Financial Inclusion and The State of The Minority Banking Sector

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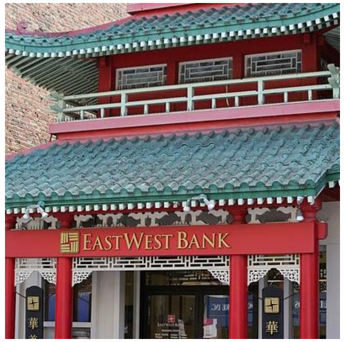
21ST CENTURY CITIES INITIATIVE



National Bankers Association Foundation

Minority Depository Institutions:

State of Knowledge, Sector Summary, Lending Activity, and Impact, 2010 – 2022

August 2023

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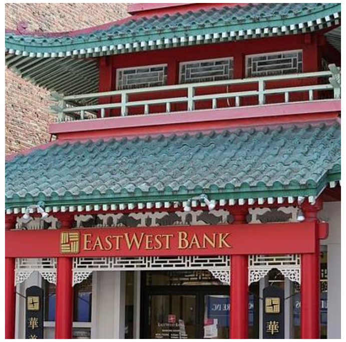

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What is an MDI?

Any Federally insured depository institution where **51 percent or more** of the voting stock is owned by minority individuals. "Minority" as defined by Section 308 of FIRREA means any "**Black American, Asian American, Hispanic American, or Native American**." The voting stock must be held by U.S. citizens or permanent legal U.S. residents to be counted in determining minority ownership.

Why did we look at MDIs?

A growing body of research establishes that MDIs originate a greater share of loans across all loan types to minority borrowers and are located in places with higher poverty rates and non-white populations than places served by non-MDI financial institutions including non-MDI community banks. Yet research on MDIs remains relatively sparse.

Motivating questions

1. What is the current state of knowledge on MDIs?
2. How has the sector changed since 2010?
3. What is their geography, demographic served, lending activity, and possible impact?

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Literature

- There is broad consensus in the literature that MDIs serve communities that have much higher shares of minority and low- and moderate-income (LMI) populations (Barth et al 2018, Barth & Xu 2020, Friesenhahn & Kwan 2021, FDIC 2019, Babajanova 2022, Breitenstein 2014, Toussaint-Comeau & Newberger 2017, Neal & Walsh 2020, Kashian et al 2016, Kashian et al 2014, Howell et al 2020)
- In response to the COVID-19 pandemic, MDIs disbursed more Paycheck Protection Program (PPP) loans than their peers and more credit to minority borrowers, responding to the greater need in those communities (Howell et al 2020, Friesenhahn & Kwant 2021)
- Berger et al (2022) find that if the banking industry performed similarly to MDIs, almost 2 million minority jobs would have been maintained and an additional $50 billion per year would have been available for small businesses during the Recession
- Long history in the academic literature of papers finding that MDIs are less efficient than their peers (Brimmer 1971, Boorman & Kwast 1974, Elyasiani & Mehdian 1992), and while some recent research confirms these findings (Young 2019, Breitenstein 2014, Kashian et al 2017, Toussaint-Comeau & Newberger 2017)
- **However**, Fairchild et al (2020), Barth & Xu (2020), and Barth et al (2023) compare MDIs to non-MDIs that serve similar communities using propensity score matching and how MDIs compare to comparable institutions instead of all commercial banks, finding that MDIs are not on average less efficient

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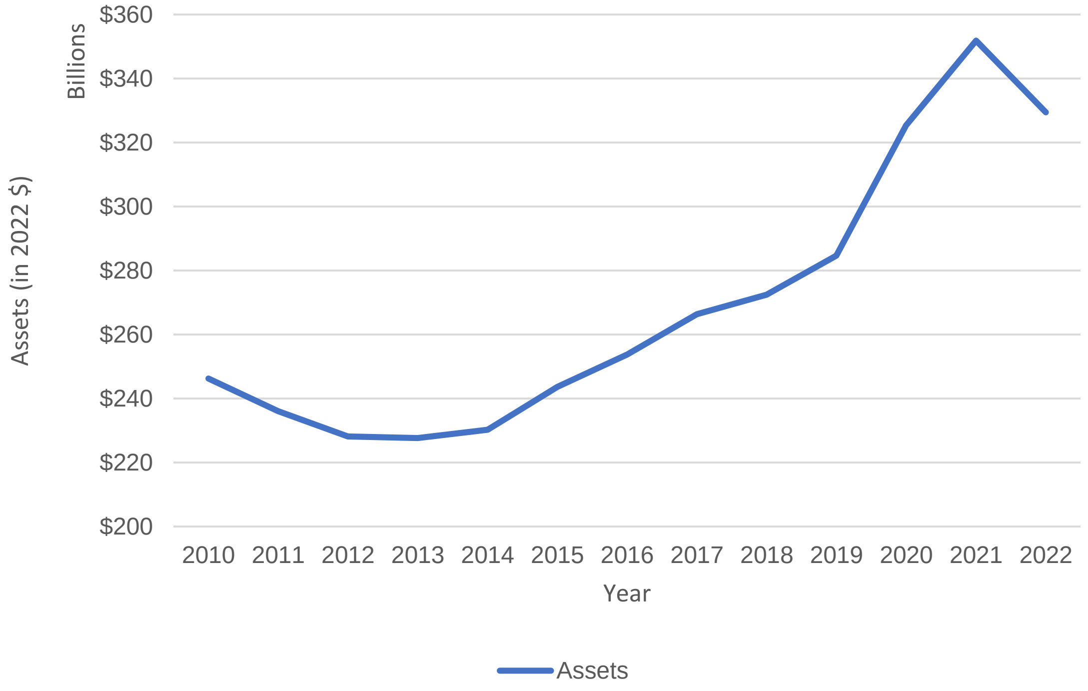
State of the Sector

