CAPCO

UNBANKED & UNDERSERVED

LATINX DEMOGRAPHIC CHANGES & CREATING FINANCIAL INCLUSION

DEMOGRAPHIC CHANGES IN THE U.S.

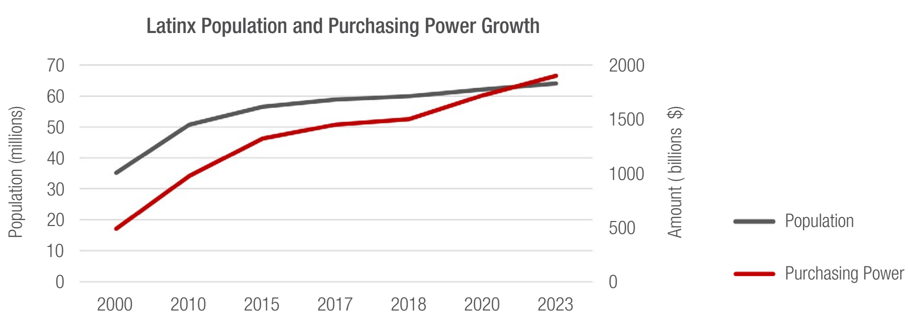
Demographic shifts in the U.S. and the resulting changes in predominant client expectations are affecting the ways FIs are compelled to develop and deliver products and services. A perennial market force, up-and-coming social groups have unquestionably driven the American economic apparatus as seen across historic periods including the Great Wave of Immigration (1880s-1910s), the post-World War II baby boom (1946-1964), and immigration after the 1980s-early 2000s.

According to a 2015 report by the U.S. Census Bureau, by 2044 the U.S. is expected to become a "Majority-Minority"[1] nation. This shift has already materialized noticeably in several states including California, Hawaii, New Mexico, Texas, and the District of Columbia.

The Hispanic[2] community comprises 25 percent of the majority-minority population, a total of 60 million Americans, of which an estimated 32.5 million are millennials and Gen Zers. However, despite these remarkable population growth statistics, **most of the Latinx community is not fully integrated in the financial system,** with large segments being presently unbanked or underbanked.

POPULATION AND PURCHASING POWER HAVE CHANGED

In addition to ballooning population numbers, the Latinx demographic has developed disproportionally more purchasing power[3] and has become **one of the country's most valuable and productive consumer groups.**



source: Pew Research Center and Nielsen

1. Transition at which the non-Hispanic White population comprises less than 50 percent of the nation's total population.
2. Hispanic refers to individuals who speak Spanish. Specifically, it refers to individuals from Spanish-speaking countries of Latin America and Spain and those with Hispanic descent.
3. The amount of money that a person or group has available to buy products and services.

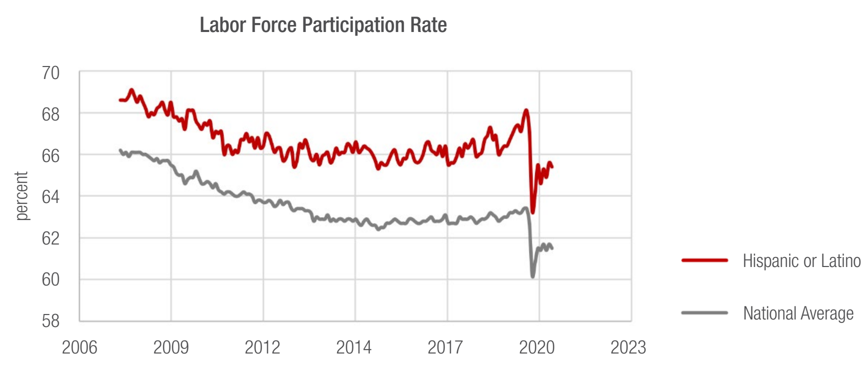
According to a Nielsen report, Latinx buying power rose from $213 billion in 1990 to $1.5 trillion in 2018. By 2023, that number is projected to increase to $1.9 trillion. Notably, the Latinx total real GDP between 2010 and 2018 grew with an annualized average of rate of 3.3%, exceeding the average across several demographic groups by 1.2%. **Indeed, if the U.S Latinx population were their own nation, they would have the world's seventh-largest GDP[4] at $2.13 trillion, adjusted for inflation, behind the U.K. and France.**

