

USURY, INVESTMENT AND THE SUB-PRIME SECTOR

**Richard Higginson, Michael Parsons
and David Clough**

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The sub-prime sector

The sub-prime sector for lending has gained wide notoriety in recent months as a result of the part it played in precipitating a crisis in the global credit market. Mortgage loans made in the United States with insufficient regard to borrowers' ability to pay were 'securitized' — sold on to other investors in a secondary market — and when the underlying loans were found to be of much less value than expected, many financial institutions found themselves under severe pressure. In this context, the focus of concern on the sub-prime sector has largely been consequences for lenders and investors in mortgage-based securities, as well as for the very serious knock-on effects for other companies and individuals. The primary focus of this report, in contrast, is the impact of sub-prime lending on *borrowers*. It seeks to relate traditions of thinking about the ethics of lending in the Jewish and Christian traditions to the 21st century context of the sub-prime lending market in order to address the question of whether it is ethical to invest in companies with exposure to the sub-prime market.

Sub-prime lending is lending primarily directed to those who do not meet conventional criteria of credit-worthiness. The sub-prime sector can be divided into two main categories. The traditional sub-prime market, referred to as 'home credit' in this report, is the offering of small unsecured loans at high interest rates to consumers with low incomes, with repayments often collected door-to-door on a weekly basis. The second category, 'sub-prime secured lending' provides mortgage and home equity loans secured on property to those who have difficulty in obtaining credit elsewhere. The home credit category has dominated the debate about sub-prime lending in the United Kingdom; the category of sub-prime secured lending is more prevalent in the United States and has attracted more scrutiny there.

Home credit

Access to and use of consumer credit have expanded enormously over recent decades. This wider use of credit accentuates the exclusion experienced by those who cannot access mainstream credit facilities. Although there is a widespread perception that credit can be obtained very easily, in 2002 as many as 7.8 million consumers in the UK (around one in five households) were denied access to mainstream credit.¹ This is credit provided by a high street bank, building society or large finance house and consists, typically, of overdraft facilities, personal loans, credit cards, store cards or hire purchase agreements. Many more potential customers are thought to exclude themselves from mainstream credit because they believe — probably with some accuracy — that they are likely to be refused.

Home credit offers small, short-term, unsecured cash loans. They typically vary from £50 to £500, with the average value of a home credit loan being around £300. Loans are repaid, generally within a year, in weekly instalments that are collected from the customer's home by agents of the lenders. The loans tend to be used to pay for essentials rather than luxuries.

¹ National Consumer Council report *Home Credit: an investigation into the UK home credit market*, 2004, p.2. The report was written by Claire Whyley and Steve Brooker.

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The Competition Commission's 2006 report into the Home Credit Market identified some 430 home credit lenders, most of them small enterprises, but including 22 that they classified as large or medium.² Of the six largest lenders, five are public companies listed on the London Stock Exchange. These are Provident Financial (easily the largest, with around 60% of the market), Cattles, London Scottish Bank, S & U, Park Group and Mutual Clothing & Supply Co. Ltd. In 2004 home credit lenders lent about £1.5 billion to around 2.3 million customers, and collected around £1.9 billion in repayments.³

The home credit industry serves a vulnerable, low-income customer base, drawn from socio-economic groups D and E. A typical customer is female, under 35, unemployed, and living in housing rented from a local council or housing association.⁴ Customers' financial circumstances are often unstable; some have a history of bad debt and a damaged credit rating. They often have low levels of financial literacy, little knowledge of alternative financial products and come from a family tradition of home credit use. The agents employed by home credit companies are frequently former customers who can readily identify with the people they are now serving. They are therefore often sympathetic to customers' struggles, and where customers cannot make their repayment for a particular reason one week this is often permitted without penalty.

Home credit companies are licensed. Most are members of the industry's trade body, the Consumer Credit Association (CCA).⁵ This publishes a Code of Practice and a Business Conduct Pledge to which members subscribe.

There are also non-commercial organisations that offer loans to poor people. Community credit unions are mutual savings and loan institutions owned and run by members who have some common bond, such as living and working in a particular locality. They were set up with two main objectives: to promote saving among people on low incomes and to provide access to low-cost credit. Community credit unions provide a positive model but they do not yet offer a viable alternative to the home credit industry. Their national coverage is patchy, they require members to be able to save regularly (albeit a minimum amount of £1 a week) and they do not offer a home collection service for repayment.⁶

Since 1988 (and revised in 1998), the Government has run a Social Fund which supplements mainstream social security provision in two forms: a regulated scheme made up of maternity, funeral, cold weather and winter fuel payments; and a discretionary scheme including repayable budgeting and crisis loans. These Budgeting Loans come closest to providing an alternative to home credit. They are available to people in receipt of Income Support and Job Seekers Allowance, and are intended to help with one-off, unexpected, or large lump-sum expenses. Loans are made in cash and are interest-free. The Social Fund is a useful provision, but it is

² Competition Commission *Home Credit Market Inquiry: Provisional Findings Report*, 2006, section 2.57.

³ *Op.cit.*, 4.

⁴ *Home Credit*, p.3.

⁵ *Op.cit.*, p.11.

⁶ *Op.cit.*, pp.34-36.

cash-limited, bureaucratic (requiring written applications) and inflexible: budgeting loan recipients do not have the option of missing the occasional repayment.⁷

In addition, poor people are also offered credit by unlicensed moneylenders, often known as 'loan sharks'. These are most prevalent among the most deprived communities, such as high-rise estates. They target people whose need for loans is desperate, and whose access to other forms of credit is most problematic.⁸

The licensed home credit industry therefore seems to be meeting a clearly defined need, for poor people to be able to borrow money in a way with which they are comfortable.⁹ This credit is notable for several distinctive features:

- Simple access — the minimum of paperwork and bureaucracy is important for people with low literacy skills or a history of financial problems
- Loans made in cash — that is the medium of exchange customers are familiar with, many making little use if any of a bank account
- Weekly repayments — this provides a discipline which stops customers getting hopelessly into debt
- Personal visits — customers appreciate the relationship which they can build up with the company agents
- Flexible arrangements — these are important for coping with short-term cash flow problems.

Research indicates that most of its customers are content with the service it provides. However, practice in the home credit industry has been subject to searching criticism, notably from the National Consumer Council. Their 2004 Report identified six features of the home credit market that are having an adverse effect on an already vulnerable group of customers¹⁰:

- Little evidence of switching — customers are either ignorant of more advantageous credit provision or simply fail to use it
- Significant switching costs — early settlement costs tend to penalise customers, who often get 'locked into' repeat purchases
- Information asymmetries — sellers are usually better informed than buyers
- High market concentration — dominated by a small number of major companies, with one (Provident Financial) having a dominant position
- Barriers to entry for new suppliers — there are high start-up costs, and reputational factors which deter other financial institutions from entering the market
- High prices — the National Consumer Council claiming that average APRs (Annual Percentage Rates) for the sector are 177%, and that even after taking into account the costs of doorstep collection, a revised figure of 82% APR is still high.

The Competition Commission has subsequently investigated the home credit industry and published its provisional findings in 2006. It concentrated on the final complaint (that of high pricing) and upheld it, recognising that several of the other features

⁷ *Op.cit.*, pp.36-37.

