5-6-2022

Bank Types, Inclusivity, and Payroll Protection Program Lending During COVID-19

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National Conference on Inclusive Economic Development & Recovery

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Research Questions

1. Do bank types matter in the implementation of the Paycheck Protection Program (PPP)?

2. Do differences in PPP lending between poor and non-poor, and minority- and majority-white communities vary by bank type?

Bank Types

- Top 50 Derivative Banks - large market-based financial institutions.
- Community Banks - small, locally-owned and -operating deposit-taking institutions closely tied to local economies.
- Credit Unions - financial cooperatives owned and operated by depositor-members, engaged in conventional lending practices.
- Community Deposit Finance Institutions (CDFIs) – federal certification to assist low-income individuals and communities.
- Farm Credit System (FCS) - nationwide network of cooperative lending institutions that assist US agricultural firms.
- Financial Technology Firms (FinTech) – financial institutions that use software to offer traditional banking services to firms.
- NB: We examine systems associated with each bank type.

Hypotheses

Null

- H0: The difference between lending to firms in poor and majority-minority communities versus non-poor and majority white communities will be similar across all types of banks.

Theories of corporate market-based vs relational banking

- H1a: Poor and minority communities will be less well served in the PPP by giant bank corporations than comparable nonpoor or majority white communities (receive fewer PPP loans or no loans at all).
- H1b: Poor and minority communities will be as well if not better served by alternative banks and FinTechs than large bank corporations in PPP lending than nonpoor or white communities.

Theories of localism, relational banking and racial segregation.

- H2a: Poor and minority communities will be less well served in PPP lending by community banks (and perhaps credit unions or farm credit associations) than comparable nonpoor or majority white communities
- H2b: Poor and minority communities will be markedly better served in the PPP by CDFIs, and as well if not better served by giant bank corporations than nonpoor or white communities.

Data and Methods

Data

- Merged SBA loan-level data (11.7 million loans), ACS socio-economic data and bank/lender information.
- Unit of analysis is 32,000 ZIP Code Tabulation Areas (ZCTAs).
- Descriptive statistics for loan outcomes by ZCTA.

Methodology

- Zero-inflated Negative Binomial (ZINB) model to measure:

