How do home country institutions influence immigrants' financial market behavior in the U.S.?

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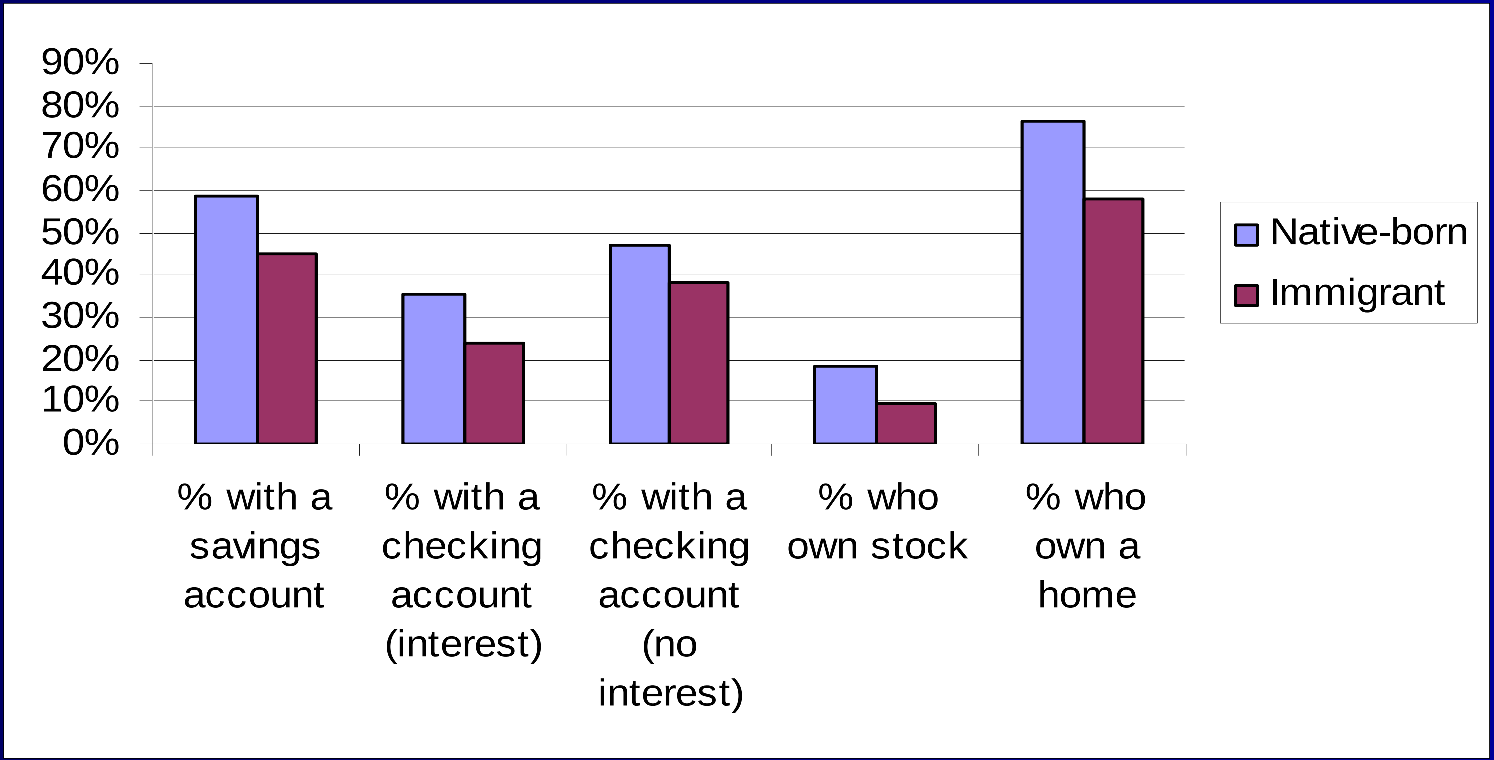
Why is immigrant financial market participation important?