- 147 MDIs (4thQ 2022), down from 197 in 2010 (lower than 32% decline for all FDIC banks)
- 1,523 MDI branches, down from 1,957 in 2010 (similar to all FDIC banks)
- Assets grew by 34% from $246 billion in 2010 to $329 billion in 2022 (similar to all FDIC banks)
- Deposits grew by 110% from $134 billion in 2010 to $282 billion in 2022 (less that 132% growth for all FDIC banks)
- MDI Ownership: 50% Asian or Pacific Islander American, 20% Hispanic American, 14% Black or African American, 14% Native American or Alaskan Native American, and 2% multiracial
- MDIs tend to be much smaller as measured by assets and deposits



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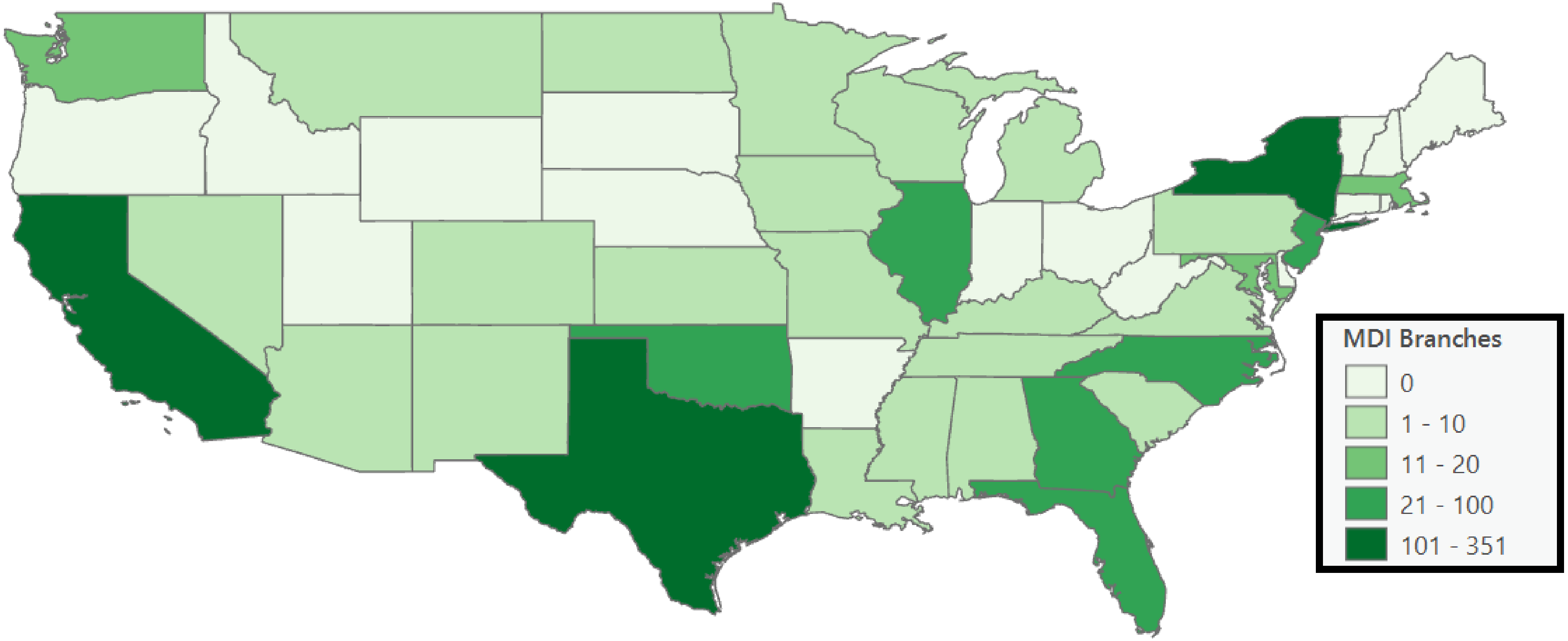
Geography Served

- Branches in 32 states and territories, in 92 cities, and in 732 zip codes
- High concentration in a handful of states and metro areas and in urban areas, generally
- Large cities without a single MDI branch: St. Louis, Pittsburgh, Phoenix, Cincinnati, Cleveland, Indianapolis, and Columbus.