⁸ *Op.cit.*, pp.37-38.

⁹ *Op.cit.*, pp.19-21.

¹⁰ *Op.cit.*, pp.4-6.

contributed to bringing it about. The Commission found that ‘the prices of home credit loans, however measured, were high by comparison with the prices of other credit products’¹¹, the TCC (Total Cost of Credit) often amounting to twice or more as much. They took the view that home credit companies were making unreasonable profits in excess of the cost of capital. In response, the companies — notably Provident Financial — have defended their pricing strategy and criticised the Competition Commission’s analysis of profitability.¹²

This is the context in which the question of whether the Christian Churches might appropriately invest in this part of the sub-prime market has arisen. Of the five publicly listed companies cited earlier, Provident Financial is the most likely to attract investment, because it is the largest. However, the issue of investment in the sub-prime sector is also relevant to bigger, better known financial institutions, because they are potential or actual acquirers of home credit companies. Thus far the major banks have largely avoided the home credit industry. The National Consumer Council report attributes this to reputational risk: ‘Although it has improved its image over recent years, a degree of stigma remains attached to the industry. In particular, this is because it targets people on low incomes and charges high interest rates.’¹³ However, HSBC did acquire Household International, a company operating in a similar sub-prime market in the USA, in 2002. This aroused surprise and attracted criticism; HSBC had has problems with the company and is now selling parts of it off.¹⁴

Sub-prime secured lending

While sub-prime mortgage and home equity lending has its roots in programmes to increase home ownership in the United States in the 1960s and 1970s,¹⁵ the market has expanded rapidly in recent years. Sub-prime mortgage originations in the U. S. grew from \$34 billion in 1999 to \$213 billion in 2002, representing 8.6% of originations in that year.¹⁶ Since 2002, the expansion has accelerated, accounting for 13–14% of the market in 2007.¹⁷ While most borrowers could afford the loans they were sold in a period of rapid house price rises and low interest rates, when these conditions changed foreclosure rates rose rapidly, and the Federal Reserve Board

¹¹ *Home Credit Market Inquiry*, section 6.

¹² Provident Financial website,

www.providentfinancial.com/plc/About_us/Consumer_credit_regulation.aspx

¹³ *Home Credit*, p.60.

¹⁴ See *The Independent*, 23 October 2007,

<http://news.independent.co.uk/business/news/article3087293.ece>. For a social scientific perspective on the continued prevalence of home credit, see: A. Leyshon, D. Burton, D. Knights, C. Alferoff and P.

Signoretta, ‘Towards an ecology of retail financial services: understanding the persistence of door-to-door credit and insurance providers’, *Environment and Planning A* 36(4) (2004), pp. 625 – 645.

¹⁵ Gregory D. Squires, *Why the Poor Pay More: How to Stop Predatory Lending* (Westport, CT: Greenwood, 2004), viii.

¹⁶ United States General Accounting Office, *Consumer Protection: Federal and State Agencies Face Challenges in Combating Predatory Lending* GAO-04-280 (Washington, D.C.: General Accounting Office, 2004), URL: <<http://www.gao.gov/cgi-bin/getrpt?GAO-04-280>>.

¹⁷ Roger T. Cole, Director, Division of Banking Supervision and Regulation, Federal Reserve Board, ‘Subprime mortgage market’, testimony before the U.S. Senate Committee on Banking, Housing, and Urban Affairs, March 22, 2007, URL: <<http://www.federalreserve.gov/newsevents/testimony/cole20070322a.htm>>.

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judged that the number of loans defaulting shortly after origination is evidence of lax underwriting and possible fraud by sub-prime lenders.¹⁸

In response to abuse of customers in the sub-prime market, the category of ‘predatory lending’ has been developed in the U. S. This has been defined by the General Accounting Office as ‘cases in which a broker or originating lender takes unfair advantage of a borrower, often through deception, fraud, or manipulation, to make a loan that contains terms that are disadvantageous to the borrower’.¹⁹ It identifies practices associated with predatory lending as:

- excessive fees ‘that greatly exceed the amounts justified by the costs of the services provided and the credit and interest rate risks involved’
- excessive interest rates ‘that far exceed what would be justified by any risk-based pricing calculation’
- single-premium credit insurance, which ‘unnecessarily raises the amount of interest borrowers pay’
- lending without regard to ability to pay, leading to quick foreclosures, (sometimes where payments have exceeded monthly income)
- ‘loan flipping’: repeated refinancing for which high fees are charged with no benefit to borrower
- fraud and deception
- prepayment penalties, when used to trap borrowers in high-cost loans
- balloon payments, where loans contain a final balloon payment the borrower is unlikely to be able to afford.²⁰

Not all sub-prime lending is predatory in these terms: the U. S. Department of Treasury and the Department of Housing and Urban Development recognize that ‘the emergence of a subprime mortgage market has enabled a whole class of credit-impaired borrowers to buy homes or access the equity in their homes’.²¹ However, the overwhelming majority of predatory lending takes place in the sub-prime market, which means the sub-prime market is a legitimate locus for concern in relation to ethical investment.

In a report in April 2006 detailing action in relation to a shareholder resolution the General Board of Pension and Health Benefits of the United Methodist Church advanced a similar definition of predatory lending, and referred it to their investment policy:

Predatory lending is a form of subprime lending characterized by unscrupulous or unethical lending practices. These practices can include the application of excessively high fees and interest rates, the use of balloon payments, flipping (successive refinancing of the original loan at increasingly higher rates), packing (linking the issuance of the loan to the purchase of some

¹⁸ Cole, ‘Subprime mortgage market’.

¹⁹ United States General Accounting Office, *Consumer Protection*, 18.

²⁰ United States General Accounting Office, *Consumer Protection*, 18.

²¹ Cited in United States General Accounting Office, *Consumer Protection*, 22.

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form of insurance) and steering (directing otherwise credit-worthy borrowers into high-priced subprime loans). Predatory lending tends to target certain segments of society, most often the elderly, the poor and minorities. The United Methodist Church has directed all general agencies to invest in banks that have “policies and practices that preclude predatory or harmful lending practices.” (Resolution 213, Investment Ethics).²²

Gregory Squires cites examples of predatory lending that bring these statistics and categories to life:

Take the case of Florence McKnight, an 84-year-old Rochester widow who, while heavily sedated in a hospital bed, signed a \$50,000 loan secured by her home for only \$10,000 in new windows and other home repairs. The terms of the loan called for \$72,000 in payments over 15 years, at which point she would still owe a \$40,000 balloon payment. Her home is now in foreclosure.

