

# EVALUATION OF CRA

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## Discussion Comments

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Let me say, in general, that I believe all of the papers contribute to a healthy discussion of critical issues related to the evaluation of the Community Reinvestment Act (CRA), and I commend all the authors for excellent papers and presentations that continue to stimulate our thinking on CRA. That said, let me give you a few specific comments based on my readings, the presentations, and some of the questions that have been raised during today's discussions with the papers' authors.

The first paper, *The Effect of the Community Reinvestment Act on Bank and Thrift Home Purchase Mortgage Lending*, considers the extent to which the Community Reinvestment Act has led institutions under its authority to increase the number of home purchase mortgage loans to low- and moderate-income borrowers and neighborhoods. The paper identifies the early 1990s as a point at which significant CRA activities began to occur and identifies a number of reasons for that benchmark in activities.

Those reasons include experimentation with new products at the urging of community groups, public availability of CRA ratings, expansion of available lending information through the Home Mortgage Disclosure Act, the first-time denial of a merger for CRA reasons, the strengthening of CRA regulations in the mid 1990s, and the acceleration of merger activities within the financial industry.

I would suggest that there were two additional reasons for these activities. First, the late 1980s to early 1990s was a time when we had significant community capacity to participate in partnerships with financial institutions and others through Community Development Corporations (CDCs), Community Development Financial Institutions (CDFIs), and other community-based entities. This greatly increased the ability of financial institutions to get CRA-related products out and tested without prohibitive costs to the financial institutions. Second, in the mid- to late-1980s, we were emerging out of a period, when the savings and loan restructuring (some would say "bailout") was occurring, and the public was seeking some identifiable return (*quid pro quo*) for the massive infusion of public dollars being devoted to that segment of the financial industry. Other financial institutions were feeling a need

to demonstrate their concern for community financial issues and were more than willing to invest in programs that would show their commitment to these issues.

The paper concludes that the evidence on lending patterns thus far is consistent with the proposition that CRA does have a positive effect on low- and moderate-income lending by financial institutions under its authority. However, the paper notes that its analysis does not address the question of whether lending to low- and moderate-income borrowers and communities is increased overall by CRA. Let me go out on a limb on this one and say what the paper does not. "CRA has had a direct effect on the overall lending of financial institutions to low- and moderate-income borrowers and communities, and increased merger activities have had a direct effect on the willingness of financial institutions to do CRA lending." While I have no hard data to back up that statement, I don't think anyone in this room would disagree with me.

The second paper, *Assessing the Impact of the CRA on Banking Institutions*, tries to answer the age-old question of whether CRA lending is profitable. Given the data available, the paper does a very good job in breaking down the different aspects of profitability and determines that, based on a number of definitions of profitability, a significant minority of institutions experienced at least some loss, and a significant number incurred no loss. Virtually every financial institution surveyed reported that at least some of their CRA lending was profitable. In layperson terms, few financial institutions reported losses in their CRA lending, and nearly all reported some aspect of profit. This is encouraging news and, for a number of us, not surprising. Those who have conducted economic analyses of the aggregate dollars flowing into low- and moderate-income communities have found that contrary to popular belief, strong sources of capital do exist in these communities. Additionally, surveys of the payment patterns and histories of borrowers have found that low- and moderate-income borrowers are much more likely to be timely than others in their loan payments.

However, the question of profitability may not be the right question we should be asking. The more important question is what is the overall value of CRA lending to both the community and to financial institutions. As the paper suggests, there may be a number of reasons a financial institution engages in community development lending. As with any company, profit is but one of a number of motives around which the company builds activities. Other motivating factors include image, competitiveness, senior management philosophy, *etc.* I agree

with the earlier question-and-answer discussion suggesting that what may be more important to us is the issue of where this lending is being done successfully, and how to share and replicate that success. While the paper points out the complexity of coming to final conclusions over the question of profitability, its conclusions show no major areas of loss by financial institutions engaged in CRA lending and should allow us to move past profitability and on to other important questions.