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Geography Served: Competition

- MDIs were the only bank branch that existed in 174 zip codes, providing banking services to over 3.5 million
- In 25% of MDI service areas, they were the ONLY bank branch present

Image: Yelp, Bank of Cherokee County Hulbert branch in Hulbert, Oklahoma. January 29, 2019

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Demographics of Service Areas - Branches

Owner/ operator status	Branches	White	Black	Asian	Hispanic	Unemployed	Median income	Poverty rate
Non-MDIs	77,263	79%	4%	2%	7%	5%	$35,207	10%
All MDIs	1,457	51%	4%	5%	34%	6%	$32,285	17%
AMDI	664	37%	3%	36%	18%	5%	$38,567	11%
BMDI	85	29%	56%	3%	6%	8%	$30,857	23%
HMDI	610	61%	3%	0%	95%	8%	$26,669	26%
MMDI	2	69%	3%	19%	11%	5%	$84,635	9%
NMDI	96	69%	3%	1%	7%	6%	$26,753	18%

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Economic and Social Cohesion

	MDI	Non-MDI	Non-MDI Community Bank
Economic connectedness	0.701	0.601	0.562
Neighborhood economic connectedness	0.454	0.400	0.386
Friend clustering	0.081	0.084	0.117
Support	0.787	0.867	0.989
Volunteering rate	0.044	0.039	0.038
Civic orgs	0.011	0.011	0.014

Source: Opportunity Insights https://opportunityinsights.org/data/ Note: See here for definitions of economic and social connectedness.

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Climate Risk

Average share of properties at risk by bank branch type present

Risk category	Level of risk	Non-MDI	MDI	Non-MDI community bank	AMDI	BMDI	HMDI	MMDI	NMDI
Flood	Low	85%	81%	86%	84%	80%	77%	94%	89%
	Medium	7%	10%	6%	10%	7%	13%	3%	5%
	High	8%	8%	8%	6%	14%	10%	3%	6%
Fire	Low	93%	91%	93%	98%	100%	84%	100%	66%
	Medium	6%	7%	5%	2%	0%	13%	0%	27%
	High	2%	2%	2%	0%	0%	3%	0%	6%
Heat	Low	32%	11%	40%	15%	8%	1%	3%	16%
	Medium	41%	43%	41%	58%	44%	11%	72%	61%
	High	27%	46%	19%	27%	47%	88%	25%	23%
Wind	Low	59%	42%	67%	60%	19%	5%	50%	79%
	Medium	27%	33%	23%	32%	61%	33%	50%	13%
	High	14%	24%	10%	7%	20%	61%	0%	8%

Source: First Street Foundation

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Closing Thoughts

- Causes and consequences of MDI sector expansion and consolidation?
- Welfare and social and economic mobility implications of access to credit for minorities and underserved communities?
- Geographic granularity – Metro areas vs counties vs zip codes vs census tracts
- Need for data on race of borrower

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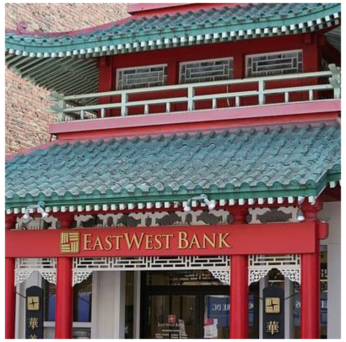
Anthony Barr, National Bankers Association Foundation



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Analysis of 2021 MDI Lending

As part of our MDI report, we looked at 2021 loan originations for a sample of MDIs, most of whom were National Bankers Association members. We used Census Bureau's ACS data to explore the characteristics of the zip-codes that received lending. Our sample included 10 banks, or roughly 7% of the MDI sector – holding 16.5billion in assets, roughly 5% of the sector's total assets.

Our sample includes one Asian bank, six Black banks, two Hispanic banks, and one Native bank.

Billions of Dollars Deployed in 2021

In 2021, our sample banks issued a total of 57,316 loans for a total of $3.4 billion in loan originations, with an average loan size of $59,000. Notably, the largest bank in our sample is well in excess of $1 billion in assets under management, and consequently deployed a sizable share of the total number of loans and loan dollars. When excluding that bank, the sample issued 19,921 loans for a total of $1.7 billion with an average loan size of $85,431.

