



iStockphoto

# Credit Crisis **SQUEEZES** Car Buyers

A new partnership between a nonprofit and the banking sector is helping people who have poor credit get financial education, repair their financial standing, and buy a decent car. And not a moment too soon, say advocates for the poor, given that some lenders who made bad home loans before the meltdown are hanging out their auto-loan shingles.

by Debby Miller, More Than Wheels

## Buying a Car with Bad Credit

Most of us get up in the morning and get into a car that we know will start and will take us to our destination. (See “Means of Transportation to Work.”) But imagine for a moment that your car needs costly repairs and that you cannot purchase a new car because your credit is bad. Worse yet, imagine having a shot at a job that would allow you to become self-sufficient but no way to get there—no car, no public transportation at the hours you need it. (See “Transportation to Work, by Workers’ Annual Earnings,” p. 9.)

is nearly impossible to purchase a functional car at a fair price with affordable financing. Buyers with damaged credit pay excessive prices for older—often unsafe—vehicles at interest rates that are three or five times the rate available to other borrowers. Soon their car needs repairs costing too much for families living from paycheck to paycheck. The car may die before it is paid for or be repossessed soon after the first payment.

Owning a car should help people get out of poverty and into stable employment and a better way of life, not the opposite. Consider the following facts:

than those with poor credit.

Good credit improves opportunities for rental housing, employment, and access to savings and investment accounts. That is why working on credit repair is so important.

## A Purchase that Rebuilds Credit

In 2001, Robert Chambers and Leo Hamill started a nonprofit organization to meet the transportation needs of consumers who had credit problems. It would allow them to purchase new or gently used cars and would provide the financial education and credit-repair tools to create lasting change. That year, the nonprofit More Than Wheels (then called Bonnie CLAC) started up in New Hampshire. Since then, it has helped roughly 1,500 families purchase affordable, reliable, fuel-efficient cars with only a 5 percent default rate. The program expanded into Massachusetts in 2010.

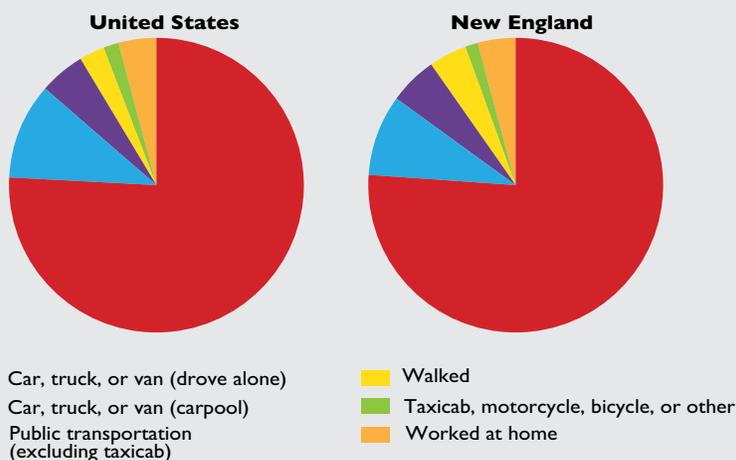
The organization and local lenders agree on rate, terms, and underwriting criteria for clients. More Than Wheels then offers clients a six-week financial education course (including tips on car safety and basic maintenance), credit-repair coaching, counseling on insurance and the like, and help with developing a positive payment history. The lender approves the loan with a low interest rate on the basis of the agreed-on criteria and the changes observed in financial behavior over four to 12 months, depending on the severity of the credit issues. More Than Wheels mitigates risk to the lender through a loan guarantee in case of default. Thus lenders can make loans to borrowers they would not have normally been able to engage, boosting overall loan production.

More Than Wheels gives people a better way to buy a car, providing a proven and effective set of tools that helps them get back on the road to financial freedom. The program demands hard work and diligent financial planning, but the results have been life-changing for customers willing to see it through. The automobile purchase becomes a catalyst to change financial decision making and to encourage choices that build better credit scores and improve economic well-being. Additionally, consumers gain intangible benefits such as empowerment, responsibility, and self-confidence.