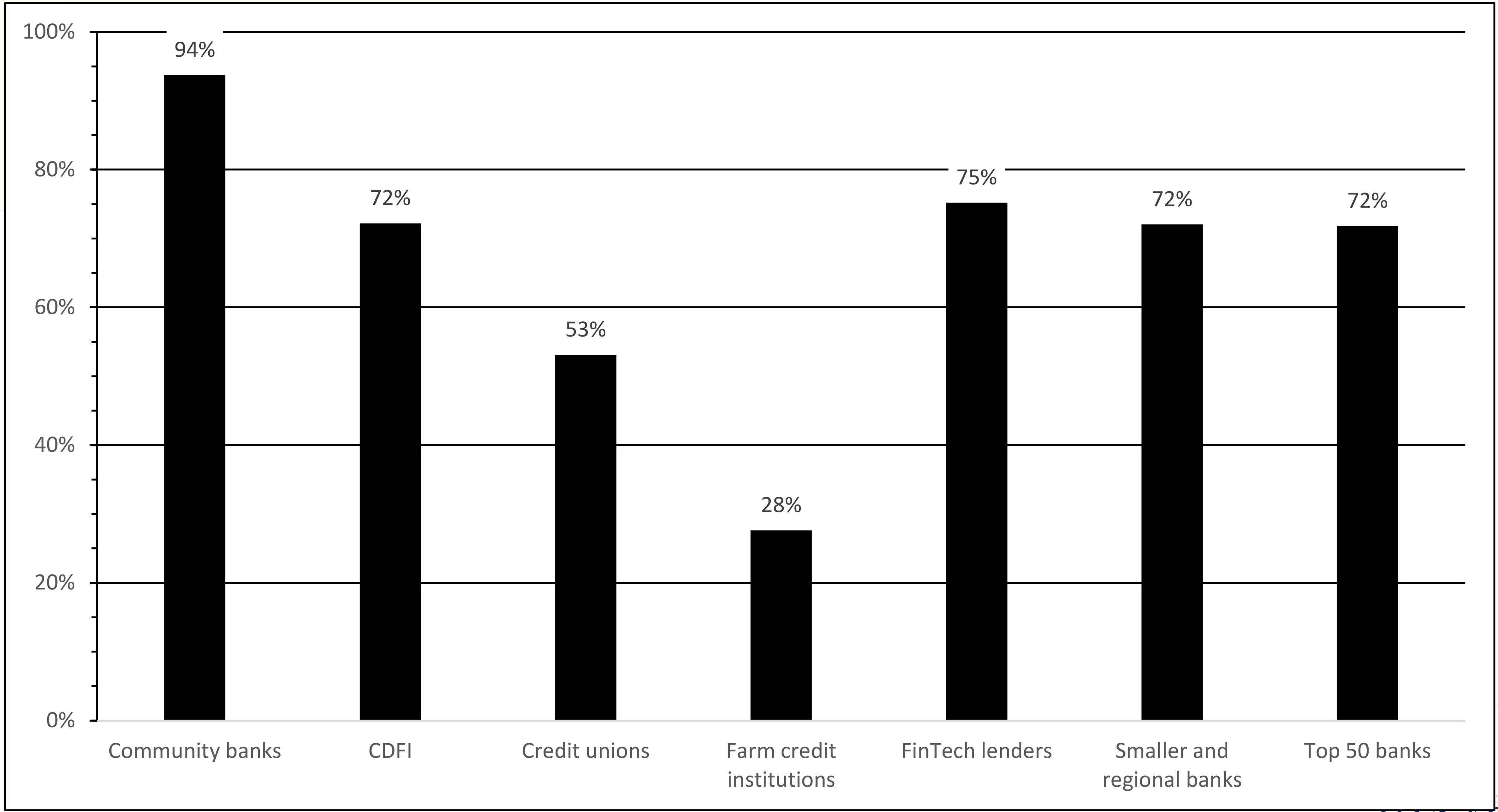
  a) The effect of community characteristic on whether a bank type lends in a community and how much they lend.

  b) Two key community characteristics -- poverty (≥ 20%) and race (white%< 50) -- are used to determine whether not each bank type makes a loan at all in that community and, if so, how many loans that bank type makes.

  c) ZINB generates the probability of zero (i.e. a bank type not making a loan in a ZCTA) and the conditional probability of zeros and positive counts.

- Controls include: 1) log of population; 2) log of business establishments; 3) dummy variable for poverty (≥ 20%) and minority (white % < 50); 4) county controls for bank ecology including #branches, ROA, local deposits, #lenders of same type, log of county population.
- The dependent variable is the number of loans made by each bank type.
- Robustness checks include: 1) Modeling only loans to small businesses (under 100 employees); 2) commuter zones instead of county; and 3) using various poverty and minority thresholds.