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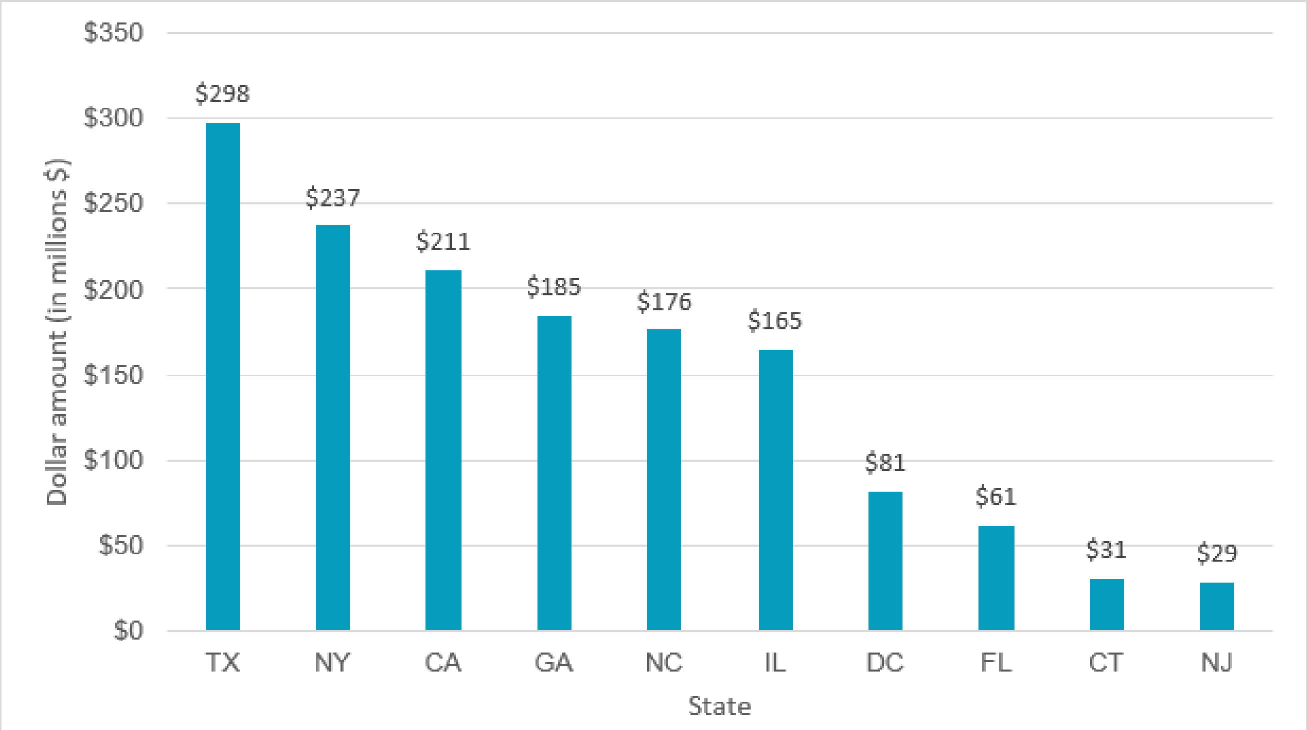
Geography Served

- Our sample banks are headquartered across six states and represent all four regions of the United States with six banks in the South, one bank each in the Northeast, Midwest, and West, and one bank in Puerto Rico. Loan dollars were spread across all four regions, with significant amounts of loan dollars flowing to states in all four regions.
- Our sample banks deployed loans in 6,052 unique zip codes, which includes lending in 3,659 distinct cities. A total of 172 million people lived in the zip codes that received lending dollars in our sample, reflecting over half (51%) of the total current U.S population.

