The Center for

Community Capitalism

A Policy & Business Case for Increasing Access to Financial Services in the U.S.

Prepared for presentation at World Bank Conference
Broadening Access to Financial Services
Cartagena, Colombia
April, 28-29, 2004

by
Dr. Michael A. Stegman
Center for Community Capitalism
University of North Carolina at Chapel Hill

Why policymakers care whether people are banked

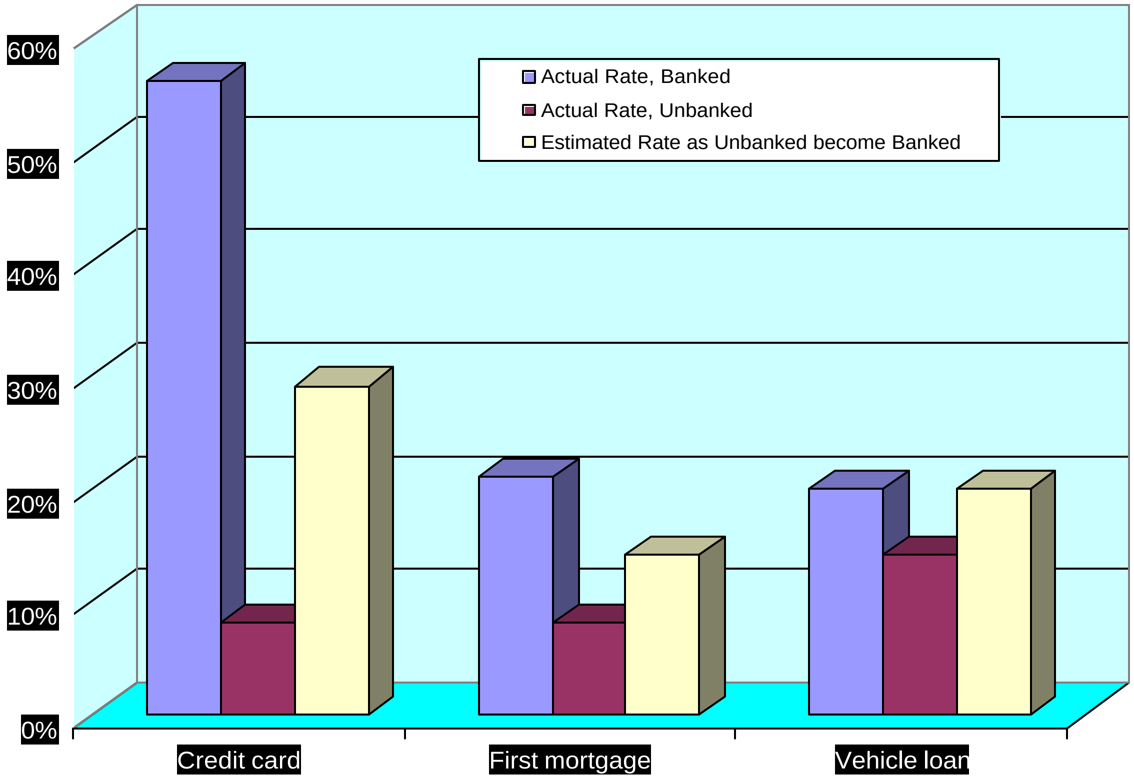
- U.S. policy moving toward asset-based social policies—rewarding work, incentives for taking more responsibility for financial future & retirement security;
  - People with bank accounts are more than twice as likely to hold savings, as are people who are unbanked, and are more likely to add to their savings on at least a monthly basis.
  - Wealth disparities are greater than income disparities & growing;
    - The bottom 90 percent of Americans earn 60 percent of all income,
    - but own less than 30 percent of all net worth
    - and less than 20 percent of total financial assets.

Why banks should care about increasing financial access

- Strong link between account ownership and use of bank credit
  - Lower-income families with checking, savings, or money market accounts are six times as likely as to have credit cards and are more than twice as likely to have a mortgage.
- Demographics shape the future market
  - Nearly 60 percent of all first-time buyers between now and 2010 will be young minority & immigrant families.
- In practical terms, big part of this growing market is not part of the financial mainstream
  - more than 40 percent of unbanked low- and moderate-income African American and Hispanic renters are unbanked.

.

