000–45,000	\$45,000–60,000	\$60,000–75,000	\$75,000–90,000	\$90,000–105,000	\$105,000+
San Francisco	1%	3%	7%	13%	16%	16%	43%
New York	1%	6%	13%	19%	18%	14%	28%
Los Angeles	2%	7%	15%	19%	16%	13%	29%
Washington, DC	2%	11%	19%	21%	16%	11%	20%
Seattle	2%	14%	21%	21%	14%	9%	17%
Denver	4%	18%	22%	19%	12%	8%	16%
Hartford	4%	19%	25%	20%	12%	8%	11%
Chicago	4%	17%	24%	21%	13%	8%	13%
Baltimore	7%	19%	22%	18%	12%	8%	14%
Atlanta	8%	23%	23%	17%	10%	7%	12%
Indianapolis	15%	27%	21%	14%	8%	5%	9%
Pittsburgh	20%	28%	21%	14%	7%	4%	6%

Source: Author's Analysis of 2004 Home Mortgage Disclosure Act Data.

Note: High Cost Loans are defined by the Federal Reserve; this table says, for instance, that households in Atlanta that earned between \$0–30,000 a year accounted for about 8 percent of all households in the Atlanta metropolitan area that purchased a high-cost loan in 2004.

As with auto insurance, home insurance prices could be much higher for lower income drivers because of a number of personal characteristics that insurance companies factor into pricing decisions. Some of these factors, like credit scores, occupation, and education, are closely correlated with household income.¹⁰⁵ But because there are so few disclosure laws in the insurance industry, we lack sufficient data to analyze the full impact of all of these factors.

Lower income consumers tend to pay more for furniture and appliances because they are much more likely than higher income households to shop at rent-to-own establishments.

Lower income consumers are much

more likely than higher income consumers to buy furniture and appliances from rent-to-own stores. Depending on specific state regulations and the combination of products they buy, this shopping tendency can cost lower income families hundreds of extra dollars every year in higher prices for furniture and appliances.

A recent analysis by the Federal Trade Commission (FTC) found that 59 percent of rent-to-own customers earn less than \$25,000 a year.¹⁰⁶ Renting to own means that consumers pay more for a piece of furniture or electronics than if they simply bought the item outright because of numerous fees these stores charge. For instance, the Wisconsin Department of Financial Institutions estimates that a \$200

television might cost as much as \$700 at one of the rent-to-own establishments in the state.¹⁰⁷ Similarly, the Maryland attorney general's office estimates that a new \$400 washing machine would cost over \$1000 if purchased from a rent-to-own business.¹⁰⁸ The myriad additional costs rent-to-own establishments pass on to their customers—including processing fees, delivery fees, installation fees, in-home collection fees, home pick-up fees, product insurance fees, and late payment fees—account for these bloated prices.¹⁰⁹ In contrast, a consumer who bought that same washing machine with a credit card charging a 24 percent interest rate would pay just \$480 over an 18 month period.¹¹⁰

In the 12 metros, home insurance premiums tend to be higher in lower income neighborhoods than higher income neighborhoods

Home Insurance Premiums, by Area and Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Indianapolis metro	\$694	\$770	\$722	\$720	\$720
New York metro	798	668	618	600	568
Denver metro	800	838	844	800	n.a.
Baltimore metro	840	812	740	704	n.a.
Atlanta metro	866	820	754	796	n.a.
Hartford metro	916	720	730	700	n.a.
Pittsburgh metro	978	998	976	1120	1082
Chicago metro	1130	748	676	720	704
Los Angeles metro	n.a.	n.a.	n.a.	n.a.	n.a.
San Francisco metro	n.a.	n.a.	n.a.	n.a.	n.a.
Seattle metro	n.a.	n.a.	n.a.	n.a.	n.a.
Washington, DC metro	n.a.	n.a.	n.a.	n.a.	n.a.
Metro Average	\$878	\$776	\$734	\$743	\$714
Indianapolis city	694	692	740	n.a.	n.a.
Denver city	800	824	860	n.a.	n.a.
New York city	806	698	846	1,020	n.a.
Atlanta city	874	868	880	880	n.a.
Baltimore city	880	870	n.a.	n.a.	n.a.
Pittsburgh city	926	920	n.a.	n.a.	n.a.
Hartford city	960	960	n.a.	n.a.	n.a.
Chicago city	1,196	884	1,026	1,060	n.a.
Los Angeles city	n.a.	n.a.	n.a.	n.a.	n.a.
San Francisco city	n.a.	n.a.	n.a.	n.a.	n.a.
Oakland city	n.a.	n.a.	n.a.	n.a.	n.a.
Seattle city	n.a.	n.a.	n.a.	n.a.	n.a.
Washington, DC city	n.a.	n.a.	n.a.	n.a.	n.a.
City Average	\$892	\$840	\$870	\$987	n.a.