The third paper, *The Impact of Bank Consolidation on CRA Business Lending*, focuses on CRA in the business lending context. This is a critical area to examine because the work of my institution finds that small business lending is critical to creating economic stability in low- and moderate-income communities. The paper uses the relatively new CRA small business loan data to examine how CRA-related business lending has been affected by bank merger activity during the late 1990s. The paper studies changes in CRA lending by financial institutions as a whole as well as how a consolidation or merger affects lending to the markets that comprised the financial institution's service area before the consolidation or merger. The paper concludes that financial institutions experiencing merger activities had systematically lower CRA-related loan growth than inactive financial institutions. However, the merger-related effects appear to be associated with a general decline in small business lending rather than a shift away from low- to moderate-income areas or very small businesses. The paper also found that merger-related effects can differ for urban and rural markets. I'm not quite sure what this means. What I do know is that more small business lending is needed in low- and moderate income communities, not less. So if the paper's conclusions suggest that there is a slowing of these activities either because of merger activities or because of other economic and market forces, there is cause for concern and we should explore ways to stimulate greater small business lending.

The fourth paper, *Community Organization and Community Reinvestment Act Lending in Washington, D.C.*, looks at the impact of CRA results from an advocacy strategy versus a community development infrastructure strategy. The paper suggests that more CRA lending can occur when the community has a community development infrastructure available to work with financial institutions. It also suggests that political involvement by the community translates into more loans. While agreeing with the paper, I believe that for CRA to be fully effective, the community must combine advocacy with developmental capacity. Regarding political activity and the correlation to more

loans, I think that the greater driver regarding lending activity is ultimately the market. With the right infrastructure, the market itself will generate many more opportunities for lending than political advocacy or action. In many communities, the political advocacy or action is directed at financial institutions with the desire to force them to take certain actions, usually to make more loans than before. I would argue that this is only a part of what will be necessary for needed capital to flow into low- and moderate-income communities. Political advocacy or action is also needed to ensure that the community has the ability to fully utilize the capital offered by financial institutions and are able to leverage that capital from other public and private sources. This includes public investment in the community infrastructure necessary to partner with and assist financial institutions in delivering the capital and support needs of the community to fully utilize the capital.

The final paper, *Boston's Soft Second Program: Reaching Low-Income and Minority Home Buyers in a Changing Financial-Services Environment*, is the type of case study needed to demonstrate the impact of CRA-related lending. It is a homeownership mortgage program that combines two mortgages to offer homeownership to some of Boston's poorest residents. The paper provides a compelling story of how advocacy and leadership from both the community and financial institutions have crafted a program that works. It also confirms that, to be successful, you need contributions from all three sectors: the community, financial institutions, and government. It also identifies a number of challenges that can directly impact the success of such a program. One is escalating housing prices. This calls for some thought about land banking and other strategies for ensuring that homeownership will be available to low- and moderate-income families in the future. Another challenge is rising unemployment and falling household incomes impacting the ability of homeowners to continue to make timely mortgage payments. A third challenge is the ability to sustain a strong economy, a theme throughout a number of the papers over the last two days.

## Conclusions

Let me now offer some concluding thoughts based on all the papers and then some comments about additional areas for research and exploration. First, in trying to look at the financial impact of CRA lending, we should not underestimate its contribution to the development of the community development lending infrastructure. While much of the resources for that infrastructure have come from other sources (The

Department of Housing and Urban Development, Treasury, foundations), financial institutions have made significant contributions to that infrastructure, both with capital and operational support. There is value added to that infrastructure, both in terms of how it serves the community and the financial institution industry, that usually will not be factored into a cost-benefit analysis of profitability.

Second, the question of whether low- and moderate-income households can be attractive markets for financial services is a difficult one to answer. I believe the ultimate answer may be no, otherwise this market would have been captured some time ago. Financial institutions have not yet been able to achieve the volume and cost containment necessary to offer these services to low- and moderate-income people at an acceptable profit margin, relative to concentrating on more profitable middle- and upper-income markets. In order to do so, significant incentives would need to be provided. Those of you who have been doing this work for some time will remember that many years ago we were having this very conversation about community development lending. Then, the questions were much less about profitability, but whether this kind of lending could be done at all. The paper by **Avery, Bostic, and Canner** suggests that we have made significant progress with community development lending, and that conclusion is demonstrated by the fact that you don't hear the questions about community lending today that we heard then.

