Improving Access to Credit in Majority-Black Neighborhoods

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Background

Achieving the American dream – the freedom of opportunity and the ability to improve one's economic wellbeing by investing in education, real estate, and entrepreneurship – requires capital. But, in the United States, access to capital for individuals and business owners is uneven based on race. In 2019, the median net worth of a typical white household, $188,200, was 7.8 times greater than that of a typical Black household, $24,100 (Bhutta et al., 2020). Most houses are bought with a mortgage and most businesses rely on credit to fund their expansion. And place matters more than ever as the overall geographic mobility of Americans is declining (Molloy et al 2017). This working paper examines access to credit in majority-Black communities and several private and public sector levers that could improve access. We examine the role that detailed microgeographic data could have on increasing the scrutiny of financial institutions under the 1977 Community Reinvestment Act, the role of the public and private sector in investing in Minority Depository Institutions, and the role of increasing access to and capacity of Community Development Financial Institutions.

Questions and Aims

1. How does local banking competition impact the rate of return on deposits and the interest rate on mortgages?
2. Does a greater "rate spread" implied by lower competition negatively affect wealth accumulation for Black households and access to neighborhood businesses in majority Black neighborhoods?
3. Does limited lending competition allow for the entry of non-traditional and predatory financial services into majority-Black neighborhoods?
4. How has the decline of Minority Depository Institutions (MDIs) impacted the welfare of Black households and neighborhoods?
5. What private and public sector policy levers could help improve access to capital for Black households and majority-Black neighborhoods? What role should the Community Reinvestment Act (CRA) play in informing policy makers? How can Community Development Financial Institutions (CDFIs) improve access to capital? How can the private and public sector invest in MDIs to increase their financial service offerings?