And there is the case of Mason and Josie, an elderly African American couple with excellent credit and a primary source of income from Mason’s veteran benefits. A broker convinced them to consolidate their 7 percent mortgage with some credit card debt. The first mortgage for \$99,000 was at 8.4 percent, but the broker added a second mortgage for \$17,000 at 13 percent. The initial loan financed almost \$6,000 in broker and third party fees, and both loans contained prepayment penalties for three and five years, respectively. In addition, both loans had balloon payments after 15 years. After making monthly payments of almost \$950 for 15 years, they will face a payment for \$93,000.²³

Patricia McCoy makes clear the sophistication of predatory lending practices:

Predatory lending has a certain perverse genius. That genius lies in targeting cognitive anomalies in financial decision making by individuals and masterminding marketing techniques to exploit those anomalies, all to disastrous effect for borrowers. Predatory lenders make attractive terms salient and obscure the terms that might pose concern. They hunt down home owners in financial straits and capitalize on the desperation that fuels risk-taking to snare their assent. They give a hard sell on credit life insurance, knowing that people will overpay for it.²⁴

Her analysis makes clear that it is not only obvious criteria such as interest rates and fees that characterize predatory lending, but the way in which products are marketed:

Once vulnerable prospects are identified, lenders aim to lock them in psychologically and immediately. Rapid loan approval is key. So are high-pressure closings. By accelerating the loan process, lenders reduce the chance

²² General Board of Pension and Health Benefits of the United Methodist Church, ‘On Your Behalf - April Report’ (April 2006), URL: <http://www.gbophb.org/sri_funds/oyb/200604.asp>.

²³ Squires, *Why the Poor Pay More*, 1.

²⁴ Patricia McCoy, ‘Predatory Lending Practices’, in Squires, *Why the Poor Pay More*, 94.

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that borrowers will comparison-shop, making it easier for lenders to insert exploitative terms into loans.²⁵

In response to concerns about the sub-prime lending market, in December 2007 the Governors of the Federal Reserve recommended a change to the financial regulations to prohibit creditors from:

1. engaging in a pattern or practice of extending credit based on the collateral without regard to consumers' ability to repay;
2. making a loan without verifying the income and assets relied upon to make the loan;
3. imposing prepayment penalties in certain circumstances; and
4. making loans without establishing escrows for taxes and insurance.²⁶

A final point to note about the sub-prime secured lending market is that given the growth in securitization of mortgages, investors in sub-prime lending may be at a significant distance from the organizations involved in making the loan to the consumer: often investing in companies holding mortgage-based securities rather than directly in financial companies making loans. This increases the difficulty of being clear about the circumstances in which loans have been made, and highlights the need for procedures to ensure adequate scrutiny of the character of mortgage-related investments.

In making decisions about investing in the financial services industry, in addition to understanding the home credit and sub-prime secured lending markets, the Churches also have their theological and ethical heritage to consider. What is the relevance of the biblical and traditional teaching on usury to the present context? Interest is now a widely accepted part of the global financial system; indeed it may even be regarded as the bedrock of the system. The contemporary Christian Church by and large accepts interest, but the notion of usury lives on in the idea of unreasonably high or extortionate rates of interest. At the same time, there are also parts of the Church — challenged by the emergence of an alternative financial approach within Islam — who question the acceptance of interest altogether. An account and evaluation of the Christian tradition will therefore provide the basis on which to make an appraisal of the sub-prime market as a potential avenue for church investment.

Biblical texts: the Old Testament

There are several texts in the Old Testament which mention the charging of interest. The most explicit and detailed are three passages found in the Torah.

²⁵ McCoy, 'Predatory Lending Practices', 92. Mews and Abraham echo this point: 'We would like to suggest that it is not merely the rate of interest that is charged that may, or may not, make a financial product usurious or predatory, but also the circumstances surrounding the loan – to whom it is made, and what it is made for.' (Constant J. Mews, and Ibrahim Abraham, 'Usury and Just Compensation: Religious and Financial Ethics in Historical Perspective', *Journal of Business Ethics* 72 (2007), 9).

²⁶ Board of Governors of the Federal Reserve System, Division of Consumer and Community Affairs, 'Proposed Amendments to Regulation Z (Truth in Lending)', December 12, 2007 (<http://www.federalreserve.gov/BoardDocs/Meetings/2007/20071218/memo.pdf>).

Exodus 22:25-27

This passage comes in a section (Exodus 22:21-32:19) which has a profoundly covenantal feel: a sense of God directly addressing his people and expressing concern on matters about which he cares passionately.²⁷ It consists of laws that seek to regulate the treatment and protect the interests of disenfranchised and vulnerable groups within Israel. These groups include the widows, orphans, resident non-Israelites ('aliens') and the poor. Marshall defines the poor as 'people incapable of providing basic economic subsistence'.²⁸

Meyers explains the prohibition on charging interest in lending money thus:

The concern for the poor involves the stipulation that interest must not be charged on loans to destitute people. The harsh realities of socio-economic life in the highlands of Canaan meant the frequent need for farm families to borrow food or seed...Subsistence loans, as well as compassionate handling of essential items as pawn, were meant to help people cope with extreme poverty and *could not be the source of gain for the lenders*.²⁹

Fretheim sees care for the poor and respect for their property as a fundamentally theological matter. 'Israel must be concerned about these things because God the Creator has chosen to be concerned, not simply in giving the laws in the first place, but in attending to them in a personal way.'³⁰ These laws call into focus the nature of Israel's being the people of God: 'When the people of God mistreat the poor, they violate their own history....it is a disavowal of their own past, of those salvific acts which made them what they were'.³¹ Another commentator on Exodus, Durham, sees the prohibition of interest as expressing a familial relationship — the poor are to be treated as fellow-members of Yahweh's family.³² If collateral is held 'it must be returned before its absence causes hardship'.³³

Leviticus 25:35-38

This passage envisages a situation where a fellow countryman has fallen on hard times and become dependent on others. Again the call is to be supportive and compassionate, treating such people with the kindness that they would show to resident aliens. Solidarity is to be expressed by refraining from the charging of interest. Hartley comments: 'This prohibition is supported by the basic premise of biblical faith, the fear of God'.³⁴ Again the people are reminded of God's mercy ('I am the Lord your God, who brought you out of the land of Egypt') as a ground for showing mercy themselves.

²⁷ For example, the words (in God's voice) 'When he cries out to me, I will hear, for I am compassionate' (Ex.22:27). Fretheim, *Exodus*, p.246, suggests that 'The first person references to God move these laws to a different level of intensity...The "I" of God addresses the "you: of the people.'

²⁸ Marshall, *Israel*, p.148.

²⁹ Meyers, *Exodus*, p.200, emphasis added.

³⁰ Fretheim, *Exodus*, p.245.

³¹ *Op.cit.*, p.247.

³² Durham, *Exodus*, p.329.

³³ *Ibid.* He suggests that the collateral is 'more for the benefit of the feelings of the borrower than for the security of the lender', but this seems somewhat stretched.

³⁴ Hartley, *Leviticus*, p.440.

Deuteronomy 23:19-20

This passage explicitly forbids the charging of interest within the Israelite community while permitting interest on loans to foreigners. In the former case, the prohibition is spelt out as applying to ‘interest on money, interest on provisions, interest on anything that is lent’. It is not confined simply to poor Israelites. Obedience to this command is linked to God’s blessing: ‘so that the Lord your God may bless you in all your undertakings....’ The close-knit community ties that lie at the heart of the prohibition are highlighted by the permission to treat foreigners differently. This was not the stranger living in their midst (whom they were told to treat as one of their own), but the stranger who lived in a foreign nation, with whom there was no land-kinship network.³⁵ In that context, levying interest on loans represented a sensible minimisation of risk, and meant that Israel could take its place as an equal partner on the commercial playing ground of the ancient Middle East.³⁶

Another important passage in Deuteronomy which deals with treatment of the poor is 15:1-18. The primary aim of its stipulations is to alleviate suffering caused by debt and oppression among the Israelite community. Borrowing was and is integral to people needing support.³⁷ But the sabbatical principle is here applied to the matter of debt, commanding creditors to remit their claims every seven years — saying ‘no to the economic system that ties people inexorably in debt...and no to the relentless cycle of poverty that is accepted easily as a fact of life’.³⁸ The passage contains the stark statement ‘There should be no poor among you’ (v.4), contrasted with verse 11, ‘There will always be poor people among you’. This seeming contradiction sets the agenda: the reality of a fallen world is that poverty persists, but the ultimate intention of God is that it should be abolished — and the provisions of this passage are intended to help bring that about.