Source: Author's analysis of data collected from three major insurance companies

Note: Averages are population weighted



Why are home-related purchases more expensive for lower income consumers?

Evidence in this section has shown that lower income consumers are more likely than higher income households to buy higher-priced home loans, furniture, and appliances. Similarly, our analysis indicates that insuring a home in a lower income neighborhood is generally more expensive than in a higher income neighborhood, largely reflecting previous research on the higher costs of insuring urban homeowners. There is also evidence that at least suggests lower income home insurers may pay an additional premium, above and beyond the premium they pay for the neighborhood they live in.

To bring down these prices, leaders will need to grapple with three market dynamics that drive up these prices.

First, businesses do incur some real risks when serving lower income markets, increasing their costs.

Lower income homeowners are much more likely than higher income borrowers to fall behind on their payments, declare bankruptcy, and have low credit scores.¹¹¹ Within a metropolitan area, they are also more likely to live in urban areas, where insurance is more expensive. As is the case with all of the higher costs of doing business considered in this report, there are

many good reasons for these higher costs. But as long as these higher costs of doing business exist, businesses will rationally pass those higher costs onto lower income consumers. Importantly, the existence of these higher costs will also drive perceptions of higher costs, even when there may not be data available to support those perceptions. This also drives up prices.

Second, rent-to-own establishments are more densely concentrated in lower income neighborhoods than elsewhere, driving and responding to higher demand in those communities for rent-to-own products.

In all but one of the 12 metropoli-

tan areas in our sample, we find that the highest concentration of rent-to-own stores is in lower income neighborhoods. Atlanta is typical of this trend: For the entire metro area, there is about one establishment for every 15,808 lower income neighborhood residents. That compares to one rent-to-own establishment for approximately every 23,067 residents of neighborhoods with median incomes between \$30,000 and \$60,000, and one establishment for every 147,300 residents of a neighborhood with a median income between \$60,000 and \$90,000.

Importantly, these trends do not suggest that most rent-to-own stores are located in lower income neighborhoods. In fact, most of the 817 rent-to-own stores within the 12 metropolitan areas in our sample are located in moderate-income neighborhoods with a median income between \$30,000 and \$60,000, perhaps due to market saturation in lower income neighborhoods.

Third, unscrupulous businesses drive up housing prices for lower income families.

For instance, research on mortgage pricing suggests that between 14 and 20 percent of all borrowers who purchased a high-cost mortgage could have qualified for a better priced mortgage product, saving them hundreds or thousands of dollars in interest charges every year.¹¹² Even for those who cannot qualify for prime loans, some bad apples in the mortgage market tack on additional features to mortgage products that unnecessarily drive up costs for consumers, like long-term prepayment penalties and

In the 12 metros, rent-to-own businesses are most densely concentrated in lower income neighborhoods