The keys to the initiative’s success include the following:

- a focus on new cars and good (2-3-year-old) used cars;
- a guarantee of loans at reasonable

### Means of Transportation to Work



Source: 2005-2009 American Community Survey, U.S. Census Bureau.

For many New Englanders, having a reliable car can mean the difference between getting to a job on time and not being able to get to a job at all. If you have good credit, you can usually purchase a personal vehicle for a reasonable amount. Otherwise, the options are few. That has been especially true since the recent economic collapse.

According to the U.S. Department of Transportation, 91 percent of Americans use a personal vehicle to commute to work. Residents of some urban centers may have good public transportation, but other cities’ design and the migration of jobs to the suburbs make obtaining and holding a job without a car difficult. The need is especially acute for single mothers trying to get children to day care before work and for employees who have jobs far from home. Families with income above \$25,000 are nine times more likely to have a car than families with income below \$25,000.

Without a car, a low-income family’s opportunities are limited. But if they buy one when they have credit issues, they may find their car is more of a liability than an asset. It

- Unscrupulous lenders often coerce borrowers into borrowing more money than they can afford, leading to rapid repossession, while easy access to credit may entice consumers to select ultimately unaffordable models;
- Using a predatory loan to purchase an old, high-mileage car can cost \$10,000 to \$15,000 more than a traditional loan on a new car over the life of the automobile; and
- In 2005, the average American family spent 20 percent of its household income on transportation, but the poorest one-fifth paid 42 percent.<sup>1</sup>

Many people with poor credit borrow from friends or family or turn to payday lenders, rent-to-own centers, and “Buy Here Pay Here” car lots that can become money traps. But those who improve their credit can avoid predatory lenders and work with mainstream financial services. According to a 2004 CBS Marketwatch program, those with good credit pay approximately \$250,000 less in overall interest through their working lives

- interest rates through unique banking partnerships;
- a program proven to rebuild credit ratings for the long term;
- an effective personal financial course that changes behaviors;
- a focus on giving people the chance to improve their economic position;
- comprehensive support of the car-buying process from beginning to end; and
- ongoing support and advocacy for the life of the loan.

Empowered with new knowledge and skills, many of the participants are now able to improve their job situation, their family's overall well-being, their credit, and their financial stability. In a survey conducted by the University of New Hampshire's Carsey Institute, 75 percent of More than Wheels participants reported spending less on car repairs, 73 percent reported a better overall financial outlook, 50 percent were better able to get to their jobs, 52 percent had improved access to health care, and 38 percent had improved access to nutritious food options. Additionally, More Than Wheels has launched an annual review of credit reports to determine change in credit scores.