Where Banks do Business: Coverage Rate by ZCTA



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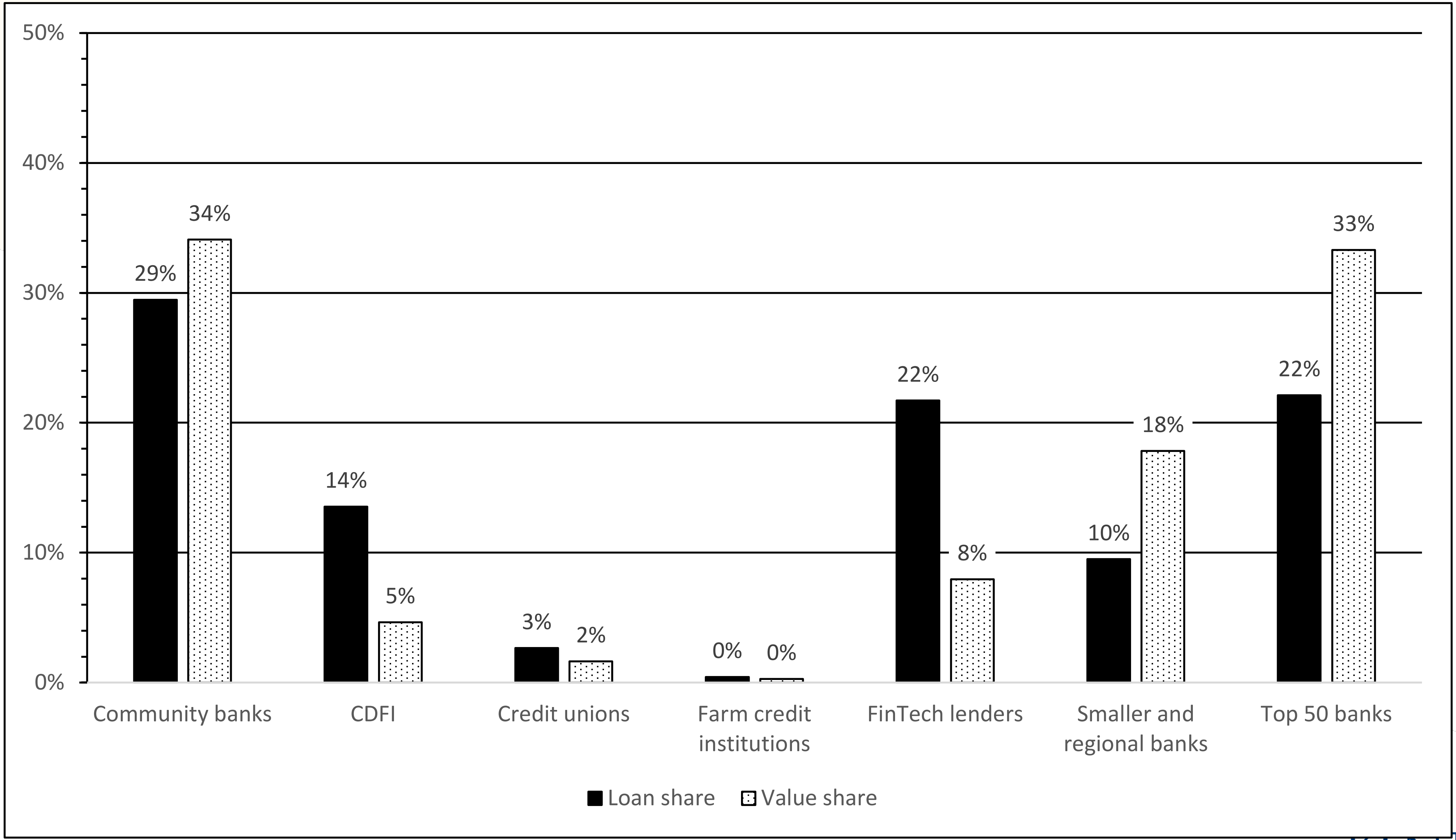
Number and Volume of Loans by Bank Type