Population Per Rent-to-Own Furniture Establishment, by Neighborhood Income

Geography	Median Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Atlanta metro	15,808	23,067	147,399	n.a.	n.a.
Denver metro	17,806	34,735	321,401	n.a.	n.a.
Indianapolis metro	17,912	23,565	326,950	n.a.	n.a.
Hartford metro	19,951	30,452	222,496	n.a.	n.a.
Seattle metro	21,750	44,118	191,221	n.a.	n.a.
Pittsburgh metro	23,382	66,278	218,803	n.a.	n.a.
Washington, DC metro	40,759	50,593	97,874	594,058	218,405
Chicago metro	51,019	64,199	206,724	220,249	61,172
Baltimore metro	60,440	36,757	272,332	n.a.	n.a.
New York metro	97,938	114,878	286,245	642,657	216,700
Los Angeles metro	119,524	123,187	325,273	207,819	n.a.
San Francisco metro	120,940	126,729	182,333	446,734	n.a.
Metro Average	56,218	60,166	205,617	455,597	239,798
Seattle city	17,799	106,976	n.a.	n.a.	n.a.
Indianapolis city	19,673	23,986	168,904	n.a.	n.a.
Atlanta city	20,824	50,411	n.a.	n.a.	n.a.
Pittsburgh city	21,760	132,560	n.a.	n.a.	n.a.
Denver city	22,745	95,861	n.a.	n.a.	n.a.
Hartford city	31,674	67,317	n.a.	n.a.	n.a.
Baltimore city	55,114	44,759	n.a.	n.a.	n.a.
Chicago city	74,811	121,643	124,994	n.a.	5,071
San Francisco city	84,062	342,662	344,052	n.a.	n.a.
Washington, DC city	88,329	84,904	n.a.	n.a.	n.a.
New York city	125,921	178,391	96,084	n.a.	15,075
Los Angeles city	262,636	164,654	446,436	66,113	n.a.
Oakland city	n.a.	92,645	n.a.	n.a.	n.a.
City Average	70,795	78,437	136,375	238,183	65,857

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

Most rent-to-own businesses are located in moderate income neighborhoods
Distribution of Rent-to-Own Furniture Establishments, by Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
San Francisco metro	8%	52%	36%	4%	0%
Washington, DC metro	8%	57%	32%	2%	2%
Seattle metro	11%	79%	9%	0%	0%
Atlanta metro	14%	80%	6%	0%	0%
Baltimore metro	14%	79%	7%	0%	0%
Chicago metro	16%	70%	11%	2%	2%
Denver metro	16%	80%	4%	0%	0%
Indianapolis metro	17%	81%	2%	0%	0%
Hartford metro	23%	69%	8%	0%	0%
Los Angeles metro	23%	65%	8%	3%	0%
New York metro	26%	56%	14%	2%	2%
Pittsburgh metro	50%	48%	2%	0%	0%
Metro Average	20%	68%	11%	1%	1%
Indianapolis city	23%	74%	3%	0%	0%
Los Angeles city	27%	59%	5%	9%	0%
Chicago city	32%	58%	6%	0%	3%
San Francisco city	33%	33%	33%	0%	0%
Washington, DC city	33%	67%	0%	0%	0%
New York city	36%	41%	19%	0%	3%
Baltimore city	40%	60%	0%	0%	n.a.
Denver city	40%	60%	0%	0%	0%
Seattle city	43%	57%	0%	0%	0%
Atlanta city	65%	35%	0%	0%	0%
Hartford city	75%	25%	0%	n.a.	n.a.
Pittsburgh city	83%	17%	0%	0%	0%
Oakland city	n.a.	n.a.	n.a.	n.a.	n.a.
City Average	33%	57%	8%	1%	1%

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

needlessly broad insurance plans.¹¹³ Similarly, rent-to-own businesses often charge two-to-three times the price of a product to mostly low- and moderate-income consumers.¹¹⁴

Finally, lower income consumers tend to be less informed than higher income consumers and have less access to the Internet, a key comparison shopping tool.

We've shown in previous sections, for instance, that lower income consumers generally do not shop around as much as higher income households when buying necessities; they also are less informed about credit reports. This lack of information puts them at a disadvantage when shopping in the housing market.

Additionally, lower income consumers have less access to the Internet.¹¹⁵ Without this tool at their disposal, lower income families miss out on a world of opportunities to save money. Besides having access to online listings that allow consumers to comparatively shop for houses, several companies now provide online mortgage prices, and others comparatively shop mortgage prices for consumers.¹¹⁶ Similarly, consumers can now order appliances, furniture, and electronics online, and get lower prices for those goods and services than they would pay in brick and mortar establishments.¹¹⁷ These resources can save homeowners money—but as long as lower income consumers lack access to these resources, or knowledge about them, they will not be able to use these market tools to get lower prices.



