THE DEBT GAZETTE

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CLIENT NEWSLETTER

Be Wary of Apps that Offer Zero Percent Interest Loans

Since COVID has slashed foot traffic to traditional brick and mortar stores, online shopping has skyrocketed along with innovations in payment alternatives. Among these new developments, you will find small-dollar amount installment loans you can repay monthly without paying interest.

Zero Percent Interest Loans through Apps: What Could Go Wrong?

Why should consumers not jump into 0% interest loans through new app-based lenders?

Although growing in usage, 0% interest installment loans through companies like *Affirm*, *Afterpay*, and *Klarna* will still lead a large portion of consumers to overextend themselves in debt. Many borrowers will also run into high late-payment fees or negative effects on their credit rating.

Recently launched apps that offer zero-interest, short-term loans for making in-store purchases have exploded onto the consumer scene this year. Store after store is teaming up with these apps to offer their customers a 3-, 4-, or 6-month financing option at the checkout stand. All proponents of these services focus almost exclusively on the 0% interest, not on the amount of debt the consumer is accruing. It's still debt, which can overwhelm any household budget at high levels.

It's Still Debt

Looking at data from The Ascent, consumers clearly use debt vehicles like credit cards and new zero-interest loan apps to make purchases they can't afford. Add the 38.4% who make purchases that don't "fit" into their budget to the 24.7% who don't want a credit check (usually because their credit rating fits the description of "precarious" due to debt troubles), then add another 14.4% who can't get a credit card (almost always due to poor past debt issues or to being new to credit), and finally add the 14% who already have a maxed out credit card or two. Since respondents could choose more than one answer, the total of consumers who buy now and pay later because of debt troubles falls somewhere between 38.4% and 92%. Even at 38.4%, that means more than one in three borrowers cannot afford the purchase but place it on credit in order to pay for it later.

What would lead anyone to believe that delaying the payment improves anyone's ability to repay the loan? Many of these households incur so much consumer debt that their minimum monthly payments already max out their budget. In such cases, high interest rates might make things worse, but low or 0% interest rates on loans will not fix the problem.

To be direct, zero-interest loans will not solve over-borrowing problems. In fact, such low-interest and easy-to-access credit programs will actually accelerate household debt. High debt balances mean larger minimum monthly payments which raise the likelihood of missed payments and a household's inability to pay for basic needs.

Great for Retailers

Companies who have created and who manage these apps will earn revenue from fees and from agreements with retailers. Good for them!

Credit card companies may lose a lot of business to these options when consumers choose to use these apps because they offer greater clarity regarding the resulting debts but also because of their ease of repayment when compared to credit card purchases. Credit card companies have long prospered by charging interest month after month on consumer purchases that happened months or even years in the past. Too bad for them!

Consumers will use these apps to fuel overspending, not lower debt levels. Higher debt balances will mean more missed payments, larger monthly installment payments, and less money to spend on their needs and wants. Not so good for them!

Retailers will minimize the credit card transaction fees they currently pay while increasing sales due to these new and easy-to-use services that promote consumer spending. Great for them!

Rather than laud these services as benefits for consumers, we need to keep in mind who benefits from them and who does not. Retailers stand to benefit most, followed by the app companies, while consumers will likely incur more debt and credit card companies will lose business.

It Will Affect Your Credit

Zero-interest loans and low-interest loan apps will likely lead to changes in borrowers' credit rating. Interest rates play no direct role in credit scores. The FICO score considers a consumer's payment history, the status of their debts, how old or how new their accounts are, and how much the consumer carries month-to-month on their account balances. However, of the 132 FICO score factors, not a single one refers to or looks at interest rates.

Consequently, these new zero-interest loans will have no direct effect on consumer credit ratings. However, as consumers' debt balances rise and they begin missing payments because of over-indebtedness, credit scores will likely begin dropping.

Late Fees

These zero-interest loans do not always come without related fees. For example, Klarna charges a $7 monthly fee if the consumer misses a payment. For a $500 purchase, a $7 monthly fee equates to $84 annualized fee or a 17% APR.

The app, Affirm, currently charges no late fees. Instead, Affirm actually charges interest on their small loans.