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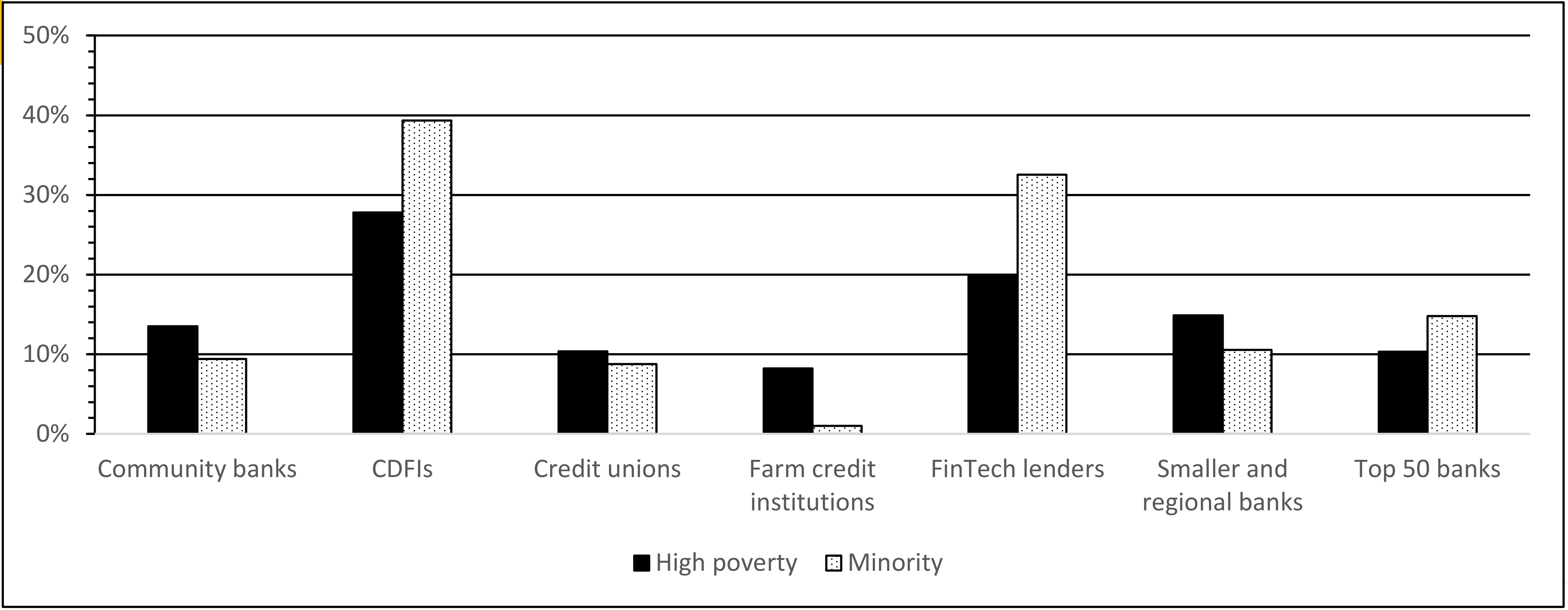
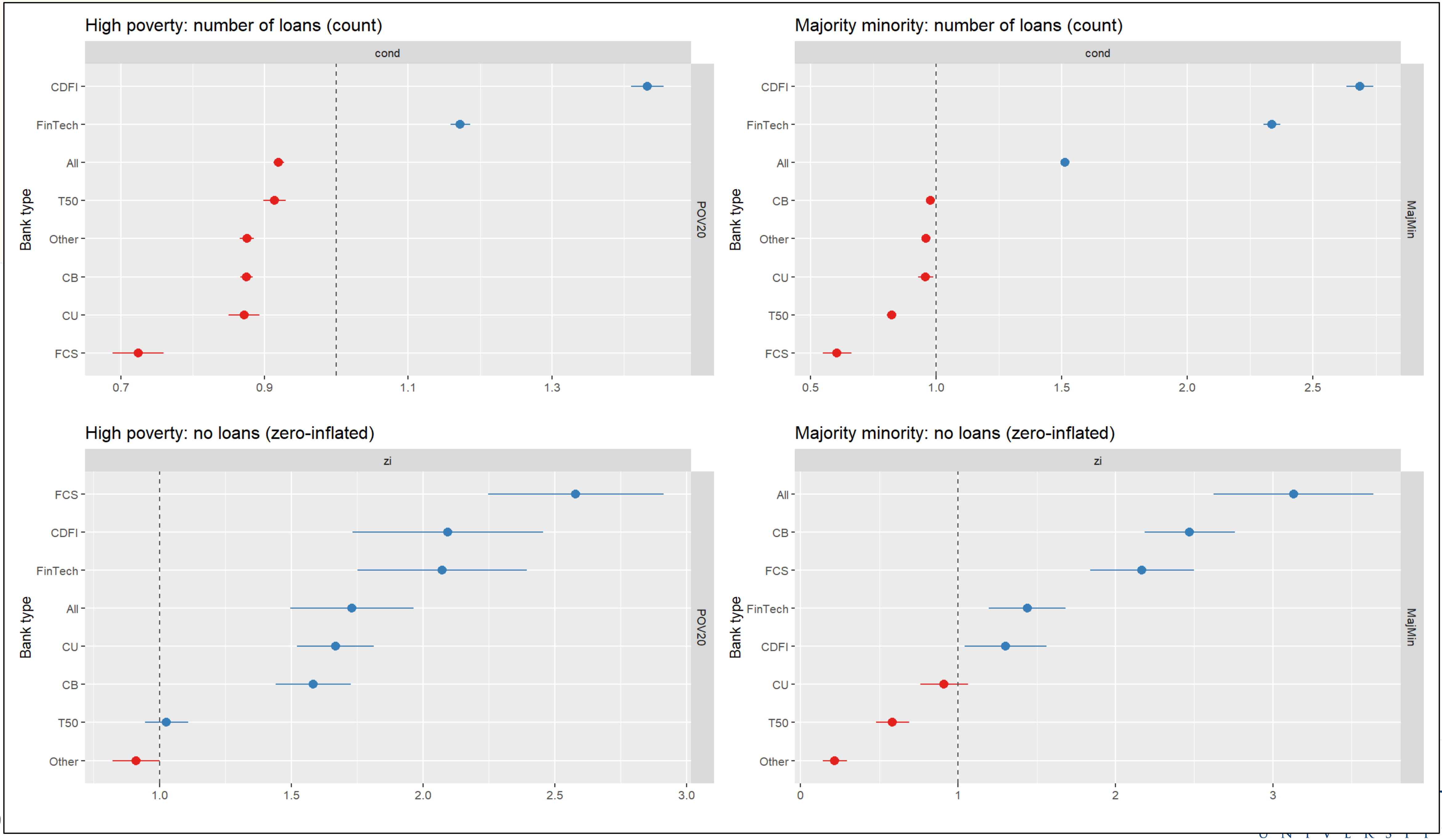
Share of Lending in High Poverty and Minority ZCTA by Bank Type - a measure of priorities