Figure 3 – Top 10 states by total loan amount



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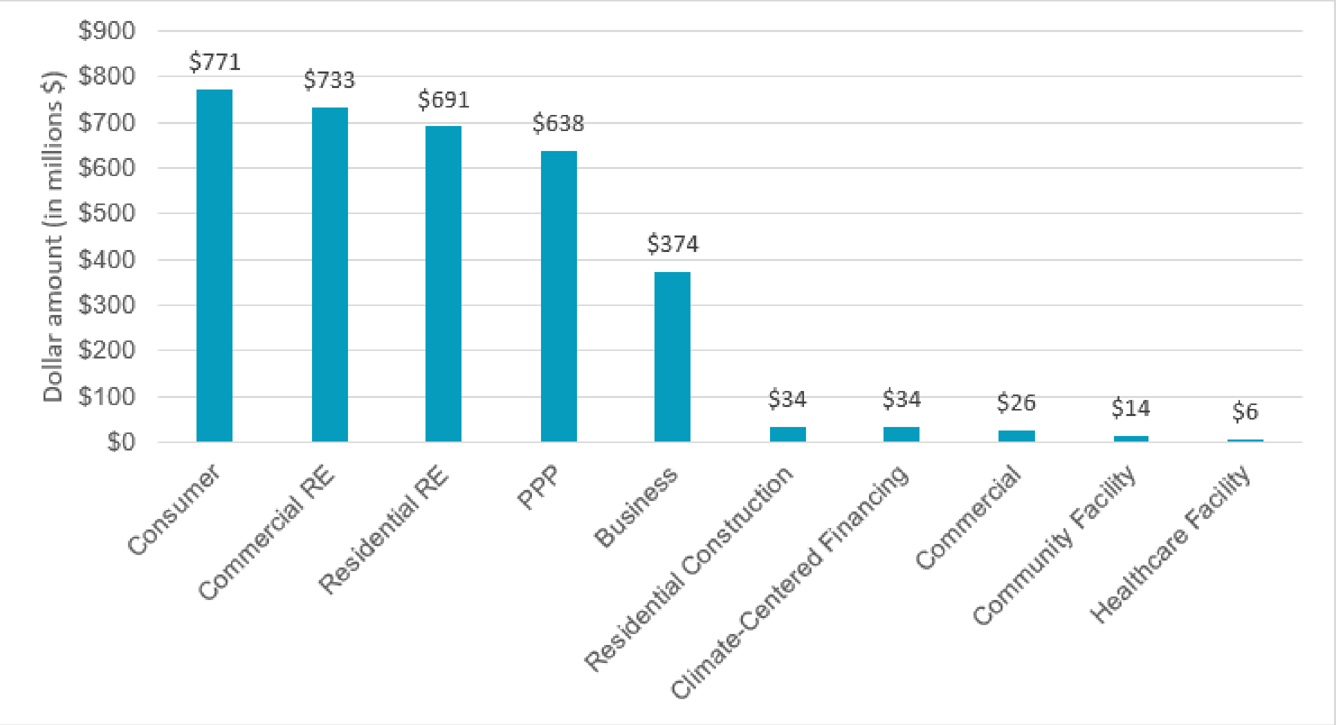
Top Lending Categories

- Consumer lending was the highest category of lending in terms of total loan dollars. Consumer lending was also the category with the greatest number of loans issued. This largely reflects the skewed impact of a single large bank.
- When excluding that bank from the analysis, commercial real estate emerges as the largest category for loan volume ($563 million) and second largest for loan volume (873), while PPP emerges as the largest category for loan volume (roughly 17,000 loans) and second largest for total amount of lending dollars ($486 million).

Figure 4 – Top lending categories by total dollar amount



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Lending Zip codes – Race/Ethnicity

Overall, 53% of the population in the loan geography of the lending sample is minority, and zip codes with that percentage minority population or higher account for $2.6 billion dollars (77% of all loan dollars) from the sample. When excluding PPP lending, the minority share of zip codes jumps up more than ten percentage points to 68%.

Median Income in Zip codes Served

The overall median household income for all zip codes in our sample was $71,765, which is roughly comparable to the national median household income in 2021 of $70,784. Nevertheless, median household income by race varied widely in the zip codes: Asian and white median incomes were higher than the national median, American Indian and Alaska Native household income matched the national median, while Black and Hispanic incomes were lower than the national median.

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Poverty in the Zip codes Served

- 13.5% of people in zip codes from our sample are living in poverty versus 11.6% of the nation's total population in 2021. Zip codes with this poverty rate or higher account for $2.6 billion of total lending dollars, roughly 76% of all lending dollars in the sample.
- 18% of people from the zip codes in the sample are 125% below the poverty line, versus 15% of the nation's population in 2021. Zip codes with this rate of 125%-based poverty or higher received $2.5 billion or 74% of total lending dollars in the sample.