IV. GROCERIES

Lower income consumers may pay more for groceries, either through higher prices or additional travel costs to reach discount grocery stores.

Grocery stores in lower income neighborhoods tend to be smaller and more expensive than in higher income neighborhoods.

Grocery stores are smaller and more expensive in lower income neighborhoods than in higher income neighborhoods. Though this does not necessarily mean that all lower income families pay those higher prices, it does mean that lower income families often have to commute to other neighborhoods to get to cheaper food, which adds to the total costs of food shopping.

The average grocery store in a lower income neighborhood is 2.5 times smaller than the average grocery store in a higher income neighborhood.

Grocery stores tend to be much smaller in lower income neighborhoods than those found in higher income neighborhoods.¹¹⁸ As was the case throughout the country up until at least the 1960s, lower income neighborhoods tend to be still densely clustered with tiny convenience stores rather than the new, supercenter-style grocery store.

In fact, across our sample of 12 metropolitan areas, there is about one mid-sized or large grocery store (greater than 10,000 square feet) in a lower-income neighborhood for every 69,055 residents in those neighborhoods, compared to one mid-sized to large grocery store for every 29,005 residents of a non lower-income neighborhood.

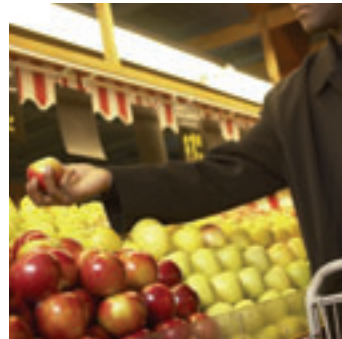
The Atlanta metro area illustrates

these general market trends. In particular, there is one mid-sized or large grocery store in one of the metro's lower-income neighborhoods for every 30,034 residents of these neighborhoods, compared to

one store for every 23,734 residents of a neighborhood with a median income between \$30,000 and \$60,000. The density of these mid-sized to large grocery stores continues to increase with household income. In fact, on

the other side of the income distribution, there is about one mid-sized to large grocery store in the area's highest income neighborhoods for every 8,426 residents of these neighborhoods.

This reinforces the fact that lower income neighborhoods generally have much less access than higher income neighborhoods to mid- to large-grocery stores, which have the space to sell lower priced goods and a more diverse variety of goods.



In the 12 metros, lower income neighborhoods have fewer mid-sized and large grocery stores than higher income neighborhoods

Population per Mid-Size and Large Grocery Store (Greater than 10,000 square feet),
by Store Size and Neighborhood Income

Geography	Neighborhood Income				
	\$0–29,999	\$30,000–59,999	\$60,000–89,999	\$90,000–119,999	\$120,000+
Denver metro	15,580	22,736	23,807	27,416	19,117
Atlanta metro	30,034	23,734	12,545	14,701	8,426
Pittsburgh metro	30,766	21,209	21,880	n.a.	n.a.
Washington, DC metro	50,949	24,950	23,872	22,848	36,401
Baltimore metro	51,805	25,270	23,343	49,119	n.a.
Los Angeles metro	61,294	49,275	33,484	29,688	56,543
Seattle metro	65,250	21,800	29,878	91,781	n.a.
Chicago metro	83,486	28,854	20,333	25,912	20,391
Hartford metro	119,707	24,915	29,666	n.a.	n.a.
New York metro	134,665	44,088	30,669	31,349	72,233
Indianapolis metro	161,206	19,033	21,797	34,358	12,870
San Francisco metro	241,879	29,954	33,490	37,228	73,327
Metro Average	69,055	31,318	25,236	28,475	38,677
Denver city	12,997	35,948	n.a.	n.a.	n.a.
Seattle city	26,698	26,744	20,740	n.a.	n.a.
Pittsburgh city	36,266	37,874	n.a.	n.a.	n.a.
Atlanta city	38,177	25,206	18,570	15,440	n.a.
Washington, DC city	44,165	55,603	91,400	16,660	35,454
Baltimore city	55,114	80,566	33,918	n.a.	n.a.
Chicago city	74,811	37,752	24,999	29,462	2,536
Los Angeles city	75,039	71,350	31,888	33,057	42,199
Indianapolis city	157,382	19,704	45,786	n.a.	n.a.
New York city	176,290	101,938	88,077	38,484	30,149
Hartford city	n.a.	n.a.	n.a.	n.a.	n.a.
San Francisco city	n.a.	34,266	28,671	34,859	n.a.
Oakland city	n.a.	138,968	40,863	29,035	n.a.
City Average	79,429	41,061	30,994	29,773	24,697