Preliminary Findings

Figure 1: Banking competition in Black neighborhoods, 2017

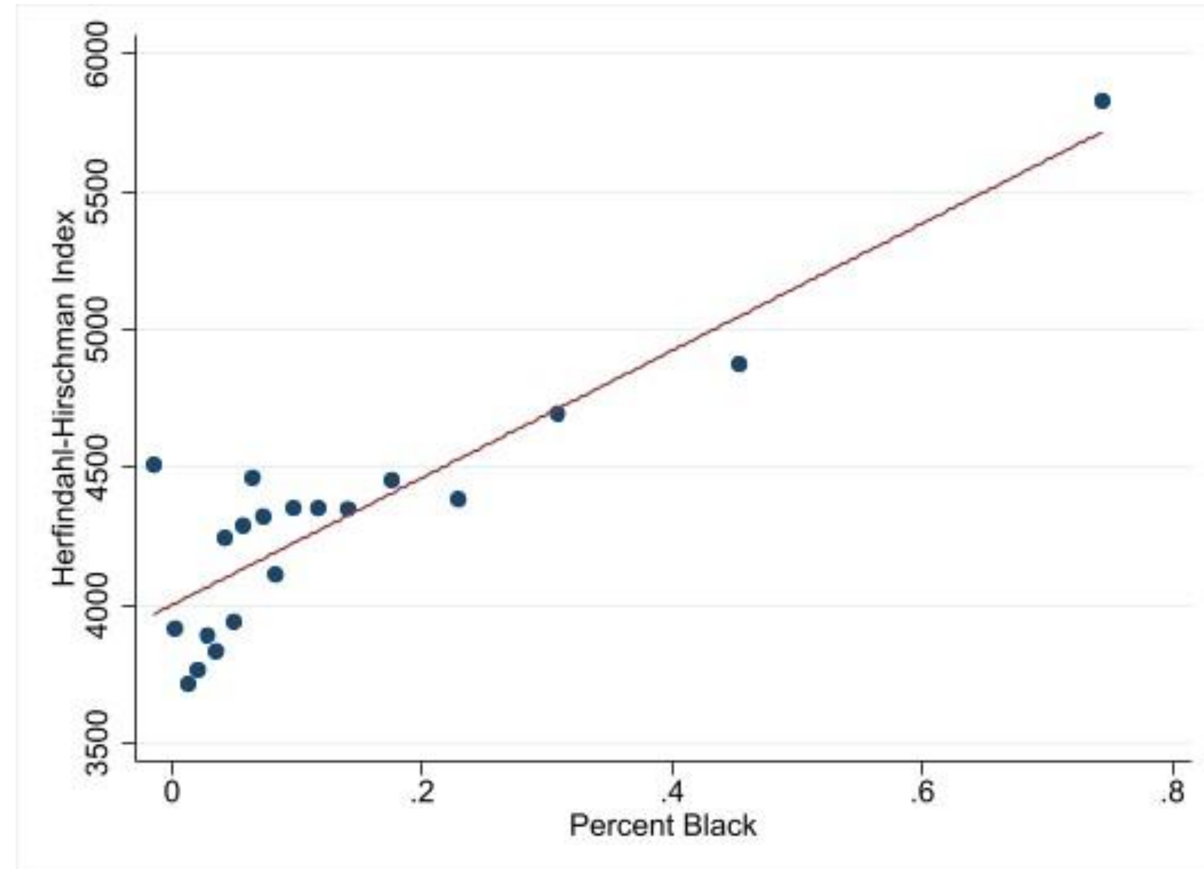


Figure 1 is a binned scatter plot that shows the relationship between the share of Black residents in a zip code and banking competition (as measured by HHI) in zip codes located in metropolitan areas with over 250,000 people after controlling for population. As the share of Black residents increases in a zip code generally the HHI increases, meaning less competition.

Figure 3: Service businesses in Atlanta, 2018

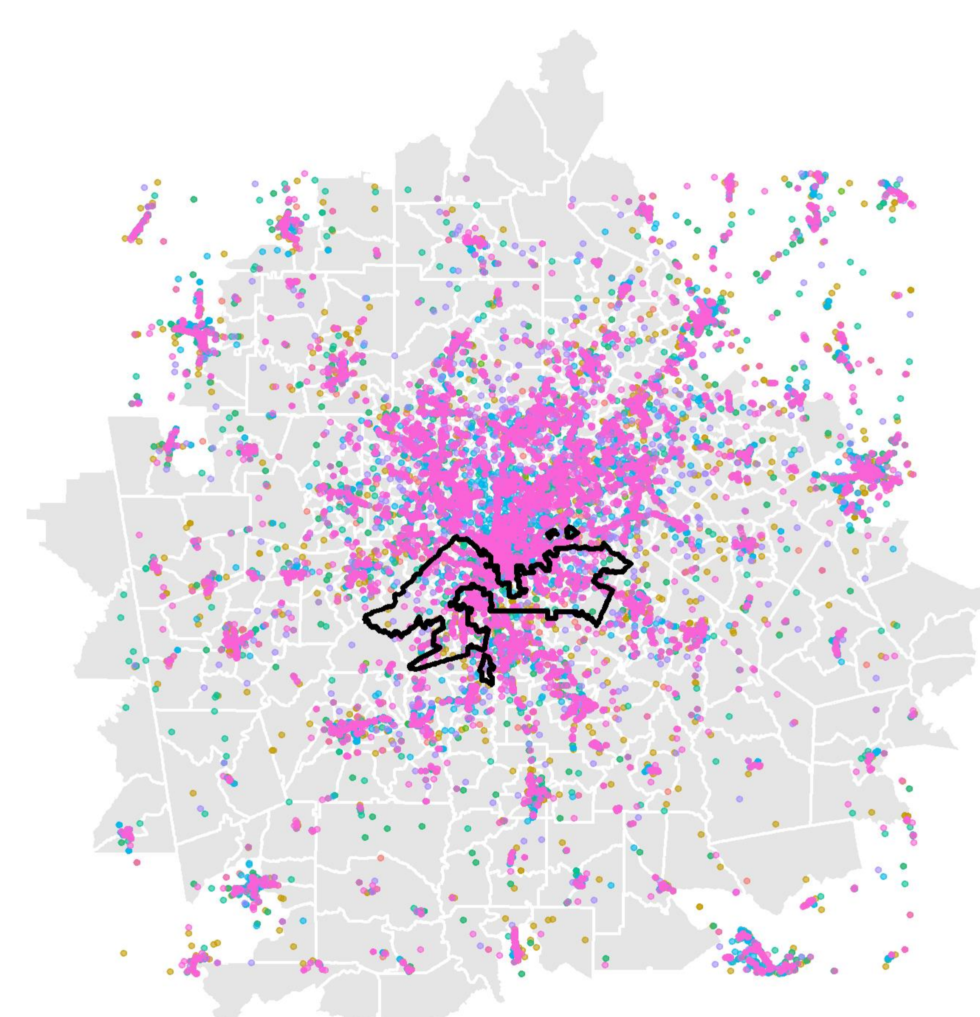


Figure 8 displays the differences in the density of local services across Atlanta. The boundary is the set of census tracts where the fraction of Black residents is greater than 80%, showing lower service levels in those neighborhoods

Figure 2: Loan-to-income ratio for mortgage loans in the Baltimore Metro Area. 1995 to 2012.