Figure 8 – Poverty rates in MDI lending areas vs national average

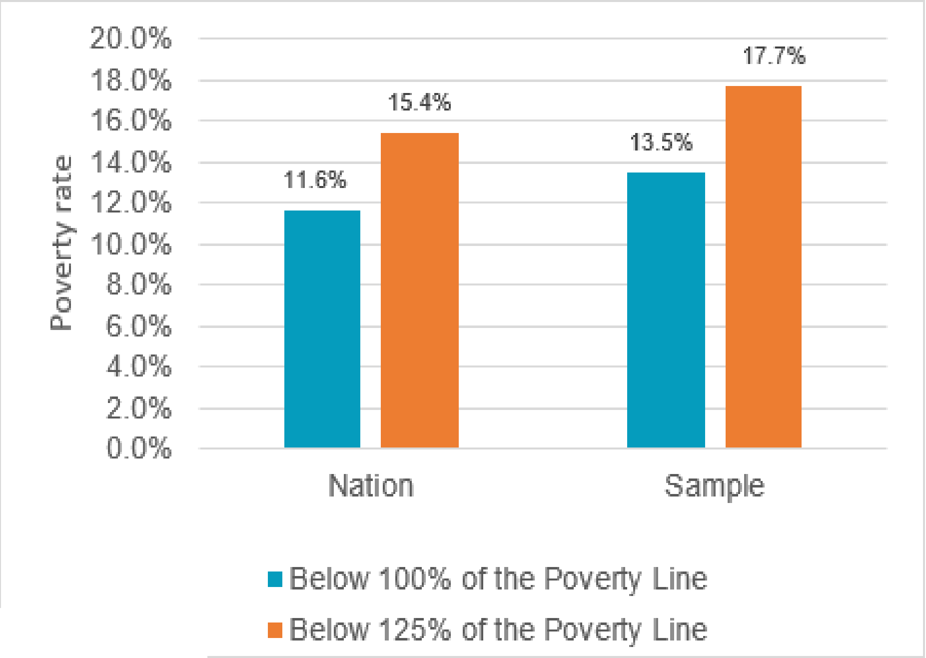

Table 8 – Poverty and household income by majority race

Race/ethnicity	Percent below 125% of the poverty line	Median household income
Black	27%	$45,000
Hispanic or Latino	28%	$49,000
Asian	12%	$107,000
White	16%	$76,000

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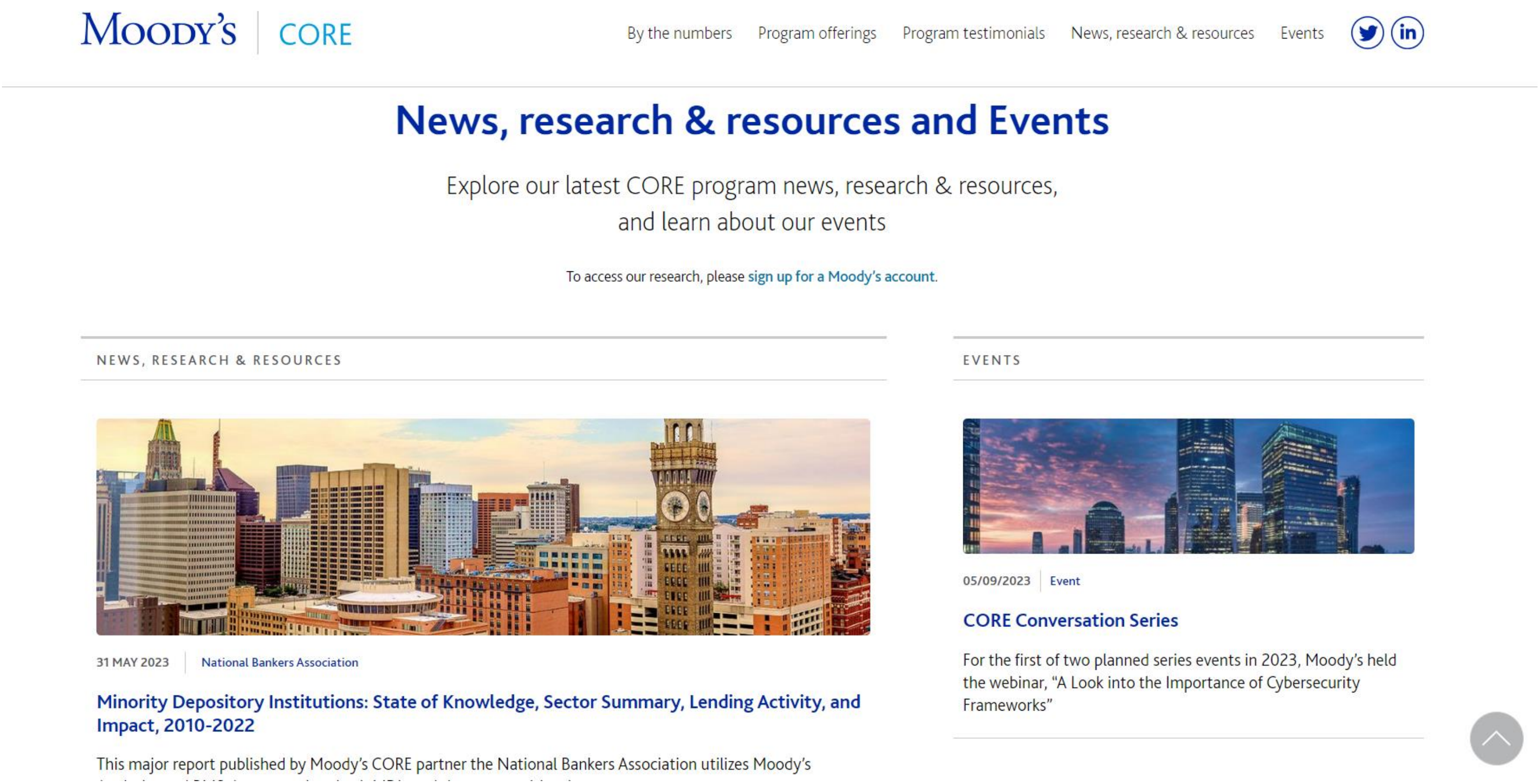
Analysis with Moody’s Data

Using Moody’s Analytics data, we examined three key economic and social variables: median household income, median unemployment rates, and total number of bankruptcy – including historical and forecasted, all at the county level. We also used Moody’s RMS data to explore climate risk, which combines historical and forecasted into a single composite score, at the postcode level.



