

Growing up in a 'bank desert' has major costs

January 22 2020, by Andrew Sorensen



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People who are exposed to banks and other financial institutions as kids are more likely to be financially stable later in life, new research from CU Boulder's Leeds School of Business shows. People without that

exposure can expect to face some serious costs.

Tony Cookson, associate professor of finance at the Leeds School of Business, along with two co-authors, James Brown of Iowa State and Rawley Heimer of Boston College, published their research in Elsevier's *Journal of Financial Economics*. They found people who were introduced to [banks](#) as children have better [credit](#) and lower delinquencies. That higher credit score can translate to real financial advantages, Cookson said, like a 5% discount in a home mortgage over time.

"Finance is a thing you learn by doing," Cookson said. "People who grow up with finance are likely to learn the things you learn from interacting with a bank."

Those skills include understanding the power of compound interest and why it's so important to build a credit history.

Cookson and his co-authors documented the disparity by matching credit data from the Federal Reserve Bank of New York to people living in a unique setting: Native American reservations.

Native American reservations as a microcosm of finance

The tragic history of reservations led to circumstances that can reveal valuable insights for academics like Cookson. Public policy has created conditions that don't exist outside of reservations, or only exist on reservations. Sometimes policies differ by reservation. One such policy is Public Law 280 (PL280).

Congress enacted PL280 in 1953, leaving some reservations under the

domain of tribal courts, while transitioning disputes on other reservations to state courts.

"This made a difference in what types of contracts get signed," said Cookson, who has been working on Native American reservations since his master's thesis in 2006. "It changed lenders' incentives to lend or help create small businesses."

Without small business activity, Cookson and his team found, banks started to avoid tribal [court](#) reservations.

"There were these bank deserts if you're under tribal courts, because banks didn't have a basis for conducting most of their business."

Banks were less likely to locate on reservations with tribal courts because of lesser predictability of contract disputes under tribal courts, according to the paper.

The end result: tribal court reservations had 20% fewer bank branches per capita by the 2000s, Cookson's team said. And the people on those reservations ended up paying the price.

"There are individuals who don't end up developing credit history at all," Cookson said. "That changes the nature of the economic activities you can engage in. Someone without a credit card is not able to go to the store and use a credit card."

A lack of credit can exclude people from larger financial decisions as well, including mortgages or student loans.

Cookson and his co-authors also conducted a financial survey across several reservations. They found residents of tribal court reservations did not develop knowledge they could use to climb up the financial ladder.

"People who grew up near a bank knew more about bank-specific financial products," he said.

Native Americans who grew up near a bank also trusted bank officials to help with financial decisions more than those people who didn't, according to the researchers' survey.

The impacts of these gaps in financial opportunity can last a lifetime.

The broader impact of bank deserts

These banking deserts aren't just limited to Native American reservations, according to the researchers.

A 2016 Federal Reserve Bank of New York study pegged nearly 400 urban areas and more than 700 rural areas without a bank branch within 10 miles. The study estimated 3.74 million people live in those areas.

That number could be growing. S&P Global Market Intelligence marked a record of nearly 2,000 US bank branch closures in 2018 as online and mobile banking become trendier.

And all of the people in those deserts are subject to the same financial disadvantages as people living under tribal courts, Cookson said.

"I think wherever possible, it is a good idea to encourage [financial institutions](#) to operate in these types of communities," said Cookson.

While Cookson said he isn't advocating for subsidizing banks necessarily, he does think policymakers should take a hard look at where banks are and where they aren't.

"Ultimately, we're facing a policy tradeoff," he said. "Having banking,

especially local banking, in your community is really a valuable thing for households. Even with [online banking](#) available, local banks matter because people learn when they bank."

More information: James R. Brown et al. Growing up without finance, *Journal of Financial Economics* (2019). [DOI: 10.1016/j.jfineco.2019.05.006](#)

Provided by University of Colorado at Boulder

Citation: Growing up in a 'bank desert' has major costs (2020, January 22) retrieved 2 May 2024 from <https://phys.org/news/2020-01-bank-major.html>

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