Source: Author's analysis of 2005 data from InfoUSA, and 2000 Census Bureau Data

Note: Averages are population weighted

The greater proximity and concentration of smaller grocery stores drives up food prices in lower income neighborhoods.

With groceries available mostly in smaller stores, lower income neighborhoods tend to have higher food prices than higher income neighborhoods. Prices tend to be higher in smaller grocery stores than in larger grocery stores because of the lower economies of scale, the smaller distribution channels, and because their customers tend to be more captive.

To examine this trend, we considered the price of 132 different products sold at over 3,000 grocery stores.¹¹⁹ The methods section of

dozen eggs in stores less than 10,000 square feet was \$3.03. That exact same brand of eggs cost, on average, \$2.89 in stores greater than 10,000 square feet. Similarly, the average price of a box of Honey Nut Cheerios, which was one of the best-selling products in the sample, was \$4.71 at stores with less than 10,000 square feet of retail space; \$4.56 in stores greater than 10,000 square feet. We found this strong relationship between average price and store size in all of the eleven major food categories in our sample.

Multiplied over the course of a year, and added to the premiums for other basic food items, this evidence suggests lower income families shopping at small local grocery stores can end up paying hundreds of dollars extra for food. The typical dense concentration of small stores, and the frequent absence of any grocery stores greater than 10,000 square feet, suggests that many lower income families bear this added cost.

All of this evidence supports the conventional wisdom that smaller stores charge higher prices. Our finding that smaller stores account for almost all grocery stores in lower income neighborhoods leads

The dearth of big-box, low-cost grocery stores in lower income neighborhoods indicate an unmet market opportunity.

this report provides an overview of our criteria for selecting both grocery products and stores.

Of the 132 products in our sample, 67 percent were more expensive in stores smaller than 10,000 square feet than in larger stores. For instance, the average price of a



to the conclusion that consumers in those neighborhoods pay more for groceries. Even when lower income consumers want to avoid these higher prices, they often have to commute to larger grocery stores found in higher income neighborhoods—and this commute may very well negate much of the savings they find at these larger stores.

Besides the immediate differences in prices across neighborhoods, the absence of modern, large grocery stores in lower income neighborhoods also means that there tends to be a lower a) quantity of food items, b) availability of other services, such as a pharmacy, across our population of grocery stores, and perhaps a lower overall quality as well. An analysis by Philadelphia-based Food Trust found that these important grocery store differences across neighborhoods add up to substantial (and costly) differences in the diets and health of the people in these neighborhoods.¹²⁰ Through these ways, examining just the average price difference across stores may significantly underestimate the true, higher cost of buying groceries in lower income neighborhoods.



Why do lower income neighborhoods face higher food costs?

The dearth of big-box, low-cost grocery stores in lower income neighborhoods indicate an unmet market opportunity. The reasons for this include higher costs of doing business, as well as systematic undercounts of demand, or perceived high crime rates in these neighborhoods that lead to false perceptions of high costs.

Recent evidence suggests, however, that this is generally not the case in stores that sell food to high proportions of lower income families.¹²¹ Higher costs might also relate to strict urban zoning requirements and the expense of urban land and development, which do not match the trends in this industry for bigger stores.

Frequently though, higher costs of doing business have to do with misperceptions driven by inaccurate data assessments of market

demand in lower income neighborhoods. Social Compact, for instance, has illustrated in numerous studies that traditional methods of estimating market demand systematically undercount demand in lower income neighborhoods.¹²² One company that sees enormous opportunity in lower income neighborhoods is Wal-Mart, which recently announced plans to open 150 stores in underserved lower income markets.¹²³ ■