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Moody's Analytics – Socioeconomic Data

Figure 9 – Historical and forecasted median household income

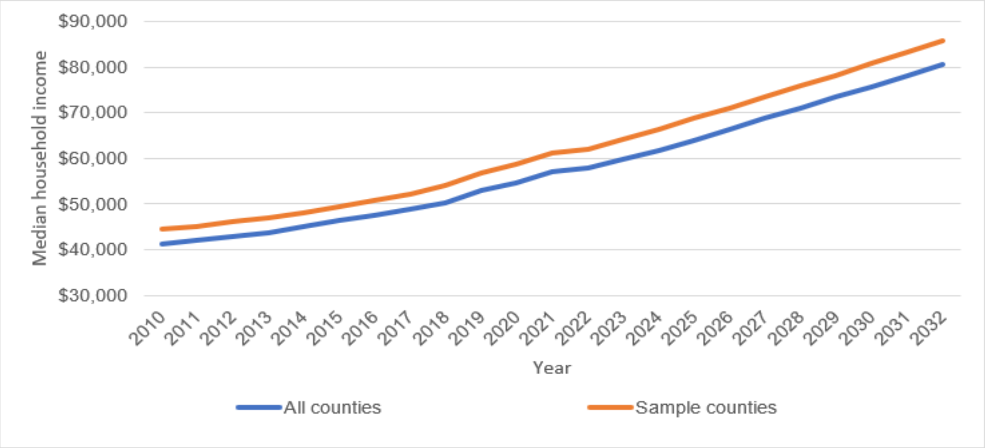
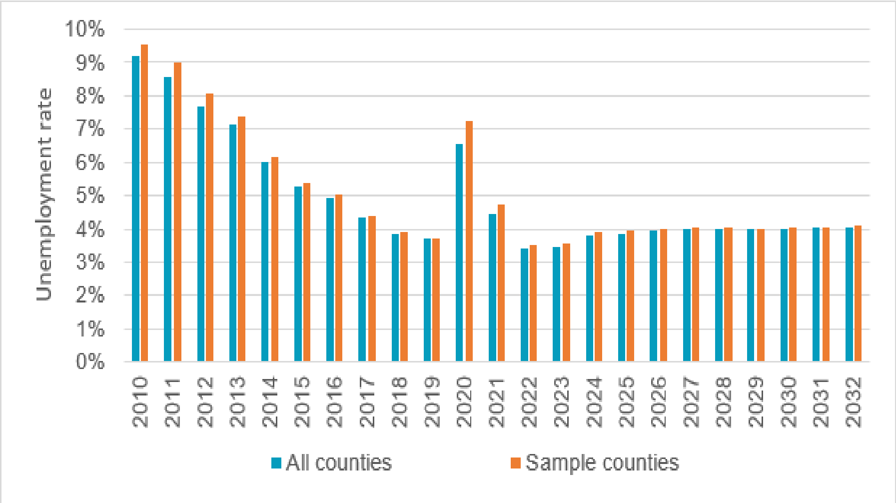
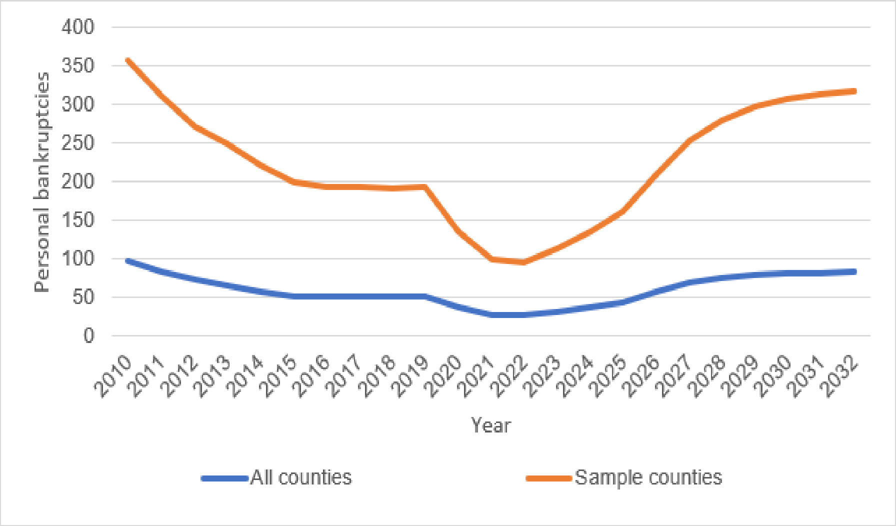


Figure 10 – Historic and forecasted unemployment rates



The median county in our sample has higher median household income, higher unemployment rates, and greater rates of bankruptcy – historically and forecasted into the future.