Cross-Selling Potential as the Unbanked Become Banked



Enormous growth in minority & immigrant purchasing power, 1990-2000

Category	1990 Buying Power (billions)	2001 Buying Power	Percent Change	Market Share 1990	Market Share 2001
Minority Total	$439.9	$860.6	95.6%	10.6%	12.2%
Black	**$307.8**	**$572.1**	**85.9**	**7.4**	**8.1**
Amer. In.	$ 19.2	$ 34.8	81.0	0.5	0.5
Asian	**$112.9**	**$253.8**	**124.8**	**2.7**	**3.6**
Latino	**$207.5**	**$452**	**118.0**	**5.0**	**6.4**
White	$3,715	$6,219.8	67.4	89.4	87.8
Total all races	$4,154.9	$7,080.4	70.4%	100.0%	100.0%

A business case for investing in America's inner cities

	America's Inner Cities	Mexico
Households	7.7 million	24.6 million
Average disposable household income	$23,888	$11,024
Total household income	$184 billion	$272 billion
Consumer Spending power per sq. mile	**$43,000,000**	**$224,433**
Proximity to large markets & clusters	High	Low
Average education level	Medium	Low
Currency stability	High	Low
Government stability	High	Low
Stable, known legal system	High	Low
American business norms and language	High	Low

Remittance business is driving product development & acquisitions to expand access to Latin American markets

- For most of the 1990s, remittances exceeded offical development assistance;
- Global remittance market is $95 billion a year;
- Mexican immigrants send $2 billion a month home to their families through remittance services;
- Competition among U.S. banks, and technology driving down prices;
- Bank of America’s SafeSend is a card that uses a telephone Internet and the ATM network, rather than expensive wire services to transfer money.

Technology is a driving force in banking revolution

• full service branch transaction	$1.07
• telephone transaction	$0.54
• ATM transaction	$0.27
• on-line transaction	$0 1.5

The rise of fee-based banking has potential to convert unbanked into profitable customers

- No longer do banks make most of their money from the interest spread.
- Non-interest revenues, particularly fee income, is driving bank income.
  - Bank fees in U.S. now account for about 44% of net operating revenues for commercial banks;
    - ATM surcharges generate $2 billion in revenues
    - In 2000, 400-million bounced checks generated $40 billion in fees.
    - Banks starting to charge for over-the-counter (teller) transactions;
- A global phenomenon – India, Hong Kong, New Zealand, Canada, Thailand.

Same technology driving banking is driving changes in government benefits

- Between 1999 & 2002 public policy began pushing direct deposit of social security, and ATM access for cash assistance and food benefits
- Can't have direct deposit without a bank account
- Replacing paper checks with electronic delivery put U.S. Treasury Department in the business of designing bank accounts for the unbanked
  - On May 2, 2002,Treasury awarded 15 grants totaling $8+ million to financial institutions to assist 35,500 unbanked low- and moderate-income individuals open accounts.

Electronic delivery of government benefits has hidden policy potential

"[direct deposit] could soon result in millions of Americans being brought into the banking system for the first time, and it will change dramatically the way in which they handle money."

Treasury Secretary, Robert E. Rubin

www.ccc.unc.edu

75 years of U.S. banking legislation: 1. the Great Depression

- 1930s – federal deposit insurance (the FDIC) -- $2,500 per account, periodically raised to $100,000 in 1980;
- Congress erects barriers between commercial banking, investment banking, insurance & brokerage services;
- Federal support of residential mortgage market
  - 1/6 of all U.S. home mortgages refinanced;
  - introduction of federal home mortgage insurance;
  - creation of federally supported secondary mortgage market (Fannie Mae);

2. combating redlining & racial discrimination

www.ccc.unc.edu

The 1960s & 1970s

- President Kennedy's Executive Order on equal opportunity
- The 1964 Civil Rights Act
- Home Mortgage Disclosure Act (HMDA)
  - Requires financial institutions to publicly report on loan applications, denials, and approvals, by race & neighborhood location;

3. The Carrot & Sticks of the Community Reinvestment Act (CRA)

- Passed in 1977, the purpose of the CRA is to fight redlining and increase flow of credit to low income neighborhoods.
- CRA enforced by examining CRA record of banks, issuing written report with rating, & taking account of bank's CRA record when considering application to expand business.
- Together, HMDA & CRA have created a citizen's army of local enforcers
- NGO's analyze bank behavior and file grievances

Federal Reserve study suggests CRA does not force banks to make bad loans

- "…lenders active in lower-income neighborhoods and with lower-income borrowers appear to be as profitable as other home purchase lenders."