Consequently, **Latinxs represent a justified bet upon which we as a country and our financial institutions can lay stake to facilitate our economic growth and prosperity as a nation.** Here we have a target demographic with tremendous purchasing power which has not yet become a primary business focus for banks and FIs in select regions of the United States.

SOCIOECONOMIC ENVIRONMENT

Labor Force Participation

The current and anticipated profile of key marketplace indicators reinforces the need for banks and financial institutions to serve the financial needs of the Latinx demographic. For example, with a labor force participation rate (LFPR) of 68 percent prior to the Covid-19 pandemic, the Hispanic population led the country, in contrast to a 63 percent national average. With such persistent overperformance in this respect, it is doing us a disservice that most of the Latinx community is not heavily involved in the institutional banking system.



source: Pew Research Center and Nielsen

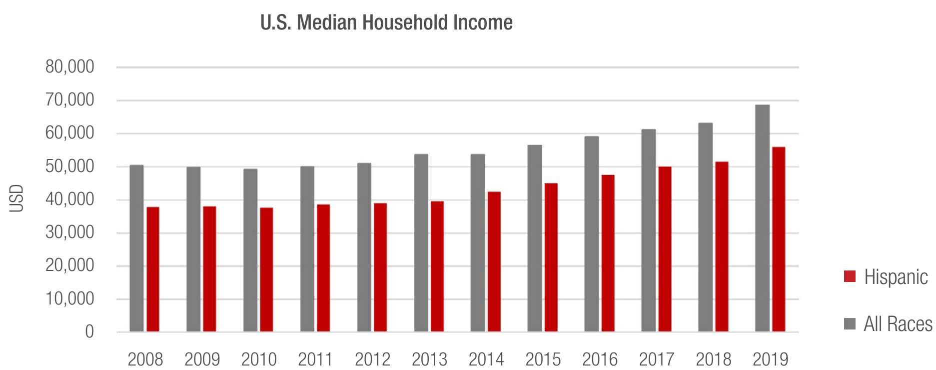
4. The total value of goods and services produced in a country during one year

As it turns out, 10 percent of Hispanic households are unbanked, and 22 percent are underbanked,[5] that cohort relying on higher-cost channels for their financial needs. Products and services obtained outside the banking system are called alternative financial services (AFS) and include money orders, check cashing, international remittances services, payday loans, pawn shop loans, and auto shop loans.

Household Income[6]

With 40 percent of the largest minority demographic beholden to AFS, the usage of AFS means that these households are realizing higher costs and fees, and exorbitant penalty interest rates, stifling socioeconomic advancement and their contribution to economic productivity. Coupled with the plainly expanding economic wherewithal of the community, this statistic magnifies the commercial and community service opportunity at hand to transition members of the Latinx community from unbanked and underbanked to "fully banked."

Hispanic households have seen a steady income increase from $37,913 USD in 2008 to $56,113 USD in 2019, adjusted for inflation. While this is a noteworthy statistic, in the past decade, Hispanic household income continues lagging behind the national average. Challenging common logic, the relative position of Hispanic households in terms of rate of wealth accumulation could be a function of the disadvantage realized by being underbanked, as being "fully banked" opens the door to the power of investment within an array of vehicles including credit, equity markets, real estate, bonds, and other securitized vehicles.



source: Current Population Survey (CPS) Annual Social and Economic (ASEC) Supplement, note: adjusted for inflation

Consumer Trends

On the consumer side, homeownership rates are a leading indicator that communities are capitalizing on opportunities to improve their economic condition. Primarily, there has been a large increase in homeownership rates[7] amongst the Latinx population – reaching a high of 51 percent in Q2 2020, up 4.9 pp from Q2 2019. Homeownership, commonly accepted as the first steppingstone to building wealth, is an indicator towards what is possible when households have access to banking products.