- 1 in 9 individuals living in US were born abroad
- Financial market participation measures immigrant success
- Financial market participation measures society's progress in successfully incorporating immigrants

Why is financial market participation important?

- Impacts ability of households to cope with income uncertainty, find pathways out of poverty
- Impacts access and cost of credit for emergencies, home purchases, small business investment
- Impacts 2nd generation: Children learn how to use financial services from their parents
- Impacts community development: geographic concentration, target of criminals

Financial Market Participation



Survey on Income and Program Participation: 1996 – 2000, Panel

Why is immigrant financial market participation lower?

- Immigrant characteristics
  - Education, language, legal status, income
- Part of the story
- Controlling for characteristics, immigrants are 4.6 percentage points *less* likely to own stock or have a savings account

Why is immigrant financial market participation lower?

- Countries with better institutions grow faster and have more developed financial markets
- Are migrants from countries with “better” institutions more likely to participate in U.S. financial markets?
- How long do you have to experience a set of institutions for them to impact behavior?
- How persistent are these effects?

Measuring Institutional Quality

- Use a summary measure that captures ability of the country's institutions to protect private property and provide incentives for investment.
- Evaluates the risk of "outright confiscation and forced nationalization" of property. Average over 1982 – 1995. Source: International Country Risk Guide (ICRG) IRIS-3 Data.

Institutional Quality

- Low: 1.81 (Iraq)
- High: 10.00 (Luxembourg, Switzerland, Netherlands)
- Median: 7.07
- Mexico 7.51, China 7.79, Canada 9.79, El Salvador 5.07
- U.S. 9.98

Financial Market Participation Measures

- Stock Market Participation
  - Investor must be convinced that stock broker won’t abscond with funds and that institutional and legal framework is adequate to ensure that company invests in profitable projects and returns proceeds to investors
- Savings Account Ownership
  - Investor must be convinced that bank will keep funds safe, accurately pay interest and return funds upon demand.

Are migrants from countries with “better” institutions more likely to participate in U.S. financial markets?

- Yes. Suppose institutions in El Salvador were as good as Mexico’s between 1982 and 1995
  - Stock market participation of Salvadorans in the US would be 5.25 percentage points higher
  - Savings account ownership would be 4.75 percentage points higher
- Home country institutions are very important. They fully “explain” lower immigrant financial market participation rates.
  - Once home country institutional quality is controlled for, being an immigrant has no significant impact on financial market participation

How long do you have to experience a set of institutions for them to impact behavior?

- Look at the impact of institutions on financial market participation as a function of how old people were when they migrated.
- Home country institutions significantly impact the behavior of immigrants who arrive in the U.S. when they are 16 or older

How persistent are the effects of home country institutions?

- Look at the impact of institutions on financial market participation as a function of how long immigrants have lived in the U.S.
- Only immigrants who have lived in the U.S. for more than 32 years are unaffected by home country institutions.

Robustness of Findings

- Alternative measures of institutional quality
- Adding other important country level controls (GDP per capita, English is an official language)
- Various techniques for controlling for the possibility that the choice to migrate to the U.S. is effected by institutional quality

Summary of Findings

- Individuals on the brink of adulthood (less than 16) learn important lessons about how the world works.
- These lessons are likely to be learned in the family, and possibly in school. They are *not* likely to be the result of direct experience
- The effects of these lessons are very persistent, 30 plus years.

Implications

- Financial education, products and services, as well as outreach strategies may be more successful if they are tailored to the particular institutional backgrounds of different immigrant groups
  - Latin America v. Eastern Europe
  - Mexico v. Haiti
  - China v. India

Conclusions

- The decision to participate in U.S. financial markets marks an important stage in immigrant adjustment to U.S. institutions.
- Achieving financial access for many immigrants involves challenging powerful lessons, absorbed early in life.
- Immigrants have signaled their readiness to absorb new lessons by coming to the U.S.