Looking for something the government got right?

0 Like 1 Tweet 0 g+1 @

By Jeff Gelles, Inquirer Columnist

POSTED: November 18, 2013

Right about now, foes of 2010's health-care reform are gleefully pointing to the law's rocky rollout as evidence for Ronald Reagan's famous declaration that "government is not the solution to our problem; government is the problem." Even some Obamacare supporters worry it's a sign that government can't get things right.

But before you fall for a notion that helps too many Americans gloss over the government's achievements - say, Social Security, Medicare, and the moon landings - you might want to consider the epiphany reported recently by University of Chicago economist Neale Mahoney.

A professor at Chicago's business school, Mahoney decided to study another of the Obama administration's accomplishments: 2009's credit-card reform. With access to a vast trove of data from the nation's eight largest banks, he expected to find evidence consistent with the antiregulatory philosophy that has long steeped "Chicago School" economists.

Mahoney even had a tentative title in mind: "Whac-A-Mole: The Unintended Consequences of Fee Regulation in the Credit Card Industry." His expectation, fueled by arguments from groups such as the American Bankers Association, was that market forces would confound any effort to limit rates or fees. Like the mole in the arcade game, he figured, they'd just pop up elsewhere, if in another form.

That was the strongest argument against tighter credit-card regulation, despite growing public anger over practices - such as "any time, any reason" rate increases, or "over limit" fees on transactions that could simply be turned down - that consumer advocates such as Elizabeth Warren had called out as "tricks and traps" and that the Federal Reserve had finally labeled unfair and deceptive.

Sure, those may be lousy practices, the 2009 law's critics said. But borrowers would just have to fend for themselves, because it's pointless for government to try to intervene. Rules, they argued, are never a match for market forces.

But it turns out Mahoney's assumptions - and those of government's reflexive critics - were wrong.

In a working paper published last month, Mahoney and three coauthors estimate that 2009's CARD Act cut 2.8 percent from the average annual cost of credit-card borrowing. That's enough to save U.S. consumers about $20.8 billion a year in total interest and fees.

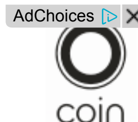
To Mahoney, who calls himself "data-driven" rather than an adherent to any particular economic perspective, the results were a revelation. He says earlier studies raised good questions about the usefulness of financial regulation. But a deep dive into this latest example of "Big Data" - years of anonymous records on 150 million card accounts - answered them.

"When we looked at the data, the results just jumped off the page," Mahoney told me. "There wasn't the expected increase in interest charges, or new revenue from any other fee category."

The savings were most dramatic for consumers with FICO credit scores below 620, who paid an astounding annual rate of 44 percent for card borrowing. And more than half came from fees, including some the 2009 law limited or barred.

The result of the new rules? Fees on those borrowers dropped more

AdChoices



All your cards. One Coin.
Pre-order now for $50

Pennsylvania MENTOR
Bringing Caring Closer
Come Join us in our expansion efforts!
Submit Inquiries of your resume via email today at
parecruitment@thementornetwork.com

We Recommend

Jeff Gelles: New regulation of credit-reporting agencies could help consumers
August 5, 2012

Discover to pay $214 million to settle charges of deceptive marketing
September 26, 2012

Find More Stories About

Credit Card

Market Forces

than 60 percent. And there is no evidence that the banks - which he says profited from those borrowers even through the worst of the financial crisis - managed to raise their interest rates to compensate. In other words, the mole stayed whacked.

Safari Power Saver
Click to Start Flash Plug-in

Nor were the benefits limited to those with the worst credit histories, perhaps because banks profited from practices, such as charging late fees when a payment arrived on its due date but after noon, "that could trip up all but the most sophisticated customers," Mahoney says.

For all customers they studied, the average interest rate dropped about 1 percentage point after the law took full effect, to about 13 percent. But by limiting nuisance fees, the average customer's total borrowing costs dropped nearly three times as much, from about 22 percent to about 19 percent.

Mahoney's theory is that banks, forced to cut fees customers were overlooking or unable to avoid, were constrained by market forces from raising interest rates - something they did notice.

"This shows that financial regulation can benefit customers, and that the markets won't always be able to adapt to unravel its effects," Mahoney says.

In other words, sometimes government can do just what it intends.

jgelles@phillynews.com215-854-2776

@jeffgelles www.inquirer.com/consumer

Flights to Los Angeles

united.com

Fly to Los Angeles, CA and Get Our Guaranteed Lowest Fare.

FEATURED ARTICLES

Marple Newtown High mourns loss of man slain over headphones

Family affair: The making of Michael Carter-Williams

'Babe' Heffron, 90, hero of 'Band of Brothers'

More:

In Bulk Trucking, Chemical Leaman Is Rolling Toward The Top

Frank Nofer, 71, famed graphic artist

George Mattson, 88, Olympian, Crew Coach

De Mazia Art Brings $2.38 Million

Leader Of Jbm Sentenced To Life Aaron Jones Was Convicted Of Conspiring To Distribute $100 Million In Cocaine. He Plans To Appeal.

Jbm 8 Believed Founders