There are other Old Testament texts that mention interest more briefly, but always with a mark of disapproval. Wright observes that ‘In Israel, it was among the defining marks of righteousness that a person did *not* lend at interest; conversely the charging of interest was morally and socially condemned’.³⁹ In Psalm 15 the person who may dwell in God’s sanctuary is one, *inter alia*, ‘who lends his money without interest’ (v.5), and the righteous man of Ezekiel 18:8, 13 and 17 is similarly restrained.⁴⁰ Nehemiah becomes very angry when he learns of Israelites exacting interest from their fellow-countrymen and forcing them into financial slavery (Neh.5:1-12) — this

³⁵ Wright, *Deuteronomy*, p.188 makes this distinction: these foreigners ‘had no stake in the land and were probably traders’.

³⁶ It should be noted that the charging of interest was common in surrounding countries of the time. Von Rad, *Deuteronomy*, p.148 notes that interest rates were between 20 to 50% elsewhere; see also Wright, *Deuteronomy*, p.251; Goringe, ‘Usury’, p.861.

³⁷ A point well made by Mills in *Jubilee Manifesto*, p.201. He comments: ‘In relational terms, loans are often more fulfilling than gifts because the exchange is between relatively equal parties (in that the borrower is expected to repay), the lender places trust in the borrower’s willingness to repay and repayment takes place over time, increasing the number of interactions between the parties.’

³⁸ Miller, *Deuteronomy*, pp.138-9.

³⁹ Wright, *Deuteronomy*, p.251.

⁴⁰ In Ezekiel 18 levying interest is put on an immoral par with sins such as robbery and idolatry. See also Proverbs 28:8.

in a post-exilic urban context. The strength of feeling in these texts is not to be underestimated.

Biblical texts: the New Testament

In contrast to the Old Testament, the New Testament is lacking in texts that speak of interest in a clear, unambiguous way. Some comment is both appropriate and necessary, however.

First, it is noteworthy that when Jesus proclaimed God's willingness to forgive sins he used the analogy of debt.⁴¹ He recognised the oppression that being oppressed by a burden of debt entailed — and the freedom that could come from its cancellation. Second, he makes the Old Testament commands to lend without interest even more radical by urging his disciples to 'lend, without expecting anything in return' (Luke 6:34-35; cf Matt.5:42). It is not altogether clear whether 'anything' refers to 'any interest' or the repayment of the loan itself, but either way it implies a generous attitude unconcerned about financial return.

In contrast, it has been suggested that Jesus demonstrated acceptance of the levelling of interest when, in the Parable of the Talents, the unprofitable servant falls under the condemnation: 'you ought to have invested my money with the bankers, and on my own return I would have received what was my own with interest' (Matt.25:27; c.f. Luke 19:23). It is true that Jesus here accepts the earning of bank-related interest as a fact of life, but that may just be a detail of the story, Jesus being true to how things are; it does not necessarily mean that Jesus was commending such a system. Paul Mills and Michael Schluter have suggested that for the servant to invest his money in this way would be a case of him taking a leaf out of his master's book, a 'hard man' who reaped where he did not sow.⁴² It has to be said that the evidence of this parable in relation to Jesus' attitude to interest is inconclusive.

The same may be said about the story of the dishonest steward (Luke 16:1-8), which is generally considered the most difficult of all Jesus' parables to interpret. Some commentators, in an attempt to explain why Jesus should commend a man who appears to act dishonestly, have suggested that in letting debtors off part of their debt the steward was foregoing the interest which his master had unjustly charged them.⁴³ This is ingenious, but unproven; it begs the question of why the word 'dishonest' or 'unrighteous' is still used about the steward in verse 8. Clearly, however, Jesus does see something to commend about the man's *shrewdness* with regard to his use of money. This may provide a counterbalance to the seemingly carefree attitude to money in his teaching noted earlier.

In the book of Acts, the early church's *koinonia*-living, in which they had everything in common and there were no needy people among them⁴⁴ can be seen as a natural,

⁴¹ The German language preserves the link more closely because the same word *Schuld* means both 'debt' and 'guilt'.

⁴² Mills, *Jubilee Manifesto*, p.204. Among some Liberation theologians such as C.S.Song, author of *Third Eye Theology*, the third servant is even seen as a hero of the story because he refuses to go along with his master's dubious practices.

⁴³ See e.g. Derrett, *Law in the New Testament*, pp.56-63.

⁴⁴ Acts 2:44-45 & 4:32-37.

dynamic and radical corollary both to the teaching of Deuteronomy 15 and Jesus' example. It is difficult to imagine interest being levied on loans in such a community. This type of sharing was not abandoned as quickly as is sometimes assumed. Gonzalez notes how it continued well into the second and third centuries AD.⁴⁵

Church tradition: the Patristic period

The patristic period presents a consistent picture. Many of the Church Fathers condemn usury (the levelling of interest) as contravening Scripture and breaking the laws of charity. Gonzalez claims that with the possible exception of Clement (who is contradictory on the subject) usury was universally condemned in the early church.⁴⁶ It is important, though, to read that denunciation within the broader context of teaching on money, which encourages — indeed requires — the sharing of wealth.⁴⁷

Tertullian objects to usury not only because the Old Testament Law prohibits it, but also because oaths were sworn in the transactions establishing contracts.⁴⁸ Around the same time Cyprian of Carthage dedicated an entire thesis of his *Testimonia* to denouncing usury. His primary argument is that it is contrary to the love the Christian should show towards the poor, whilst a secondary argument is the apparent deceit of the lender, for with the appearance of giving he disguises his inner motive of impoverishing his neighbour.⁴⁹ In contrast, he argues that everything belongs to God and should be held in common. Therefore 'those who have must share with their neighbour'.⁵⁰

The Cappadocian Fathers brought different emphases.⁵¹ Basil of Caesarea organised relief for the poor⁵², Gregory of Nyssa related the subject to the doctrine of creation, while Gregory of Nazianzus emphasised human solidarity. These theologians were adamant in attacking usury as one of the main causes of poverty.

Basil speaks of usury as not just making the poor poorer, but depriving them of their freedom.⁵³ It is inhuman that on seeing someone in need the lender takes advantage by charging interest. 'On the other hand, to give to the poor, either as a loan without interest or as an outright gift, is to lend to God.'⁵⁴ Basil speaks of bread, cloaks, shoes and money stored or hoarded by the wealthy as belonging to the destitute as much as to the rich people listening to his sermon.⁵⁵

⁴⁵ Gonzalez, *Faith and Wealth*, p.205.

⁴⁶ *Op.cit.*, p.204.