5. Unbanked: no one in the household had a checking or savings account.
6. Household income is the total amount of money earned by all members of a single household. Sources include wages, salaries, investment returns, retirement accounts and welfare payments.
7. The homeownership rate is the proportion of households that is owner-occupied.

Although increasing homeownership rates among the Latinx demographic indicate positive engagement with the institutional financial system, 32 percent of Hispanic households have no mainstream credit (a precursor to homeownership), compared to 14 percent of White households. Likewise, by providing broader and more affordable access to consumer credit we can anticipate a larger proportion of the Latinx community will migrate towards homeownership over time.

However, the first step towards access to credit is understanding how credit scores function. While a portion of Hispanic households may be banked, most may not seek credit until a need arises; there is a need for improved education surrounding the value of creating a credit profile and the role of credit as a key enabler to financial well-being.

Additionally, for those with a credit line, research shows the Latinx demographic is eager to improve their credit scores, with Latinx millennials leading the way. According, to insights from Chase Slate 2016 Credit Outlook:

- 54 percent of Hispanics checked their credit scores
- 78 percent of Hispanic millennials want to improve their credit scores

Millennials are an avenue to actuate change amongst older portions of the Hispanic population. Indeed, in multi-generational households engrained reservation and historical disenfranchisement with the institutional banking spectrum can and has hindered full participation.

Lastly, we cap our market perspective by touching briefly on the savings rate among Latinx households. The savings rate among Hispanic households increased from 48 percent in 2017 to 54 percent in 2019; and although savings account ownership rates are lower among Hispanic households, this could mean they save within informal banking vehicles. For example, informal saving practices, such as community lending circles, are common among the Latinx demographic, however, such practices, of course do not factor into one's credit score history. Nonetheless, objective data illustrates that these practices demonstrate values aligned with financial responsibility.

Undoubtedly, there is ample opportunity for the banking sector to empower the demographic to enjoy the benefits of participating in the mainstream financial environment. Importantly, we see clear evidence that Latinx households have demonstrated they know how to manage their money. We can see this in the positive socioeconomic trends that will only compound as the demographic grows and is supported by cultural awareness within the U.S.

To address the Latinx demographic's hesitation, banks need to understand the group's diverse makeup in terms of generational behaviours, household models, household status, years since immigration to the U.S., and employment characterization to open doors to transition the group into the institutional banking system. To accelerate this, banks and financial institutions must thoughtfully design products, services, and experiences that are targeted and compelling across individuals and households in their journey toward the American Dream.

HOW CAN BANKS PREPARE FOR FUTURE DEMOGRAPHIC CHANGES?

Banks must consider the design and development of their products and services and ultimately rethink their distribution channel strategies with an emphasis on a multi-channel engagement and compelling digital products to transform the Latinx perception and bespoke servicing of institutional banks.

a) Innovate

Tailor the customer experience, both in-person and digitally, uniquely for the Latinx demographic. According to a FDIC 2019 report, minority households were less likely to visit a branch; reasons for this may include the following: feeling out of place, confused, and not seen amidst a busy crowded space, or perhaps not having a local branch in their neighborhood.

For this, banks must have well-kept spaces, and hire bilingual bankers who can meet the needs of the customer and reduce the chance of miscommunication. Digitally, FIs must think about ways to use AI to better align customized products and services in geographies where Latinx demographics are more prevalent. The Latinx demographic is not homogenous, therefore increased use of AI capabilities to identify second-level personalization opportunities and potential product solutions is critical.

b) Educate

To increase market exposure and raise awareness around products and services, especially amongst millennial and Gen Z customers, banks may consider deploying targeted ads and cultivating key local community partnerships. This bi-directional engagement will foster cultural awareness for banks and increase client engagement from the Latinx community. For example, community centers are important resources often organized and relied upon by this group. Banks may seek to build relationships with community organizations to better understand each local Latinx population's needs to foster customer confidence. Banks may also consider sponsoring workshops and "Get to Know the Bank" information sessions.