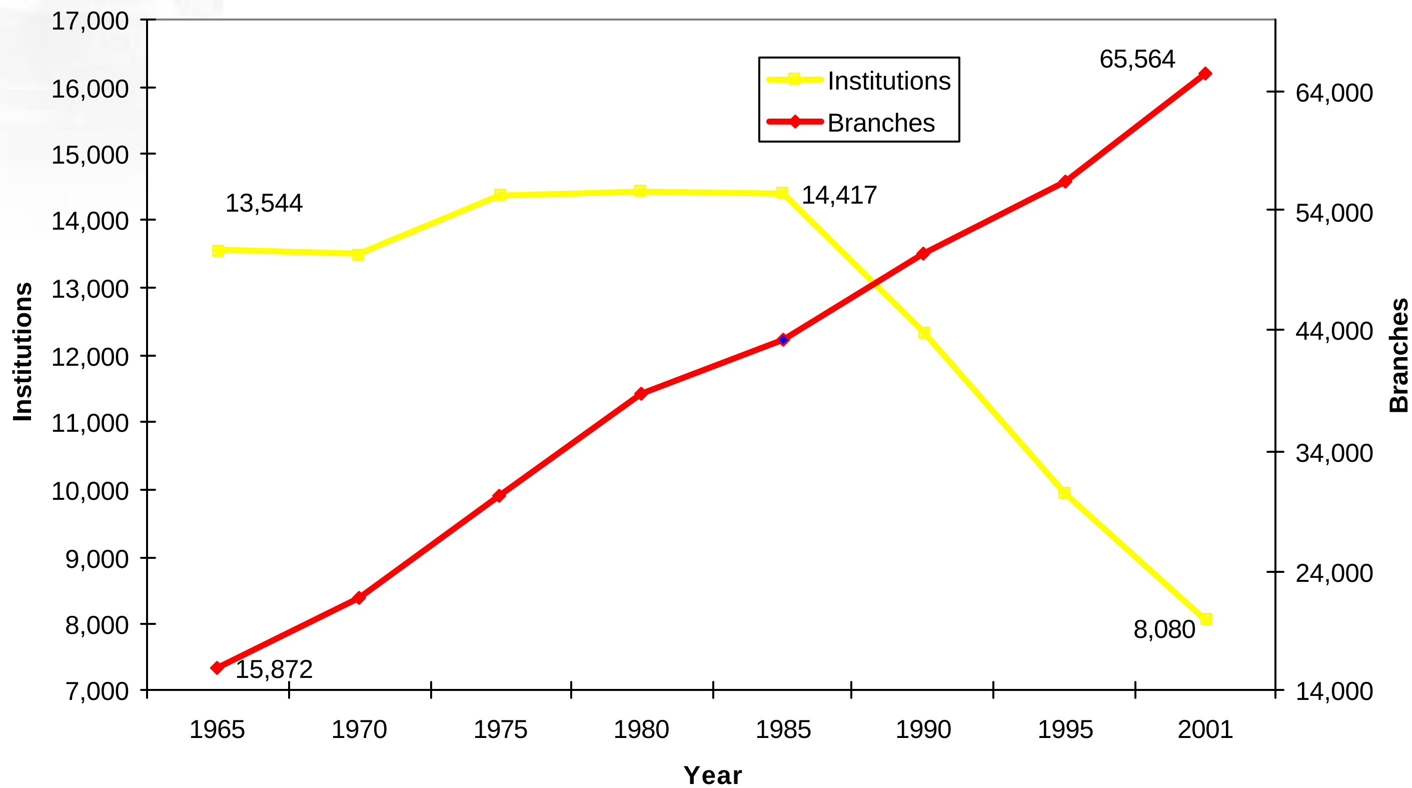
- "…We find no compelling evidence of lower income profitability at commercial banks that specialize in home purchase lending in lower income neighborhoods or to lower-income borrowers."