⁴⁷ See e. g. the *Didache*, *The Shepherd of Hermas* and Clement of Alexandria's 'Who is the rich man that is saved?', found in Phan, *Message of the Fathers of the Church*, for this twofold perspective.

⁴⁸ Tertullian, *Adv. Marc.* IV, 17.

⁴⁹ Cyprian, *Test.* III, 48; *Strom* 2.18.

⁵⁰ Cyprian, quoted by Murphy, 'Social Thought', p.856.

⁵¹ Gonzalez, *Faith and Wealth*, pp.175-178.

⁵² See Cort, *Christian Socialism*, p.43.

⁵³ Basil, *Hom. II in ps.* 14; *Ep.* 18.

⁵⁴ González, *Faith and Wealth*, p. 177. Proverbs 19:17 says, 'He who is kind to the poor lends to the Lord, and he will reward him for what he has done.'

⁵⁵ 'Are not you covetous, are not you a defrauder, when you keep for private use what you were given for distribution? When someone strips a man of his clothes we call him a thief. And one who might clothe the naked and does not – should not he be given the same name?' – Basil, quoted by Cort, *Christian Socialism*, 43.

Gregory of Nyssa states that usury is a sin unknown to nature because it draws gain from inanimate things — in nature it is only living things that provide fruit. (This is an idea similar to that found in Aristotle — that money is intrinsically sterile.) Usury adds to the numbers of poor.⁵⁶ The usurer is graphically and uncompromisingly likened to a thief.⁵⁷ González summarises Gregory’s sermon illustration:

The poor man waits at the lender’s doorstep precisely because he is poor and hopes that the other’s wealth will help him. The lender, to whom the poor comes as a friend, is in truth an enemy. He finds his supposed friend wounded and wounds him even more, loaded with anxiety and adds one more anxiety to his burden.⁵⁸

For Gregory, usury is not the ultimate source of poverty: that consists in the unwillingness of the rich to share with those in need.⁵⁹

The same uncompromising stance on usury is seen in the fourth and fifth centuries. For example, Ambrose’s work *De Tobia* appears to condemn usury absolutely;⁶⁰ though he concedes that it might be used against enemies!⁶¹ The same is found in works by John Chrysostom.⁶² ‘Do not say, “I am using what belongs to me.” You are using what belongs to others. All the wealth of the world belongs to you and to the others in common, as the sun, air, earth, and all the rest.’⁶³ Greeley argues that Chrysostom’s conclusions derive from his understanding of the church as the body of Christ.⁶⁴ ‘In the church as in a body there is a solidarity among members. We should help the poor because they are our co-members in the body of Christ.’⁶⁵ There is identification between Christ and the poor; the ground for generosity is Christ himself. This reference to the church, at first sight, appears limiting. However, Chrysostom extends his application to include anyone suffering from poverty and oppression — even ‘an unbeliever’.⁶⁶ This important broadening of application to include unbelievers is of course significant. It broadens the base from redemption in Christ to creation in Adam.

We are all formed with the same eyes, the same body, the same soul, the same structure in all respects, all things from the earth, all men from one man, and all in the same habitation.⁶⁷

⁵⁶ Gregory, *Hom. IV in Eccl.*

⁵⁷ Gregory, *Contra usuarios.*

⁵⁸ González, *Faith*, 176.

⁵⁹ González, *Faith*, 178. González concludes his brief helpful study on the Cappadocian Fathers with the following summary: ‘All that is not necessary is superfluous and therefore must not be retained as long as others lack the necessities of life. To do otherwise, to claim that one has exclusive right to something that another needs, is tantamount to theft and even homicide’ (p. 178).

⁶⁰ Ambrose, *De Tob.* 42. See also his *De bono mortis* 12, 56.

⁶¹ Ambrose’s perspective is seen in the quotation, ‘You are not making a gift to the poor. You are handing them what is theirs’ – quoted by Murphy, ‘Social Thought’, p.856.

⁶² Chrysostom, *Hom. 41 in Gen; Hom. XIII in 1 Cor; Hom. X in 1 Thess; Hom. 57 on Matthew.*

⁶³ Chrysostom, quoted by Cort, *Christian Socialism*, 45.

⁶⁴ See Greeley, ‘St John Chrysostom’, pp. 1163–1168.

⁶⁵ *Op.cit.*, p.1163.

⁶⁶ Quoted from *In Heb. Hom.* 10.4, by Greeley, ‘St John Chrysostom’, p. 1164.

⁶⁷ Quoted from *In 1 Tim. Hom.* 12.3 by Greeley, ‘St John Chrysostom’, 1164. Chrysostom’s application is clear: ‘The possessions of the Lord are all common. Is not this an evil then that you

An important part of Chrysostom's intention was to dislodge wealthy Christians 'from the conviction that an uncrossable social gulf separated them from the poor'.⁶⁸ Ultimately, his message was one of humble mutuality.⁶⁹

The great councils of the church responded to the subject in a similar way. The Council of Nicea (325) ordered usurious clergy to be deposed, the Council of Carthage (345) condemned its practice by laity, the third Lateran Council (1179) denied usurers the sacrament or Christian burial and the second Council of Lyons (1274) forbade the letting of property to foreign usurers. Usury was again prohibited by the Council of Vienna (1311).⁷⁰

Church tradition: the Medieval period

For the most part, theologians and churchmen of the medieval period retained the earlier condemnation of usury. Peter Abelard's comment is pertinent: 'How very many indeed do we daily see dying, groaning deeply, reproaching themselves greatly for usuries, plunderings, oppressions of the poor...and consulting a priest to free them from these faults.'⁷¹ In expounding the seventh commandment Peter Lombard claims that 'Here also usury is prohibited, which is contained under robbery.'⁷² Among the Scholastic theologians of the early middle ages the equation between usury and robbery was very common. They anticipated the counter-argument that the borrower had agreed to the transaction by saying that he did so with a forced or compelled will rather than an absolute and voluntary will.⁷³

Thomas Aquinas' teaching on usury was influential, as on much else. Aquinas followed Aristotle in the belief that money was essentially barren, so it was 'unnatural' to make money out of money.⁷⁴ Money is made for exchange, and to lend it on interest is to sell what does not exist.⁷⁵ He regards this as a matter of justice: 'Making a charge for lending money is unjust in itself, for one party sells the other something non-existent, and this...sets up an inequality which is contrary to justice.'⁷⁶ Interestingly, as with others before him, Aquinas broadens the Old Testament stipulations to include even the foreigner who was excepted:

alone should have the Lord's property, that you alone should enjoy what is common? Is not the earth God's, and the fullness thereof? If then our possessions belong to one common Lord, they belong also to our fellow-servants' – from *In I Tim. Hom.* 12.4, quoted by Greeley, 'St John Chrysostom', 1166.

⁶⁸ Leyerle, 'John Chrysostom on Almsgiving', p.29. See, generally, pp.29–47. Leyerle speaks of the destitute as 'something of an anti-spectacle' (32, 38).

⁶⁹ See also, Jerome, *Comm. In Ez.* 18, 6; and Augustine, *Enarr. In ps 36, serm.* 3, 6; *Serm.* 38; 86; *De bapt.* 4, 9. Augustine regarded usury as a crime.

⁷⁰ See Goyder, *Just Enterprise*, pp.99–102.

⁷¹ Abelard, *Ethics*, p.79.