Figure 11 – Historic and forecasted bankruptcies



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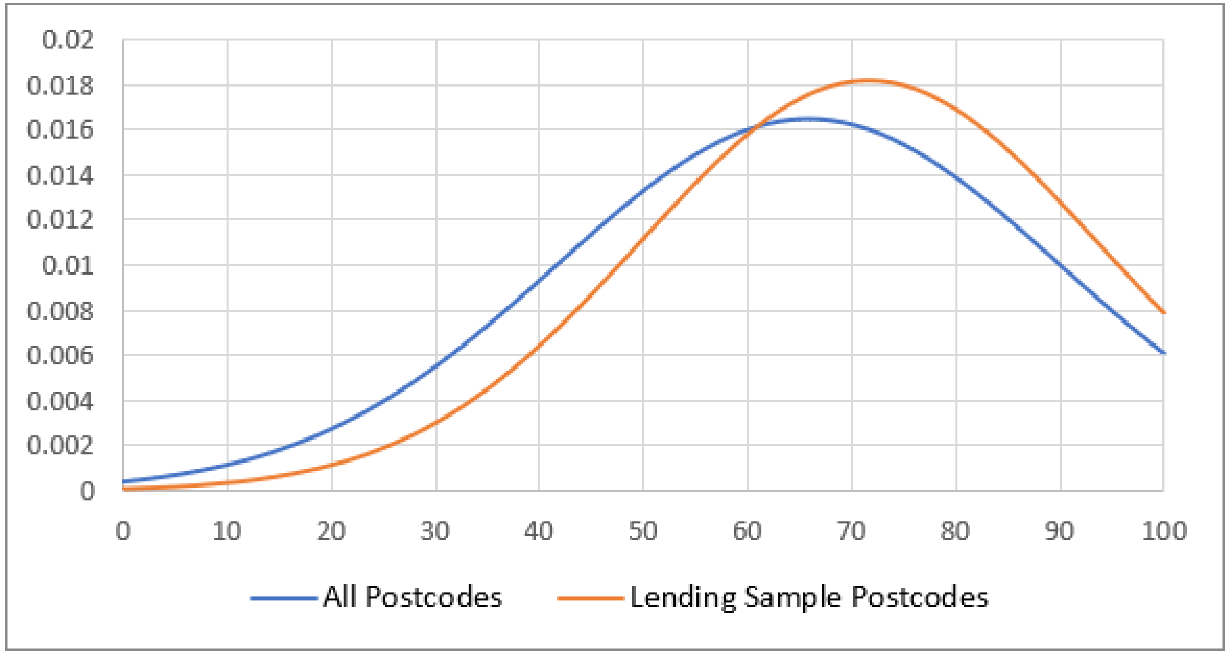
Moody's RMS – Climate Data

Postcodes in our lending sample have a median aggregated risk score of 78 which is ten points higher than the median of 68 for all postcodes in the United States. Roughly 60% of postcodes in our lending sample have an aggregated climate risk score above the median risk score for all postcodes in the United States, while 53% of postcodes in our lending sample have a median risk score of 75 or higher. Finally, nearly 28% of postcodes in the lending sample have median aggregated risk scores of 90 or above.

Figure 12 – Climate risk distribution



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Disaggregated Climate Risk by State

(Based on zips within states that received MDI lending)

Table 10 – Climate risk scores for lending sample post codes within top 10 states

Location	Overall	Flood	Heat	Hurricane	Earthquake	Water Stress	Wildfire
GA	92	52	60	77	2	46	75
FL	92	36	43	92	44	50	66
NJ	88	16	52	85	39	58	49
NY	87	19	53	81	55	57	33
DC	87	7	53	81	30	53	72
CT	86	30	51	84	30	58	47
NC	85	54	33	88	8	43	65
TX	72	20	51	45	4	70	70
US	***72***	***28***	***53***	***46***	***17***	***56***	***61***
CA	62	15	46	0	18	77	78
IL	57	29	74	0	0	74	44

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Three Takeaways and Closing Thoughts

- 1): Government, corporate, and philanthropic sectors should continue to drive additional capital to MDIs
- 2): MDIs need to be on the frontlines of climate-based finance
- 3): MDIs should be centered in all future fiscal responses to economic crises

The next few years in particular hold potential to be an inflection point for the nation as new sources of federal dollars flow to communities across the U.S. to support infrastructure, clean energy, semiconductor production, and

other key investment areas. We are confident that MDIs will continue to expand their social impact and we look forward to producing additional research that helps to deepen understanding of this vital sector.

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