Glenn Canner and Wayne Passmore, The Community Reinvestment Act and the Profitability of Mortgage-Oriented Banks, March 3, 1997

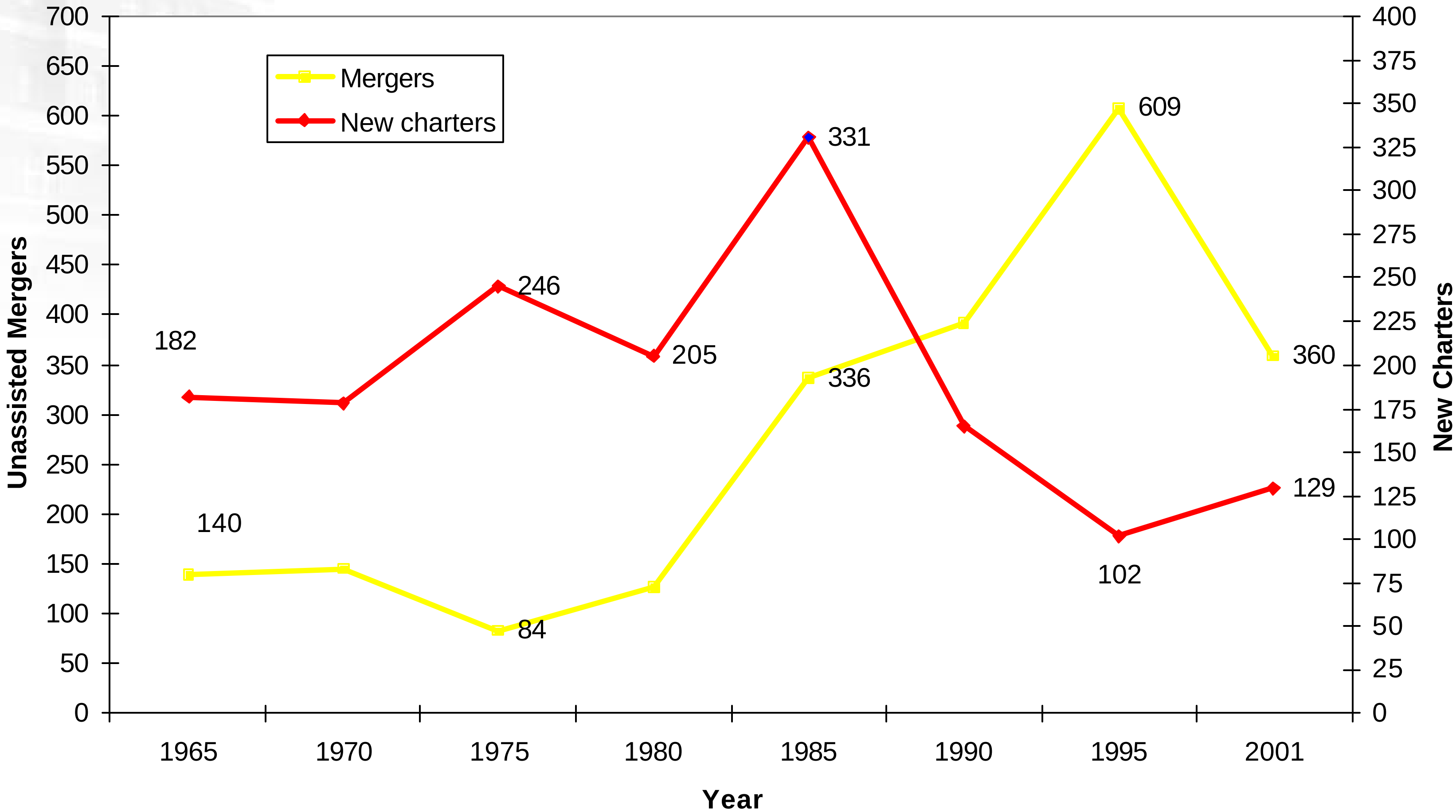
Community development finance comes of age in the 1990s

- When enacted in 1977, CRA covered 70% of all U.S. savings; today it is only about 30%;
- Congress funds a network of specialized community development financial institutions (CDFIs) that specialize in increasing access to financial services and capital
    - community development banks (32 depositories with $4+ billion in deposits in 2001);
    - community development credit unions (130+)
    - community development loan funds
    - microcredit programs
    - community development venture funds (equity)
- Recent sampling of CDFI performance found that 81 CDFIs managing $1.8 billion in assets provided more than $2.9 billion in financing, with 1.8% cumulative loss rate.