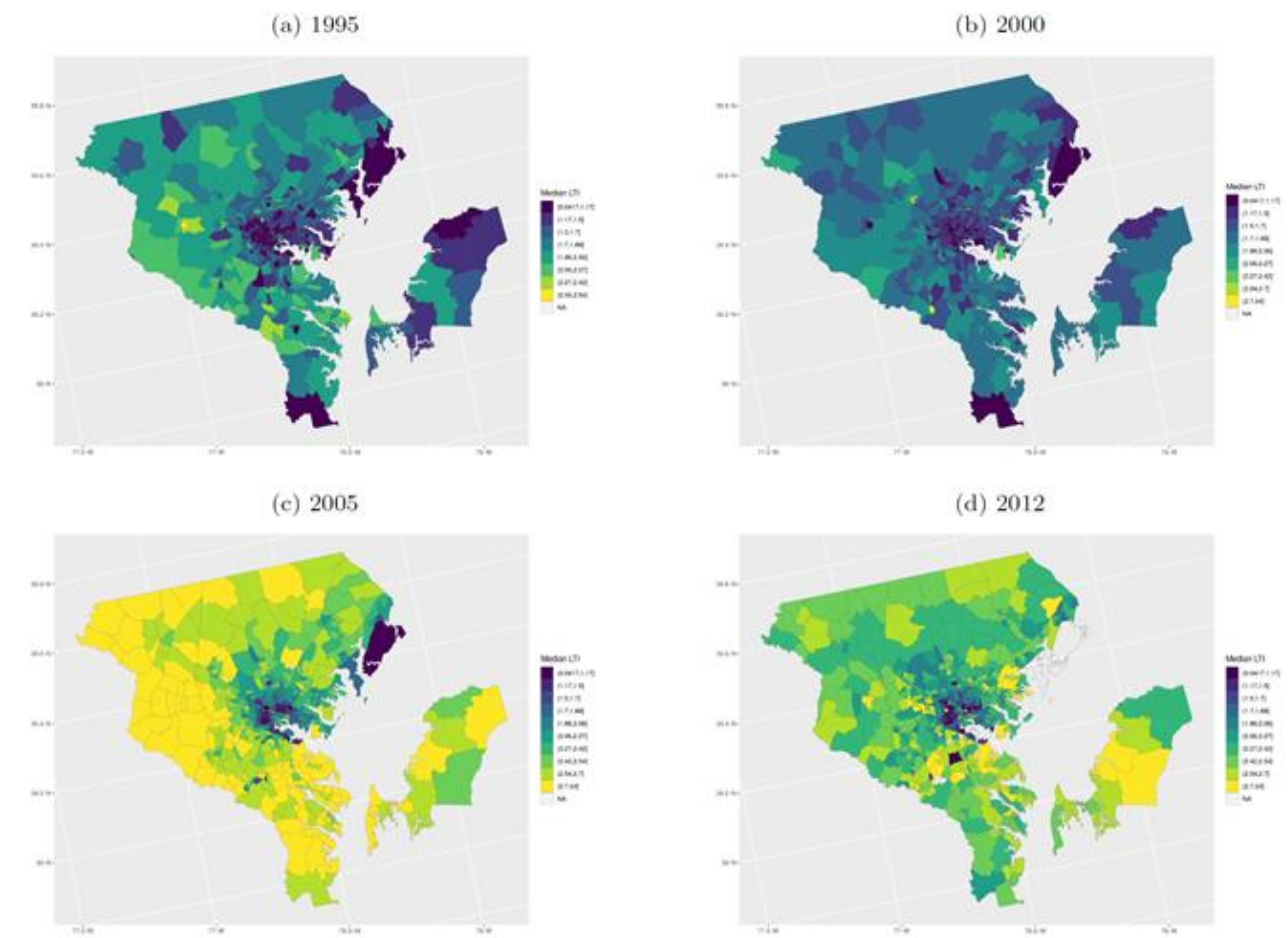
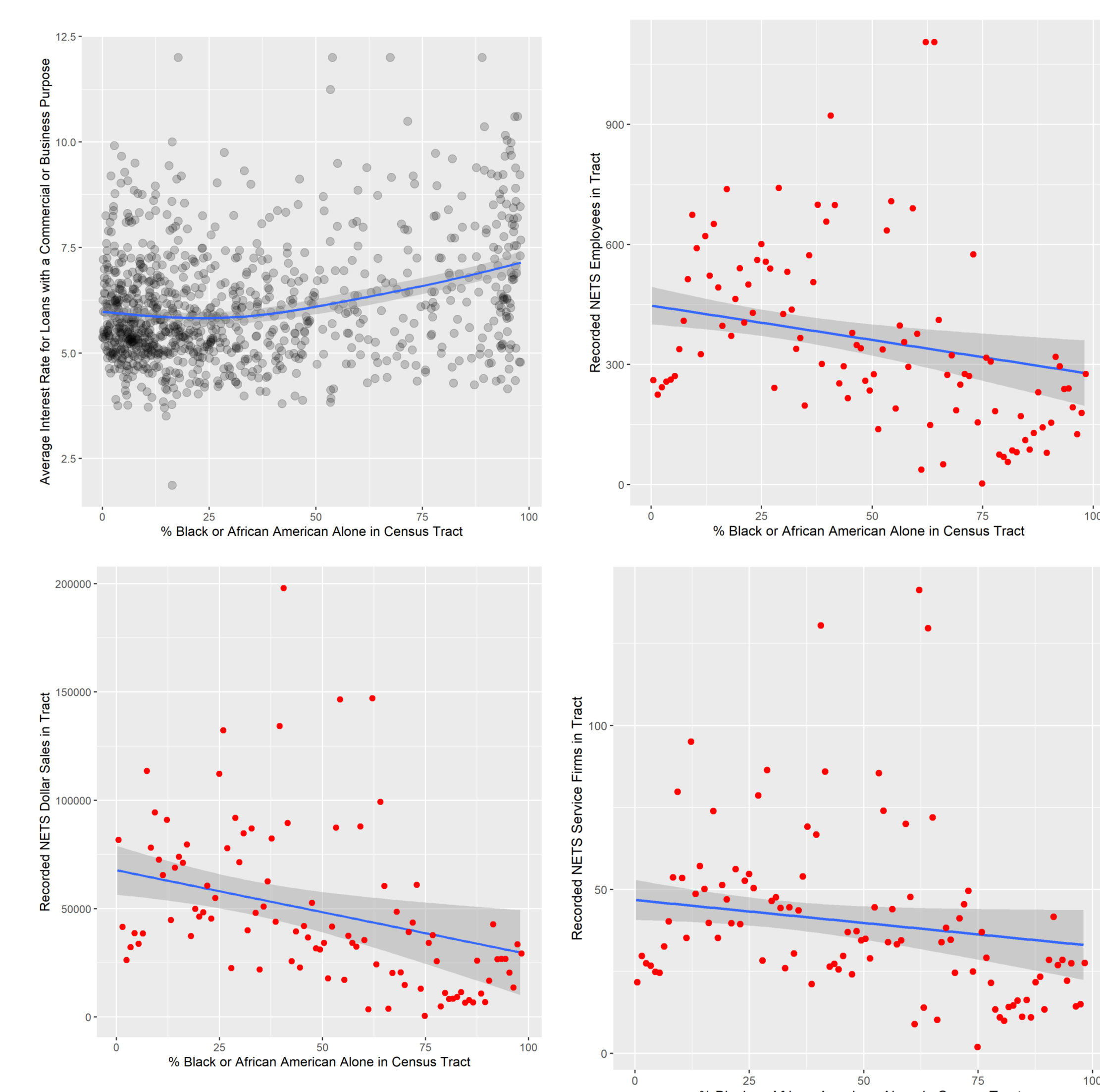


Figure 2 presents maps of the dollar weighted loan-to-income ratio (LTI) by census tract. Darker colors correspond to lower LTIs. It suggests that lenders have more stringent lending standards in Baltimore City and especially in the city's majority Black neighborhoods where the LTI ratio is the lowest.

Figure 4: Business Loans and Service Firms in Black Census Tracts



The upper-right panel shows the tract-level average dollar-weighted interest rate on loans with a commercial. Each dot is a census tract in the Atlanta metro area. Interest rates are insensitive to racial composition for the share of Black residents in a neighborhood below 25%, and then grow to be 1 percentage point higher in Black neighborhoods. The upper-left panel presents the number of employees in service firms by percentage Black. The lower-left panel presents the same but for the dollar sales. The lower-right panel shows the number of service firms.