Afterpay charges an initial $10 late fee but will add another $7 fee if the payment does not arrive within a week of its due date. *Afterpay* also caps their late fees so that they do not amount to more than 25% of the original purchase amount.

Additional Fees

Besides late fees, some apps and loan services charge "origination" fees, meaning they charge you a fee at the time of purchase, as well as monthly membership fees. Although membership-based apps advertise their low 0% APRs on loans, their membership fees basically raise even these 0% APRs to anywhere from 10% to 50% interest rates, depending upon how much debt you have incurred.

Featured Online Resource

What Is Savings and Why Don't More Households Save?

Here is the problem with all these pieces of advice: they treat savings as if it were a number to compute or an account to open. It is not.

Savings is one thing and one thing only: **Savings is a Commitment.**

Pure and simple. Most American households can afford to save money each month, so why don't they? It is not because of the dollar amount. It's because of the commitment.

You prioritize what you commit to in life. Most people commit to anything they see as immediately beneficial to them or to those they love. Even though you do not think about it, you are committed to breathing. You do not count your breaths per minute. You do not measure the volume of oxygen you inhale. You are committed to breathing and you just do it. Whatever it takes. Saving is the same way. If you are committed to saving, you will just do it. You will care less about how much you save with each paycheck. You will worry less about how much you have in your accounts. You will, instead, automatically save something every time you receive income.

How to Commit to Saving Money

This analogy begs the question, "how do you commit to savings?" You involuntarily commit to breathing, even as a newborn. You can choose to stop breathing, at least until you pass out. Then, you start breathing again. What about savings? How do you make savings as involuntary as breathing? The following seven steps will take you through the process of first making your savings meaningful, then making your savings reliable, and finally making your savings as involuntary as possible.

Find more free guides and resources online at MoneyFit.org/Academy.

Chat with Us Live Every Week

Money Fit LIVE

Each Thursday at 1:30 pm Eastern/10:30 am Pacific, join our education manager, Todd Christensen, for a live chat and pre-recorded 10- to 15-minute video on financial topics of interest. Learn tricks and hacks from the video, get your questions answered via chat, and find out how other participants have delt with their financial challenges.

Go to MoneyFit.org/live to access this video and chat.

Experian's #CreditChat

Every Wednesday at 3:00 pm Eastern/noon Pacific, Experian hosts a #CreditChat on Twitter addressing timely and relevant topics, from credit and debt to budgeting and financial goals. Our education manager has often participated as a panelist but always shares ideas, trips, and tricks related to the discussion.

Go to MoneyFit.org/creditchat to join or learn more.

Webinar Showcase

Stop Punching Holes in Your Money Bucket

On Thursday, December 3, 2020, author and Debt Reduction Services education manager, Todd Christensen, led a live chat during the premier of our newest webinar, “Stop Punching Holes in Your Money Bucket.” As part of our Money Fit LIVE webinars that premier every Thursday at 10:30 am Pacific, 1:30 Eastern, this online presentation included a pre-recorded video discussion of the topic combined with live chat opportunities to ask questions and share relevant insight and personal experience.

Anyone who watches the webinar can also receive the personalized, corresponding certificate of completion in PDF format via email after completing the request and providing the passcode noted in the webinar.

Find this and other previously premiered Money Fit LIVE webinars at https://moneyfit.org/live-archive or join us any Thursday mid-day for our latest premier at https://moneyfit.org/live.

Debt Reduction Services News

We Value Our Clients

As we strive to fulfill our Customer Experience vision “to make a difference in our clients' lives by making their experience personal, efficient, and educational,” we appreciate great quotes to guide our idea of how we want you to experience our services at Debt Reduction Services, Inc., whenever you need us or want to discuss your account:

- "When you assume negative intent, you're angry. If you take away that anger and assume positive intent, you will be amazed." Indra Nooyi (former chairman and CEO of PepsiCo)
- "Customer service shouldn't just be a department. It should be the entire company." Tony Hsieh (former CEO of Zappos)
- "I've learned that people will forget what you said. People will forget what you did. But people will never forget how you made them feel." Maya Angelou (poet and civil rights activist)

We Are Here to Help Your

Debt Reduction Services, Inc.

Toll-free (866) 688-3328

DebtReductionServices.org