POLICY BRIEF

Bill Bynum, CEO of Hope Enterprise Corporation, Hope Credit Union, and Hope Policy Institute, knows what it is like to be excluded from traditional financial institutions. Many Black families in his community relied on a credit union operated out of the school vice principal's garage. His grandmother did not feel comfortable enough to use a traditional bank until her 100th birthday in 2015.

The 12 District Banks of the Federal Reserve System are partnering on a Racism and the Economy virtual event series to highlight impacts of structural racism and potential solutions. In its tenth installment, a session focused on financial services on November 16, Bynum summarized the day's theme when he said, "Racism is all too pervasive in today's economy. Arguably, nowhere more than the banking system."

The event underscored three factors that perpetuate racial inequities through the financial services industry.

- **The high cost of being poor.** Experts including Bynum and Lisa Rice, president and CEO of the National Fair Housing Alliance, described how the mainstream credit market requires financial credentials like a good credit score that many people, especially those the system marginalizes through racism, lack. They are left to overpriced products rife with exploitation, fee extraction, and delinquency. These alternative tools may worsen borrowers' credit records, if they have any effect on them at all.
- **A mismatch between people's needs and available services.** Gaps in financial service use do not imply gaps in the sophistication of client segments or the need for improved financial literacy. "People are mostly very aware of why they make the choices they do. The reason is that banks are not serving them well," explained Lisa Servon, Penn Presidential Professor and department chair of City and Regional Planning at the University of Pennsylvania's Weitzman School of Design. Like Bynum, Camille Busette, a Brookings Institution senior fellow in economic studies and governance studies at the Metropolitan Policy Program and director of the Race, Prosperity, and Inclusion Initiative, emphasized the distrust and discrimination that her immigrant family felt in the United States. They opted to save cash under mattresses. Terri Friedline, an associate professor at the University of Michigan's School of Social Work, addressed this misalignment in the fintech industry. She pointed out different comfort levels, by race and ethnicity, with "sacrificing privacy to participate." To address the problem, Lakota Vogel, executive director of Four Bands Community Fund, a Native Community Development Financial Institution (CDFI) in South Dakota, explained how CDFIs can create opportunities where traditional banks have not met residents' needs.
- **Inequality across banking institutions.** Robert James II, chairman of the National Bankers Association and president and CEO of Carver Financial Corporation, explained that the racial wealth gap exists between both individuals and institutions. He cited that before the Great Recession, "there were 41 Black-owned banks in the [United States]. Now there's only 19. They control $6 billion in assets versus a total of $22 trillion in US commercial banks as a whole."

Solutions in policy and practice

This event featured a panel of proposals aimed at changing conditions to address structural racism in financial services. Experts made these policy recommendations:

- **Move investments to "good actors" in the financial market.** José Quiñonez, founder and CEO of Mission Asset Fund, advocates for getting people into the financial system through products designed for them. He said we do this by investing in "good actors" in the industry that meet their needs. He emphasized that we too often focus on individuals' deficits, where instead we need solutions that leverage their strengths. Vogel agreed that we should consider the benefits of relationship lending versus transactional credit products, and that it is important to perceive communities with "the right risks in mind."
- **Provide down payments for first-time homebuyers through a Special Purpose Credit Program.** Rice seeks to address the homeownership gap, which she says is "as large as it was when redlining was legal." She proposes a solution that uses the existing Special Purpose Credit Programs (SPCP) tool to meet the needs of marginalized groups. This SPCP would center on down payment assistance for first-generation homebuyers, thereby addressing steep racial inequities. James agreed that this could address racial disparities despite being race-neutral on the surface. He pushed us further to reconsider whether the 30-year mortgage is meeting needs of today's economic environment.
- **Mandate all on-time rent payments be reported to credit bureaus.** Abbey Wemimo, cofounder of Esusu Financial Inc., proposes bridging the racial wealth gap through credit building by using technology to include alternative data such as rent payments in credit reports. He called for a congressional mandate to do this, which Servon said is critical so that organizations would not have to pay to be a part of such a program.

These proposals, explored in papers created for the event, are linked above and hosted alongside preexisting Fed publications in the event's resource library.

Federal Reserve as a leader

The Federal Reserve has tools to address racism in the financial services industry. For one, the Fed can prioritize inclusion in payments through systems that are efficient, trustworthy, and accessible. Federal Reserve presidents Esther George, Tom Barkin, and Raphael Bostic cited the FedNow payments service as an example of Fed efforts to expand inclusion. In addition, the Fed can hold institutions accountable through its regulatory responsibilities. One way is to "reshape how we measure and conceive" borrower risk, as James put it. In general, presidents acknowledged opportunities for the Fed to lead on regulation through its Community Reinvestment Act obligations.

For more information

If you have additional questions or would like to connect with Federal Reserve staff in your area, contact: Samantha Porter at the Philadelphia Fed, Janelle Williams at the Atlanta Fed, or Tiffany Hollin-Wright at the Richmond Fed.