Enormous consolidation in the number of banks, but not in banking offices U.S., 1965-2001



Amidst consolidation, new banks are still being chartered

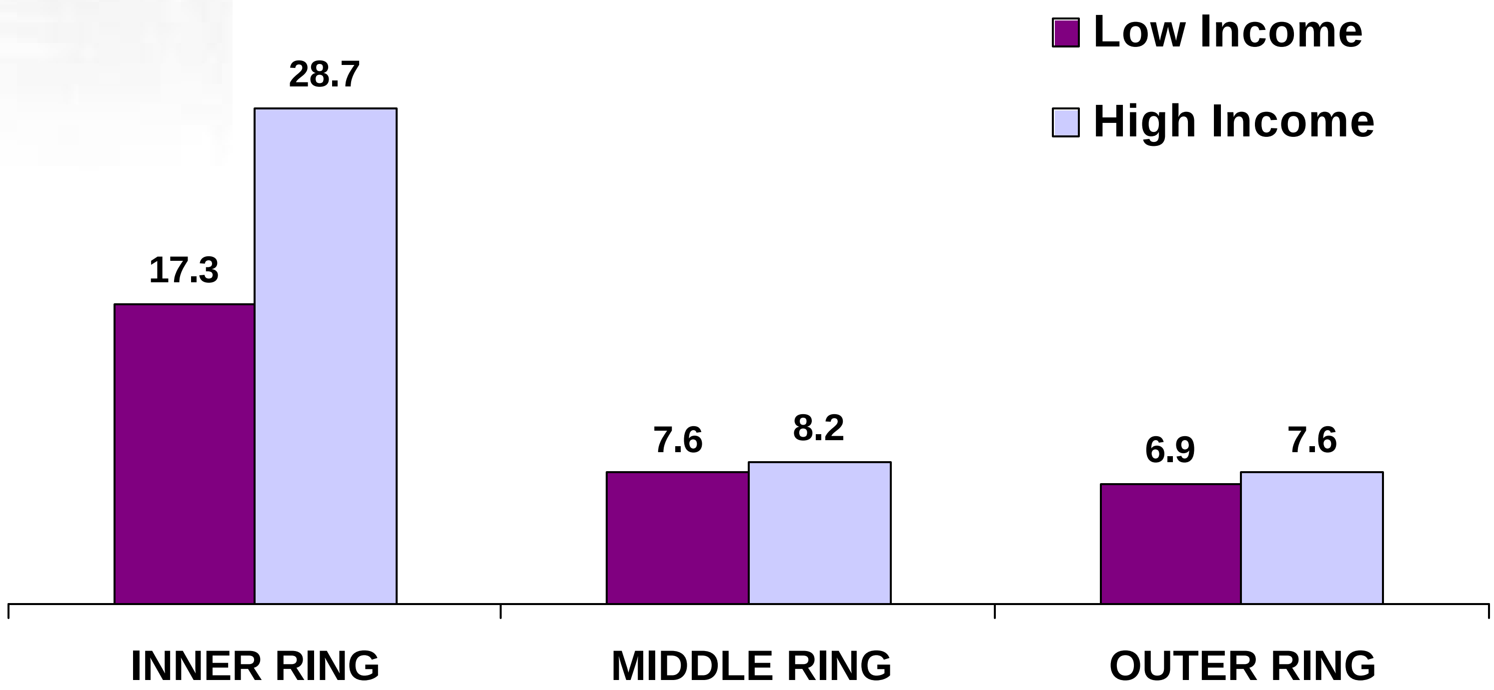


New branches growing, but not in low income communities

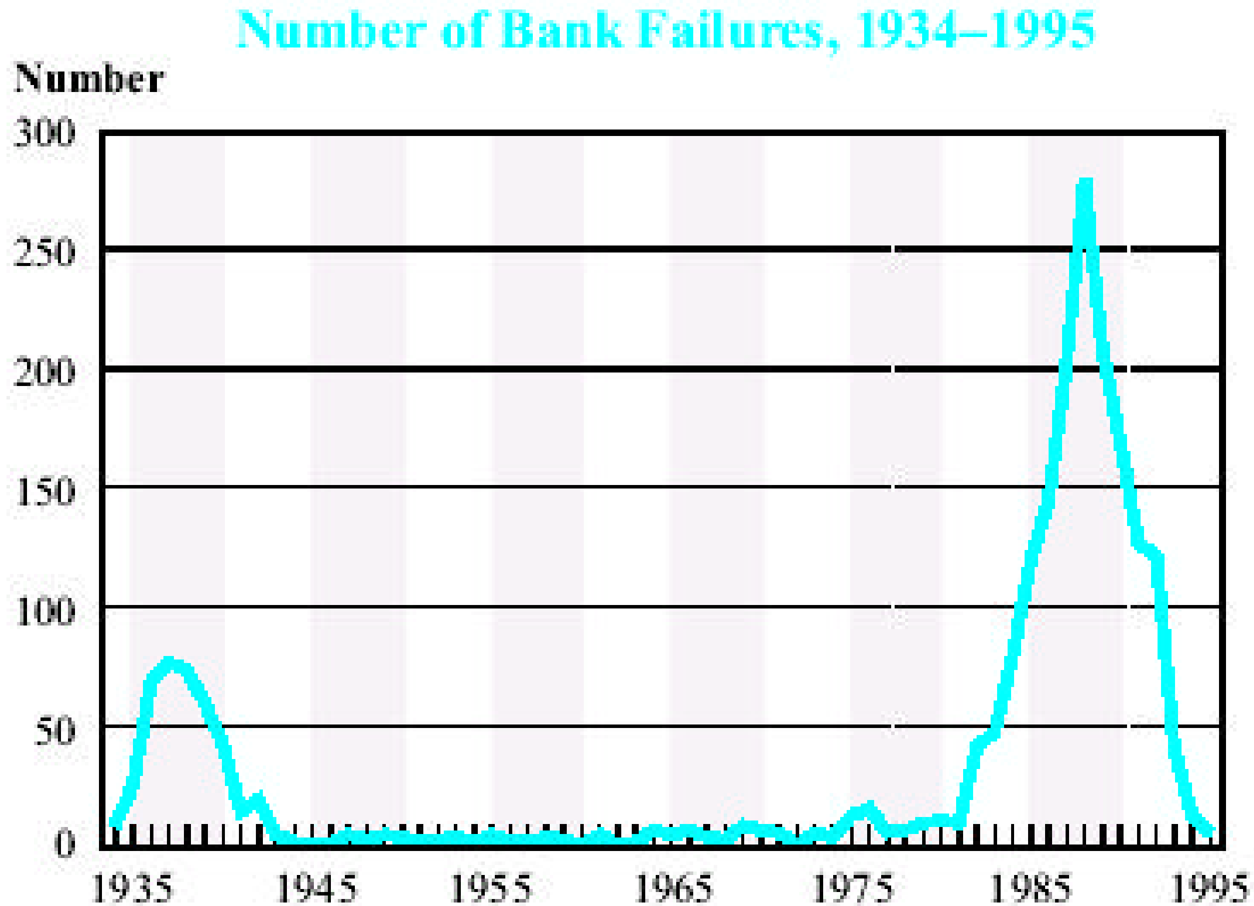
- Despite 45% reduction in number of U.S. banks & thrifts over last 15 years, U.S. banks per capita is still 5 times greater than in U.K.;
- While number of banking offices continues to grow-- by 29% over past 15 years—branches in low-income neighborhoods are down 21%;
- Consolidation & branch closings are a global phenomenon:
  - U.K. 4,500+ branches closed in last 10 years, and continuing– the rise of "bank deserts," communities with no financial institutions
  - Australia losing branches, especially in rural areas
- 20% of Wal-Mart's customers are unbanked – Can superstores turn into superbanks?

ATMs are very important delivery channel in America's 100 Largest Central Cities

(ATM addresses per 10,000 people)



Two Eras of Bank Failures in U.S.



Note: Data refer to FDIC-insured commercial and savings banks that were closed or received FDIC assistance.