⁷² Lombard, *Sentences* III.37.5: II, 211.

⁷³ See Langholm, *The Legacy of Scholasticism*, pp.60–62. He cites William of Auxerre and Thomas of Chobham in this respect.

⁷⁴ See Aristotle, *Politics*, 1.3, 1.10; *Nicomachean Ethics*, V.10.

⁷⁵ Aquinas discusses the 'sin of usury' at some length in his *Summae Theologiae*, 2.2, Qu.78. Lack of space necessitates only a brief examination.

⁷⁶ *Op.cit.*, Qu.78, Art.1 (235). He also claims that the balance of justice is restored if a man receives back what he has lent 239).

The Jews were forbidden to lend upon interest *to their brothers*, that is to say, to their fellow Jews. What we are meant to understand by this is that lending upon interest to any man is wrong in itself, in so far as we ought to treat every man as a brother and neighbour, especially in the epoch of the Gospel.⁷⁷

To a Christian, everyone should be treated as a brother.

Having asserted the sinfulness of slavery, Aquinas is forced to recognise that civil law allows the practice, though it does so, he claims, ‘to accommodate imperfect men who would be severely disadvantaged if all sins were strictly prohibited by suitable sanctions’.⁷⁸ Later he states that ‘Somebody who borrows money subject to the payment of interest does not approve the sin of usury but uses it’ — he is using the sinner ‘for good’.⁷⁹ This is a more pragmatic approach.

Aquinas has much to say about the relational aspects of lending and borrowing. People are not bound to make loans.⁸⁰ However, a person who pays interest on a loan ‘cannot be said to be acting quite voluntarily, but under some pressure’. Therefore, a ‘debt of gratitude is set up’ — the borrower is under ‘a moral obligation’.⁸¹ Interestingly, Aquinas goes on to say that this means the lender is entitled to some sort of compensation and, if he does not charge interest, that compensation should be benevolence towards the lender.⁸²

This switch of perspective is significant, because it actually raises the possibility that, just as a loan with interest can entail a lender taking advantage of a borrower, a loan without interest can also entail a borrower taking advantage of a lender. If the lender stands to lose by the loan, is it necessarily unjust that he receive financial compensation? From the early thirteenth century, there were scholastic theologians who argued that a creditor could sometimes claim compensation for loss suffered because of failure on the borrower’s part to repay the loan on time. Langholm, probably the leading expert on medieval scholastic thought, points out:

From such loss because of delay, the basis of the claim for compensation was extended to a creditor’s loss on account of the loan within the loan period itself, and the concept of a loss was extended from a loss actually sustained (*damnum emergens*) to a loss in the relative sense of a missed profit opportunity (*lucrum cessans*).⁸³

Where these two exceptions were allowed, a major fissure in the church’s traditional teaching opened up. By the sixteenth century such exceptions had become commonplace in the thinking of influential Spanish thinkers such as Luis de Molina and, following him, Juan de Lugo. They represent a decisive break with the Aristotelian tradition.⁸⁴

⁷⁷ *Op.cit.*, Qu.78, Art.1 (237), original emphasis.

⁷⁸ *Op.cit.*, Qu.78, Art.1 (237).

⁷⁹ *Op.cit.*, Qu.78, Art.4 (253).

⁸⁰ *Op.cit.*, Qu.78, Art.1 (239).

⁸¹ *Op.cit.*, Qu.78, Art 1 & Art 2 (241)

⁸² *Op.cit.*, Qu.78, Art.2 (243)

⁸³ Langholm, *The Legacy of Scholasticism*, p.75.

⁸⁴ *Op.cit.*, pp.74-76.

Church tradition: the Reformation and beyond

In the meantime, the world was changing fast, socially, economically and politically. Developing economies and the growth of a new merchant middle class soon made it difficult to carry on transactions without taking interest.⁸⁵ The two great Reformers held rather different views on the subject of usury.⁸⁶

Martin Luther stands solidly in the classical, biblical and scholastic tradition. He uses a variety of arguments against the practice in his famous treatise *On Trade and Usury*.⁸⁷ He states that it is ‘simply a commandment that we are bound to obey’,⁸⁸ and sees the widespread practice of usury as part of the perilous end-time in which he believed he was living. Luther puts the prohibition squarely in the context of an alternative — generous and open-handed giving or lending.⁸⁹ Failure to help the needy in this way is a sign of unbelief.⁹⁰ Indeed, usurers who charge a high rate (by which he means 7 to 10!%) ‘often die an unnatural death or come to some terrible end...for God is a judge for the poor and needy’.⁹¹ The lengthy treatise concludes with an appeal to those in authority to ‘help and rescue (people) from the gaping jaws of usury’.⁹² In some respects Luther is more severe than traditional Christian teaching. Apparently, ‘he would deny to usurers the sacrament, absolution, and Christian burial’.⁹³ However, according to Jones, Luther agreed that widows, orphans, students, ministers and others in need could lend at interest to support themselves.⁹⁴ His main target in attacking usury was the merchant-class whom he saw as consumed by greed.

John Calvin lived in the merchant city of Geneva and had a less jaundiced view of their practices. He was more open to the practice of usury though he expresses his acceptance in very guarded terms. In a letter to Claude de Sachin, Calvin cautiously offers advice on the subject.⁹⁵ He argues that there is no scriptural passage which ‘totally bans all usury’.⁹⁶ His comment on the Old Testament critique of usury is that:

Usury almost always travels with two inseparable companions: tyrannical cruelty and the art of deception. This is why the Holy Spirit elsewhere advises

⁸⁵ Gorringer, ‘Usury’, p.161, cites the example of Franciscan poor-relief projects that found it necessary to charge a small amount of interest to cover expenses.

⁸⁶ There is a vast amount of literature on the Reformers’ attitude to usury, indicative of the fact this is a watershed period. Note books or articles by Elder, Goddard, Jones, Kerridge, Mott, Olaf, Schulze, Valeri and Wykes in the bibliography.

⁸⁷ Luther, ‘On Trade and Usury’, *Luther’s Works (LW)* 45 pp.233-310. With typically colourful language Luther says that usury ‘lays burdens upon all lands, cites, lords and people, sucks them dry and brings them to ruin’ (p.297).

⁸⁸ LW 45 pp.277, 281, 290, 308.

⁸⁹ *Op.cit.*, pp.280-281, 291-295.

⁹⁰ *Op.cit.*, p.294.

⁹¹ *Op.cit.*, pp.305-306.

⁹² *Op.cit.*, p.310.

⁹³ White, *The Changing Continuity*, p.173.

⁹⁴ Jones, ‘Usury’, p.204. See also Stackhouse, ‘Protestantism and Poverty’, pp.6-10.

⁹⁵ Calvin, Letter to Claude de Sachin in *Calvin’s Ecclesiastical Advice*, pp.139-143.