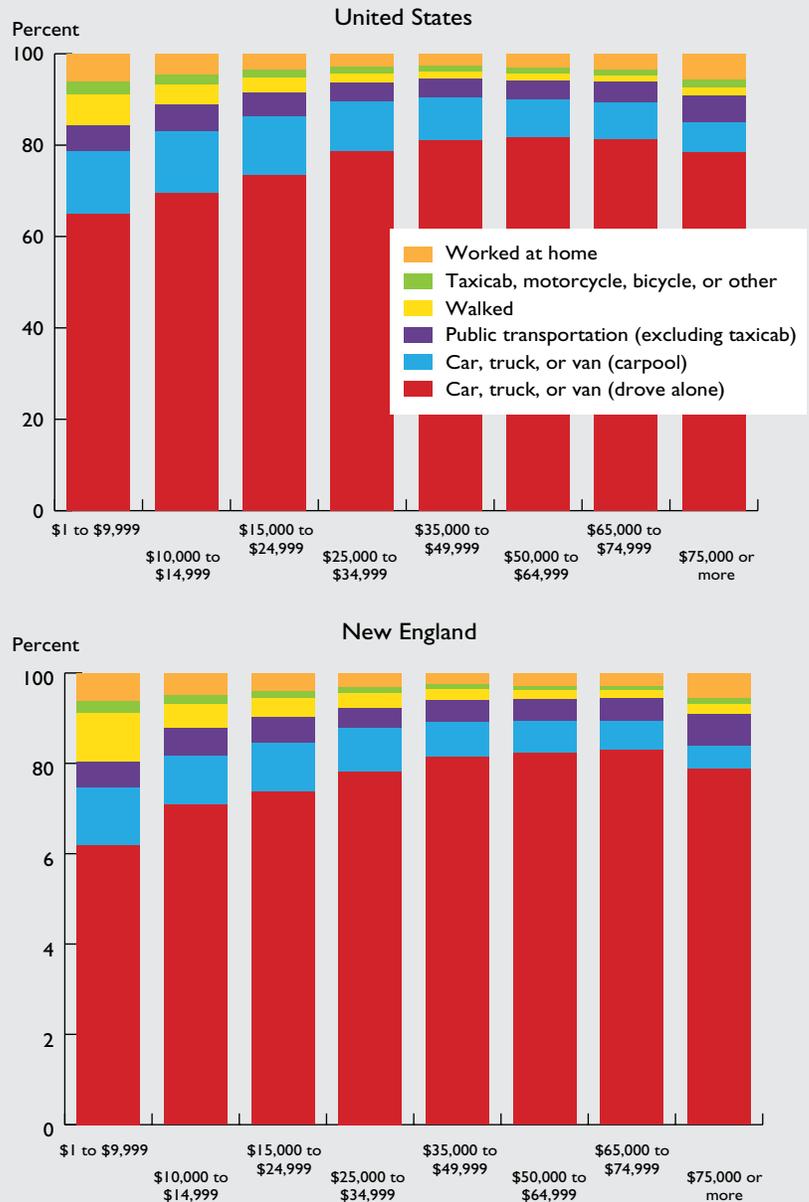
The people at More Than Wheels believe that personal-vehicle lending is not just about the car. There is much more that needs to be addressed. Although other entities are suddenly getting into auto lending for people with poor credit, they are not doing credit rehabilitation. In a way, it is good to hear that anyone is thinking about serving the needs of credit-challenged people who need reliable transportation. Nevertheless, if lenders fail to get to the root of what caused clients to be in their situation in the first place, they are just setting them up to commit the same mistakes again.

Lending to consumers with bad credit without providing financial education sends the wrong message, and that message is that it's OK to have bad credit and poor spending habits. Consumers need to get out of the doomed spiral of poverty. They need to learn how to take control of their financial lives and pass along that powerful knowledge to their children.

## Financially Healthy Consumers

More Than Wheels sees a wonderful opportunity for banks and nonprofits to work together. They have a lot to learn

## Transportation to Work, by Workers' Annual Earnings



Source: 2005-2009 American Community Survey, U.S. Census Bureau.

from each other and together could expand the thoughtful approach described here to helping those who not only need reliable transportation but also have the desire to become financially stable. Working together, banks and nonprofits can ensure that good lending occurs and can fulfill that customer desire.

Such partnerships lend themselves to proactive assistance to consumers before the loan gets made. Community development groups and others should consider providing help to consumers in the form of financial education and credit repair, with the More Than Wheels program as a model. Positively changing behaviors

of consumers who have had past credit and money problems not only helps those who have struggled financially in the past but also creates a better customer base for banks. Consumers' need for transportation presents an opportunity that can benefit many stakeholders, but it takes thoughtful lending to create strong, sustainable borrowing.

**Debby Miller** is New Hampshire executive director of More Than Wheels. She is based in Manchester.

### Endnote

<sup>1</sup> See <http://www.transact.org/library/factsheets/equity.asp>.