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High-Class Pawnshops Fill a Lending Void

Some Can Charge Interest Rates Exceeding 200%; No Credit Check and Little Paperwork

By Ianthe Jeanne Dugan
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Appraisals manager Karina Lagravinese inspects a ring to obtain its value inside the Manhattan offices of Borro, a collateral lender. Philip Montgomery for The Wall Street Journal

When Heather Robinson needed money to start a sports-apparel line, she turned to an unusual lender, offering a prized possession as collateral: a bronze nude torso sculpture.

Ms. Robinson, who directs a Washington nonprofit, brought the 16-inch statue last month to a New York firm called Borro Inc., which immediately wired her $15,000. The interest rate: 3.99% a month, or as much as 23.9% for the six-month loan term.

Borro and other collateral lenders—essentially high-end pawnshops—are a small but fast-expanding part of the shadow-lending system. Since 2008, as commercial banks have cut lending to small businesses, such alternative lenders have helped fill the void.

In some states, collateral lenders can charge interest rates exceeding 200% annually because the business isn't bound by traditional banking laws. On the upside for borrowers, there isn't a credit check and little paperwork.

So some entrepreneurs are hauling treasured possessions—Baccarat chandeliers, Picassos, Maseratis, even Houdini's handcuffs—to Borro and others to bankroll businesses historically financed by conventional loans, credit cards or not at all.

In Ms. Robinson's case, Borro was familiar with her Elizabeth Catlett sculpture: She had pledged it before to fund charitable events.

Borro is the largest of this new breed of collateral lenders, having lent nearly $100 million since opening in England in 2009.

Competitors such as iPawn Inc. and Pawngo collectively have lent tens of millions of dollars.

"If it continues being this hard for consumers and businesses to access credit, we think this can be a multibillion-dollar industry," says Paul Lee, a partner at Lightbank, a venture-capital firm that has invested $3 million in Denver-based Pawngo.

In 2012, after raising $26 million, Borro opened an office in Manhattan, with sweeping views and walls temporarily adorned with borrowed Andy Warhols.

In a year, Borro Chief Executive Officer Paul Aitken says, business has more than doubled. Half the customers are small businesses, with loans averaging $10,000 to $15,000 and up to $1 million.

"Banks are loaning to firms with 50 to 500 employees," Mr. Aitken says. "Who is looking after those with one to 50?"

These lenders are far different from traditional storefront pawnshops, which typically lend $100 to $150, according to their industry association, to people hawking gold and other goods to fill their gasoline tanks or pay rent.

In contrast, these new high-end pawnshops typically operate with an online presence and a corporate office, where borrowers mail their objects or stop in by appointment with big items such as classic cars.

But they share an important link: laws that let them generally charge far more than traditional banks, varying from state to state.

Borro Vice President Mark Bench inspects the sculpture 'Nude Torso' by artist Elizabeth Catlett. Philip Montgomery for The Wall Street Journal

In New York, collateral lenders can charge as much as 4% a month, for a total of 48% a year. Texas allows collateral lenders to charge 240% annually. By comparison, Texas has an 18% annual cap on commercial loans below $250,000.

When Benny De-Kalo, a former Lehman Brothers banker, opened iPawn in Texas last year, he wooed customers with lower rates.

"I thought if I could open an Internet pawnshop and charge 2% or 3% per month, that would be great," he says. Already, he has lent $6 million.

The average interest rate paid by small-business borrowers on a conventional bank loan nationally was 5.8% in September, according to the National Federation of Independent Businesses.

But traditional loans are elusive for some startups. Suzanne Johnson says she and her husband and two daughters were daunted by banks' requirements when they were opening "pop up" stores to sell Halloween costumes in Colorado.

Instead, Ms. Johnson sent a ruby and diamond necklace and matching ring to Pawngo, along with a sapphire bracelet, a yellow diamond ring and other items, ultimately borrowing $80,000.

Pawngo charges an average 7% a month, says Jim McHose, an accountant who formed the firm in 2011.

"Yes, that's a very high cost," Mr. McHose says. "But these loans are taken for specific projects, and the borrowers often still earn money."

Most customers repay within three to six months.

Pawngo has lent about $10 million, typically in chunks of $1,000 to $5,000.

"Big banks are doing big deals like Twitter, not the local dentist," Mr. McHose says.

Some old-line pawnshops are expanding to capitalize on the trend. Beverly Loan Co., a 75-year-old Beverly Hills, Calif., pawn operation, earlier this year opened an enterprise in Manhattan called New York Loan Co.

"Small businesses needed loans more than ever before," says Chief Executive Jordan Tabach-Bank. "Our bread and butter is the $20,000 loan to small-business owners who have to meet payroll or inventory demand."

Paul Phillips, a New Jersey general contractor, says he had a "dark day" in July when a shopping-center developer delayed payments.

He brought his Patek Philippe watch to New York Loan and got $20,000 to keep the job going.

Three weeks later, he says, he retrieved the watch and paid back the $20,000—plus $1,600 in interest and fees.

"It was expensive," Mr. Phillips says. "But I otherwise would have had to tell my subcontractors that I can't fund the job. Everything hinged on it."

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