⁹⁶ Goddard *Semper Reformanda*, p.249 suggest that if Calvin had believed Scripture did ban all usury then the debate for him ‘would effectively be closed’.

all good men, who praise and fear God, to abstain from usury, as much that it is rare to find a good man who also practises usury.⁹⁷

However, although Calvin admits that the world would be a better place without usury he advises its use 'for the common good'. He saw the Israelite ban on usury as of temporary rather than permanent significance, an aspect of their constitution that was appropriate to their time and place. Sixteenth century Geneva was different: it was a political union whereas Old Testament Israel was a fraternal one.⁹⁸ He concludes that 'we ought not to judge usury according to a few passages of scripture, but in accordance with the principle of equity'.⁹⁹ He therefore thought it permissible 'to make concessions to the common utility'.¹⁰⁰ He considered loans at modest rates between parties who had good business reasons to lend and borrow were acceptable.¹⁰¹

Calvin is very clear that *no one should take interest from the poor*.¹⁰² He was genuinely concerned that no one should be forced into poverty, and aware of the dangers posed by usury in this respect. The lender must not be preoccupied by personal gain; otherwise he forgets the bonds of relationship and ties of community. In a seminal study, Olson cautions that Calvin and other Protestant reformers were characterised 'more by a struggle against poverty than by a justification of lending money at interest or of keeping one's profits to oneself'.¹⁰³

It is notable that Calvin did not use the Aristotle-Aquinas argument about the barrenness of money. During the sixteenth century there was an increasing abandonment of this argument and a growing acceptance that money, too was a commodity. So money had its price, and interest named the price it carried for the privilege of borrowing it over a period of time. As commerce developed, so did the need for long-term investment: the outlay of costs might be considerable before any profits could be anticipated. Entrepreneurs needed loans to get started, and the bankers who enabled them to do so could justifiably expect some return for their services. The charging of interest is also related to an economic environment where inflation is a fact of life. If lenders' money will be worth less when they get it back, it seems fair for them to charge interest, and if there is a significant risk of their losing it, that appears fair grounds for an additional charge.

It is this changed view of money that makes the sixteenth century a crucial watershed in the Church's tradition on usury, dividing the period before from the period after it. It is not the case that in accepting modest rates of interest theologians since the

⁹⁷ Calvin, Letter, p.140. Goddard, *Semper Reformanda* p.259 quotes Calvin from elsewhere, saying: 'It is scarcely possible to find in the world a usurer who is not at the same time an extortioner, and addicted to unlawful and dishonourable gain.'

⁹⁸ Bieler, *La Pensée Economique*, p.455, asserts that Calvin was more aware of economic realities than many of his predecessors.

⁹⁹ Calvin, Letter, p.141.

¹⁰⁰ *Op.cit.*, p.142.

¹⁰¹ Similarly, in his commentary on the usury text in Deuteronomy 23, he argues that interest is justified in cases of prolonged failure to pay a debt, or a loan taken by an already monied person in order to buy land. See Calvin, *Commentaries IV*, pp.125-133.

¹⁰² Calvin, Letter, p.142.

¹⁰³ Olson, *Calvin and Social Welfare*, p.167, and his article *idem*, 'Calvin and social-ethical issues', pp.153-172. See also Stackhouse, 'Protestantism and Poverty', pp.1-35, and the related study by Haas, *Concept of Equity in Calvin's Ethics*.

Reformation have rejected all the principles of the preceding tradition. Calvin and others correctly discerned that the main principle behind the Old Testament prohibitions was protection of the poor, a zealous concern that the latter should not be exploited in their vulnerable condition. But they no longer felt that this necessitated a blanket ban on all interest. Effectively they were exhorting people to live by the spirit of the law rather than the letter of it.

The challenge posed by such an approach is that it is more difficult to live by: people are less clear what they should and should not do. What is considered a 'reasonable rate of interest' is a very subjective opinion. Rather than decoding each case by a consideration of the interests and intentions of the parties concerned (which is what a moral theologian might do), it was easier for Governments to set a figure. An English Act of Parliament of 1571 accepted charges of interest of up to 10%. In the decades that followed the practice of usury lost much of the moral stigma that had previously attached to it. Jones comments that whereas in the medieval world usury was seen as the epitome of greed and oppression, by the seventeenth century 'the matter had become relegated to the status of a theological scruple in a world that accepted lending at interest as an economic necessity'.¹⁰⁴ That is the world in which we are operating today. Since 1600, debate about interest has mainly concerned the matters of whether a maximum rate of interest should be set by law and if so what that rate should be.

Contemporary application of the Christian tradition

In this paper we adopt a post-Reformation understanding of interest, viz. that the charging of interest *can* represent a fair commercial arrangement, from which lender and borrower may mutually benefit. But we are well aware that some — arguably, *much* - charging of interest is exploitative, i.e. it takes selfish advantage of the desperate condition in which individuals, families and even certain countries find themselves. If it is the first sort of interest, we do not believe the practice falls under the biblical and traditional prohibition. If it is the second sort of interest, we believe it is as reprehensible now as it has ever been.

It is with these considerations in mind that we return to the subject of the sub-prime financial sector. How is this to be assessed from a Christian ethical perspective, with an eye to suitable investment?

Home credit

There are some positive comments which can be made about the home credit industry. It is providing for a need that is clearly evident: poor people need to borrow money and often cannot access credit in any other way. As we showed above, there are several features of the industry which suit customers well: simple access, cash loans, weekly repayments, personal visits and flexible arrangements. On the surface, this looks like an industry well attuned to their customers' needs, and this is how the major home credit companies present themselves. Provident Financial makes much of the fact that 'There is an up-front, fixed charge with no default or penalty charges

¹⁰⁴ Jones, 'Usury', p.204.

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whatsoever — even if a customer misses a repayment or takes longer to repay their loan.¹⁰⁵

However, it is difficult to avoid the conclusion that customers are paying a high price for this friendly, flexible service in terms of the interest rates charged. Companies appear to make ample allowance for the absence of penalty charges in calculating the cost of capital. The Competition Commission report includes a table providing details of ‘Large lenders: principal products, 2004’.¹⁰⁶ This lists 19 types of cash loan from the six largest lenders. The APR% ranges enormously, from 56.7% to 497%. Within this huge range, one of the loans made by Provident Financial, PPC, may be regarded as fairly typical. This attracts an APR of 177%.

The Commission was prepared to accept the view taken by the home credit companies, that APR alone is an inadequate measure of the price of a home credit loan (because extra credit charges are often missing from the APRs quoted by mainstream credit providers) and that TCC — the Total Cost of Credit — is a more appropriate basis of comparison. This indicates how much more than the amount borrowed is to be paid back by the lender. The PPC loan of £3 a week over 55 weeks attracts a TCC of £65. A Cattles loan of £5.30 a week over 30 weeks attracts a TCC of £60.¹⁰⁷

As the Commission report observes, these figures are high — we would add, very high — compared with most other forms of credit. The APR on most credit cards ranges from around 15 to 30%. The home credit industry is charging rates to the poorest members of society which far exceed rates charged by mainstream credit providers to wealthier members of society. As will be evident from the figures quoted above, these rates are generally at least twice as high but can, in some cases, be as much as ten times as high.

The industry defends its practice by claiming that home collection means the companies incur high fixed costs, and that home credit customers have a high risk of default.¹⁰⁸ These factors certainly need to be taken into account. However, the latter factor serves to counteract the former to some extent: the personal nature of the home loan collection appears to be effective in reducing the risk of default. Neither the National Consumer Council nor the Competition Commission reports believed these factors justified the substantial price gap between home credit and mainstream credit.