Recent bank failures more localized than during Great Depression

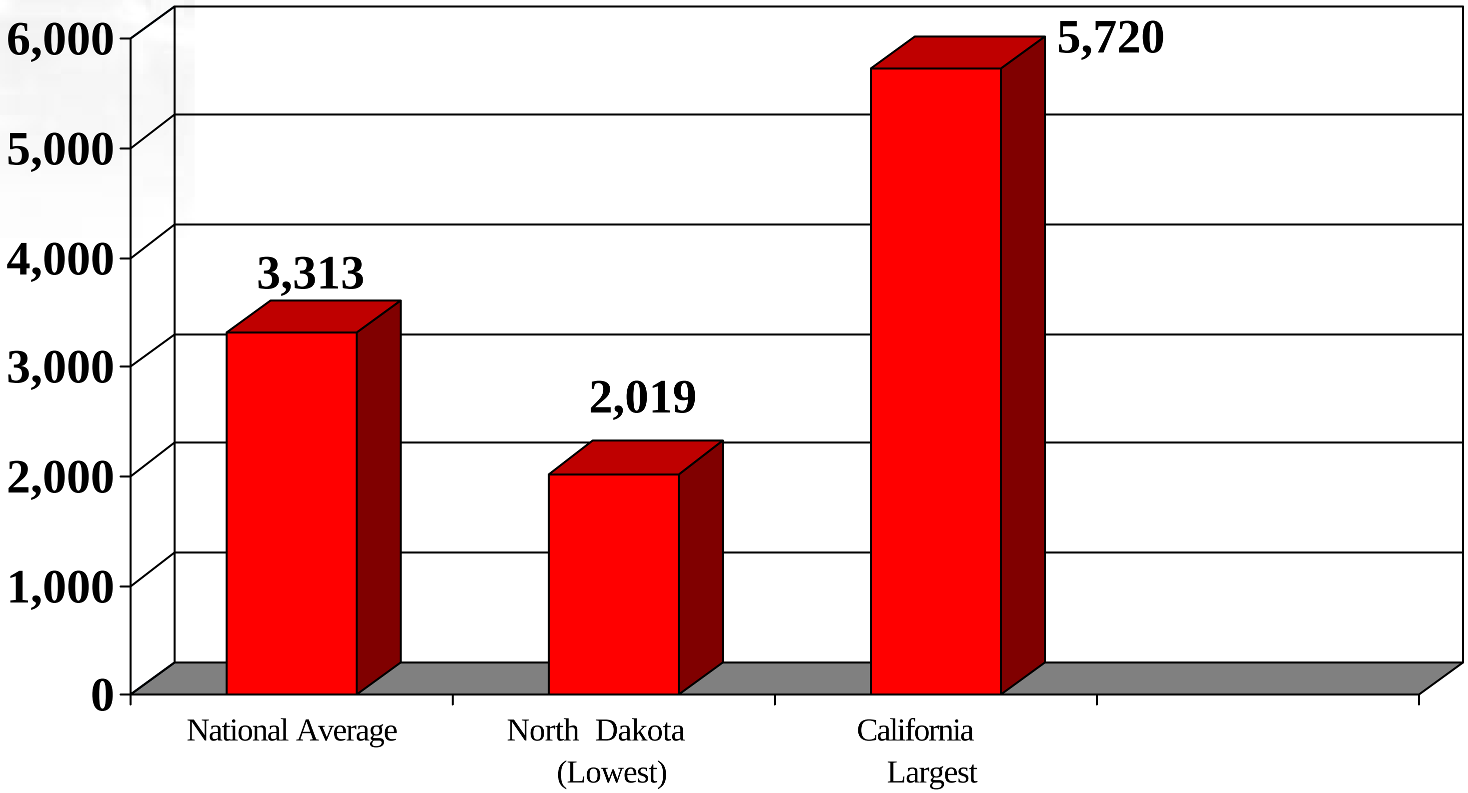
Bank Failures by State, 1980–1994

	Number of Bank Failures	Percent of Total Number of Banks	Assets of Failed Banks ($Thousands)	Percent of Total Bank Assets
Rhode Island	2	8.33	323,861	3.29
South Carolina	1	0.87	64,629	0.67
South Dakota	8	4.73	711,345	4.04
Tennessee	36	9.05	1,730,076	6.34
Texas	599	29.41	60,192,424	43.84
Utah	11	11.58	339,237	4.04
Vermont	2	5.41	93,802	2.94
Virginia	7	2.45	133,529	0.47
Washington	4	2.63	713,803	2.42
West Virginia	5	1.98	123,829	1.25
Wisconsin	2	0.30	50,882	0.19
Wyoming	20	16.67	375,332	10.30
U.S.	**1,617**	**9.14%**	**$206,178,657**	**8.98%**

Note: Data refer to FDIC-insured commercial and savings banks that were closed or received FDIC assistance. Total number of banks is the number of banks on December 31, 1979, plus banks newly chartered in 1980–94. Asset data are assets of banks existing on December 31, 1979, plus assets of newly chartered banks as of date of failure, merger, or December 31, 1994, whichever is applicable, and first available assets for Massachusetts banks that became FDIC-insured in the mid-1980s. Data exclude 13 newly chartered banks that reported no asset figures and 4 banks in U.S. territories.

But U.S. still "overbanked"

Persons per bank branch in U.S., 2003



www.ccc.unc.edu

For more information on today's presentation

- Center for Community Capitalism web site – www.ccc.unc.edu.
- Call at 919-962-6849