# Message From The Interim President

## Financial Services for Lower-Income Communities

One of the Richmond Fed's most important jobs as a regional Reserve Bank is understanding the needs of our communities, including how people and businesses in low- and moderate-income (LMI) communities are able to meet their needs for financial services.

These communities make up a substantial portion of our district. As of 2014, more than one-quarter of the Fifth District's population — 8.1 million people — lived in LMI areas. (In the banking industry, a low-income area is defined as one where the median family income is up to half of the median family income for the surrounding region; in a moderate-income community, median family income is between 50 percent and 80 percent of the median family income in the surrounding region.)

Many households in the Fifth District are "unbanked," meaning they don't have a traditional checking or savings account and instead rely on services such as check cashing, payday or auto title loans, or prepaid debit cards, to name a few. These services tend to come with higher fees and interest rates than traditional banking products. Overall, nearly 7 percent of Fifth District households are unbanked, roughly on par with the national average; the share is as high as 9 percent in South Carolina and 11 percent in the District of Columbia. An additional 21 percent of households are "underbanked," meaning they do have a traditional checking or savings account but also use one or more alternative financial services. While we don't know the exact overlap between unbanked or underbanked households and households in LMI communities, we do know that consumers who use alternative financial services tend to have lower incomes. They also tend to be younger and have less education.

In some cases, individuals might take out a payday loan or buy a prepaid card because they lack the credit history to qualify for a traditional loan or open a bank account. It's also possible they don't have enough information about the differences between traditional and alternative services. But survey evidence indicates that some consumers actually prefer to use alternative financial services, perhaps because they perceive them as more convenient — there's no waiting period for a check to clear, for example — or they wish to avoid overdraft charges or monthly account fees.

To the extent lower-income consumers do not have sufficient access to, or information about, financial services, Community Development Financial Institutions (CDFIs) aim to fill this gap. CDFIs, which are certified by the Treasury Department, specifically target households and businesses in low-income communities. (CDFIs are not necessarily the only financial institutions that serve LMI neighborhoods.) There are nearly 100 CDFIs operating in the Richmond Fed's district. A variety of institutions can become CDFIs, including banks, loan funds, venture capital firms, and credit unions.

A credit union is a nonprofit cooperative whose members all share a "common bond," such as where they work or live. Most credit unions are not CDFIs, but they did develop as a way to provide affordable credit to people who might not otherwise have access to credit. (The Federal Credit Union Act of 1934 stated that credit unions existed to provide credit to "people of small means," language that persists in the current version of the law.) Rather than requiring collateral, early credit unions relied on their cooperative structure and the social connections among their members to create incentives for risk monitoring and loan repayment.

As we discuss in this issue of *Econ Focus*, credit unions have evolved significantly since the first one opened in 1908. This evolution has prompted a host of questions about the regulations governing them and how they compete with other depository institutions. These questions are of interest not only to the Fed and other financial regulators, but also to consumers, and we hope you find the article both interesting and informative.

In addition to credit unions, this issue features articles on the efficacy of so-called "sin taxes," the economic and social repercussions of the Spanish flu pandemic of 1918-1919, and the Fed's role in foreign exchange markets, among other topics.

Thank you for reading, and we look forward to hearing from you if you'd like to share your thoughts on these or any other topics. **EF**

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