Part of the reason is that many financial institutions have community development lending programs not only for profit, but also as part of being good corporate citizens and for visibility and marketing purposes. For example, I am sure financial institutions consider the marketing value of attracting middle- and upper-income customers who are appreciative of the fact that the institution is making special efforts to invest in low- and moderate-income communities. I know that I take that factor into account when making choices about where to bank, and I'm sure many of you do the same. Having the "good corporate citizen" seal of approval has never hurt the image and marketing appeal of a financial institution, and for many it translates into a direct competitive edge in the effort to attract customers. Also, many institutions understand the concept of a double bottom line in banking. It is possible to do good while doing well. Yes, banks are in business to make money, but the discussions over the past two days have highlighted the importance of access to financial services in helping people move out of poverty and toward self-sufficiency.

We also may need to think about and clarify our goals and end

products in CRA. Is the end result to develop financial-services products for new markets (low- and moderate-income), or is it to create ways for low- and moderate-income persons to move into the financial mainstream? Are these end results contradictory, or compatible? Picking up on yesterday's discussion about the unbanked, are we okay with the creation of a two-tiered system of banking in which you have check-cashing companies providing checks for cash, payday loans, money orders, and bill-payment services for low- and moderate-income customers, and traditional checking and savings products provided by financial institutions to middle- and upper-income customers. As yesterday's discussion indicated, the current check-cashing and payday loan structure has a significant negative impact on the opportunity for low- and moderate-income households to save. If savings and wealth creation are in fact part of the formula for moving people out of poverty and towards self-sufficiency, this two-tiered system negates that opportunity. I suspect that our end goals have to again incorporate a dual purpose and result: To stimulate and create financial services markets for low- and moderate-income households that allow financial services institutions to enter and get a financial return, while at the same time allowing households to move toward more traditional banking services as their incomes rise and they move towards self-sufficiency. I also recognize this is an extremely difficult task.

Before closing, let me suggest a number of additional areas of research and exploration for future conferences. First and most importantly, we must expand our research to focus much more intensely on the financial-services needs of rural communities. Their problems, while perhaps not of the volume expressed in urban centers, are even more complex because of the limited resources available to solve them. All of the issues discussed over the last two days are occurring in rural areas and need a separate analysis and formulation of solutions.

Second, a more comprehensive body of research is needed on the current and future impact of technology on CRA and access to financial services. This is the next sleeping giant waiting for us. Third, we should look to explore in more detail the value of diversity in improving financial services to all communities. This issue surfaced in an ancillary way yesterday during the discussion on relationship banking. The point was made that the strategy of creating greater diversity of African-Americans and women in one particular financial institution resulted in an increase in lending activities to African-Americans and women. While a small point, I believe this has significant promise as a solution to the continuing perception (if not reality) of disparate lend-

ing to minorities and women. Last, we should seek to research and better understand the impact of the economy on CRA lending and financial services. If you read all the papers closely, and I'm sure you did, you will remember that a number of them raised the issue of how some increased lending activities to low- and moderate-income people are tied to the sole factor of a strong economy. And we've certainly had that for the past eight to 10 years. How CRA lending may be affected by a less robust economy is not known. The next few years may offer an unexpected opportunity to test this premise as our economy cools and lending activity tightens.

Let me make one response to the comment from the floor that we need to spend more time understanding the true cost of CRA compliance and that maybe this would require some changes in the Act. This would not be a true CRA conference without someone bringing up the burden and costs created by the paperwork and our need to reduce or eliminate CRA to lessen that burden. I agree that we should continually seek ways to reduce the CRA-related paperwork and costs associated therewith, which would also allow those resources to go into even greater delivery of financial services to low- and moderate-income people. I also believe that we need to devote more attention to the successes we are having in CRA lending, and to share and make visible those successes in a much more active way. I can think of no better message or statement for CRA than one that conveys the significant impact that this lending is having in communities and for financial institutions, and I believe this would make it much easier to have a meaningful discussion among financial institutions, community advocates, and public officials regarding changes to CRA. I also believe that the financial institutions community should play an active leadership role in identifying and publicizing these successes, and I think that the American Bankers Association should help to lead this effort.