As we have shown, concern that the poor should not be exploited lies at the heart of the Old Testament prohibition of usury. Calvin’s cautious acceptance of interest excluded the exaction of interest from the poor. Now it may well be argued that, in our contemporary climate, it is unrealistic to expect commercial enterprises to offer credit to the poorest sections of society without charging any interest; there is no way that companies could cover costs and make a profit if they did that. But the logic of the Christian tradition and the theology which underlies it is that the terms on which credit is offered to the poor should be more generous than the terms on which it is offered to the rest of society. This is demonstrably not the case. In the sub-prime

¹⁰⁵ www.providentfinancial.com/plc, ‘Home credit’

¹⁰⁶ *Home Credit Market Inquiry*, 3.9.

¹⁰⁷ *Op.cit.*

¹⁰⁸ *Home Credit*, pp.64-65.

sector, the most impoverished and disadvantaged members of society are being made to pay a higher price than those who are better able to afford the cost of credit.

For these reasons, it would seem inappropriate for Christian churches to invest in the leading home credit companies. The provisional findings of the Competition Commission are that the price of capital they charge is unreasonably high, and our own investigations support this conclusion. The company that church investors might be most interested in is Provident Financial, because it is the largest and most profitable. Provident Financial is not, of its type, a ‘bad’ company. Interestingly, it is represented on the main global sustainability indices and for four consecutive years has been included in the FTSE4Good Index. It has an impressive Corporate Responsibility policy.¹⁰⁹ But we feel that churches have to take seriously the judgment of the Commission that ‘Provident has, in the period from 1999 to 2004, been earning returns substantially and persistently in excess of the cost of capital’.¹¹⁰ Indeed, the dominant position it occupies in the industry appears to have contributed to a situation where customers pay higher prices than could be expected in a more competitive market. In the light of these concerns, we do not feel that it is an appropriate target for investment.

A similar concern might also be expressed about investment in HSBC, because of its involvement in the sub-prime sector in the USA. However, such a judgment is complicated by two factors. First, it has proved beyond the scope of this report to research the home credit industry in the USA. Second, the sub-prime sectors forms only a small part of HSBC’s overall portfolio of financial services. It may therefore be considered harsh to exclude a bank from investment on the grounds of some negative ethical criteria, when it might score positively on other grounds.¹¹¹

The recommendation that the home credit industry be excluded from church investment choices is made with some reluctance, because — as has been said — the poor do need credit, and it is good for Christians to be actively involved in giving them financial support. The most useful form of support, however, is that which has the potential for lifting them out of the state of poverty. This is the virtue of micro-credit, which provides loans for impoverished people to start small businesses. The Grameen Bank, founded by Nobel Peace Prize winner Muhammad Yunus, has won international renown for its work in this area.¹¹² Such organisations charge interest but not at excessive rates, and they are explicitly dedicated to helping poor people make a success of their business rather than looking for opportunities to exploit their vulnerability. We suggest that church investors may wish to consider the possibility of investing in micro-credit organisations, while recognising that these may not offer as a high a rate of return as investors are looking for.

The home credit industry, in contrast, does little or nothing to help poor people out of poverty. It may help them to survive, financially speaking, and this itself is an achievement. But one of the Competition Commission’s most disturbing findings was

¹⁰⁹ www.providentfinancial.com/plc, ‘Corporate responsibility’.

¹¹⁰ *Home Credit Market Inquiry*, 7.

¹¹¹ Similarly, many retailers are considered fair choices for investment even though a small proportion of their profits come from selling tobacco.

¹¹² See Yunus, *Banker to the Poor*, and for a Christian organisation which specialises in the provision of micro-credit, Opportunity International’s website www.opportunity.org.

that home credit customers are effectively penalised for settling loans early.¹¹³ Such a policy does not suggest that the home credit companies are seriously interested in helping their customers improve their position. Whereas a good customer for a micro-credit organisation is one who takes advantage of a loan and improves their financial position so that eventually they do not need further loans, a good customer for a home credit company is one who keeps coming back for further loans. From a Christian perspective, the distinction is important.

Sub-prime secured lending

While many of the same ethical issues considered under the category of home credit also apply to sub-prime secured lending, it is important also to attend to relevant differences in how traditions of usury apply to this part of the sub-prime market. In particular, it is important recognize that in contrast to the home credit industry, very few would characterize the whole of the sub-prime secured lending sector as working to the disadvantage of the poor. Where interest rates, fees, and loan terms are not disproportionate, and products are marketed appropriately with a view to what will be advantageous for the consumer given their income and situation, access to sub-prime secured lending can be a significant benefit to borrowers. Therefore, exposure to sub-prime secured lending should not in itself be a bar to investment in a company.

Alongside the statement that sub-prime secured lending is not always ethically problematic, however, we must also recognize that the overwhelming majority of predatory lending takes place in the sub-prime sector, so that to be ethically permissible any investment in this sector must be able to gain sufficient information about lending practices in order to exclude the possibility that the sub-prime lending has been predatory. Predatory lending, was defined above as ‘cases in which a broker or originating lender takes unfair advantage of a borrower, often through deception, fraud, or manipulation, to make a loan that contains terms that are disadvantageous to the borrower’, and practices associated with it included: excessive fees, excessive interest rates, single-premium credit insurance, lending without regard to ability to pay, loan flipping, fraud and deception, repayment penalties and balloon payments.¹¹⁴ From the survey of the tradition on usury it should already be clear that predatory lending fits very well within the rationale for the prohibition of usury: exploitation of the poor. It is a key component of honouring the Jewish and Christian legacy of the concern about usury, therefore, that investment gains are never made on the basis of predatory lending.

Clearly, therefore, where companies or their subsidiaries, or holdings in mortgage-based securities, are associated with predatory lending practices, this must disbar them from inclusion in an ethical investment portfolio. It may be argued that holdings in companies where exposure is very low could be acceptable, but given the stringent and central preoccupation with usury in the tradition, it is doubtful that any kind of association with what is clearly usurious lending could be legitimate.

¹¹³ See *Home Credit Market Inquiry*, 3.21: ‘Where a loan is settled early, in practice the borrower still pays most of the charges originally payable on the loan...So a borrower with a good payment record who settles a loan early will be likely to pay an effective interest rate higher than the quoted APR.’

¹¹⁴ United States General Accounting Office, *Consumer Protection*, 18–9.

Where, on the other hand, companies with exposure to sub-prime secured lending can be shown to be operating effective policies that avoid predatory lending practices, where rates and fees are proportionate, terms are fair, the vulnerable are not unjustly targeted, and sales techniques are not pressured, there can be no objection to investing in them. Indeed, where sub-prime lending is done on such terms, it can be legitimately construed as a positive benefit for those unable to obtain credit elsewhere.

Having established these two clear reference points, it is necessary to consider the territory that lies between them. In many cases where it is known that a company or mortgage-based security has exposure to the sub-prime secured lending market, it may be very difficult to ascertain the terms under which loans were made. Where companies have policies in place to prevent association with predatory lending, it may be hard to judge whether the policies are effective, how diligent staff are in operating them, and how they are monitored. Judgements in this area will require the same careful consideration as necessitated in relation to other potentially problematic investment areas. It should be clear, however, that given the moral seriousness with which usury is treated in the Jewish and Christian traditions, investors have a responsibility to take every effort to assure themselves that the objects of their investment are not involved in usurious and predatory lending.

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