High poverty: number of loans (count)
cond
CDFI
FinTech
All
T50
Other
CB
CU
FCS
Bank type
POV20
0.7
0.9
1.1
1.3
Majority minority: number of loans (count)
cond
CDFI
FinTech
All
CB
Other
CU
T50
FCS
Bank type
MajMin
0.5
1.0
1.5
2.0
2.5
High poverty: no loans (zero-inflated)
zi
FCS
CDFI
FinTech
All
CU
CB
T50
Other
Bank type
POV20
1.0
1.5
2.0
2.5
3.0
Majority minority: no loans (zero-inflated)
zi
All
CB
FCS
FinTech
CDFI
CU
T50
Other
Bank type
MajMin
0
1
2
3

Findings

- The ability and/or willingness to channel risk-free PPP resources to firms in poor and minority communities varied by bank type.
- In keeping with expectations, CDFIs appear to be the most inclusive bank type but the picture is complicated.
- CDFIs and FinTechs significantly increase their lending activity when they move from non-poor to poor or from white-majority to minority-majority communities.
- Community banks, Top 50 banks, credit unions, smaller & regional banks, and particularly FCS institutions, make fewer loans when the move from non-poor to poor or from white-majority to minority-majority communities and more inclined to avoid those communities entirely.
- Community banks, FCS and to some extent credit unions are less inclusive than the larger Top 50 and smaller & regional commercial banks, especially to the extent to which they more likely to avoid lending to poor or minority communities relative to non-poor and majority-white communities.
- Summary:
    - CDFIs and FinTechs are the most inclusive.
    - Community banks, FCS and credit unions are the least inclusive.
    - Big banks are inclusive particularly along racial lines

Implications of our Study

- Contracting out the PPP process to qualified lending institutions reduces inclusivity.
- Bank types matter in the deployment of federal assistance of SMEs through the PPP program.
- Reliance on community banks, credit unions, FCS institutions reduces inclusivity.
- Public policy should take into account the banking ecologies of communities rather than just target private banks.
- If we want more resources to flow to firms in poor and majority-minority communities, we should consider increasing the capacity of CDFIs and, possibly, FinTechs.
- Future research.

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Thank You.

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