Part of transitioning the unbanked and underbanked to **"fully banked"** means communicating the advantages of utilizing deposit accounts in lieu of AFS and how credit scores work, and creating exposure to credit card programs. This paves the way for growing simple deposit relationships into investment products, mortgages, and business services; driving improved outcomes for both community members and FIs. Ultimately, having a banking relationship and access to various financial products through a trusted partner will support clients' overall financial security in auspicious circumstances and in times of uncertainty and unforeseen environmental forces.

c) Create

To capitalize on the current low-interest-rate environment, banks should consider tailoring entry-level credit products for the Latinx demographic. Citing the previous section, we have highlighted how segments of the Latinx demographic already display high levels of financial responsibility, accordingly, from a risk and cost control perspective banks may consider both offering secure and non-secured lines of credit to facilitate fair and supportive lending within Latinx markets across the U.S.

Unbanked and underserved populations are especially targeted in predatory lending schemes. Predatory lending schemes can include penalty interest rates, high late fees, and repossession of loan collateral. Opening affordable lines of credit will both address unmet borrower demand and transition the subset of people that invest with informal community-based lending circles or AFS, such as payday loans.

d) Elevate

Continue establishing employment pipeline opportunities that expose Latinx candidates to career opportunities and create a sense of partnership and recruit within the community; this shows that institutions see the value of Latinx representation within the workforce. Additionally, it is not enough to focus on recruitment. Leadership development and retention are equally important. A focus on amplifying, training, and coaching current Latinx and BIPOC (Black, Indigenous, People of Color) talent to increase diversity within the financial services' sector can also continue fostering financial inclusion.

OUTLOOK: MARKETPLACE OPPORTUNITY

The Latinx demographic's financial health is essential for the future economy. The majority of banks and financial institutions have not embraced a demographic market focus and should incorporate a demographic-lens into their product and service go-to-market strategies. While there may be concern and uncertainty present among financial institutions on how to approach demographic changes, banks must recognize that distribution channel strategies, the development of new products and services, and outreach can occur across the horizon. Each banks' journey will be different dependent on their size and growth; however, at the forefront financial institutions should focus on **intentionality, consistency, and compelling products.**

Trust, confidence, and respect from demographic bases will follow. This paper provides a framework that can be used with more segmented BIPOC groups for cross-selling and expansion opportunities. In alignment with FIs' current policies and mission statements, taking steps towards an inclusive financial atmosphere will provide **reputational opportunity, wide community exposure, and credibility.**

The Latin meaning of economics, oeconomica, is "how to build a home" – the Latinx community has mastered economics with the informal and formal banking financial vehicles they **trust,** however much needs to be done to facilitate the full transition of the Latinx demographic from unbanked and underbanked to **"fully banked."**

SOURCES

1. Colby, S.L., & Ortman J.M. (2015). Projections of the Size and Composition of the U.S. Population: 2014 to 2060. Census.gov. Retrieved from: https://www.census.gov/newsroom/press-releases/2015/cb15-tps16.html

2. Dettling, Lisa J., Joanne W. Hsu, Lindsay Jacobs, Kevin B. Moore, and Jeffrey P. Thompson (2017). "Recent Trends in Wealth-Holding by Race and Ethnicity: Evidence from the Survey of Consumer Finances," FEDS Notes. Washington: Board of Governors of the Federal Reserve System, September 27, 2017, https://doi.org/10.17016/2380-7172.2083

3. Devine. J. & Ortman J.M. (2014). Nation to Become a Plurality, but Some Areas Already Are. Census.gov. Retrieved from: https://www.census.gov/newsroom/blogs/random-samplings/2014/06/nation-to-become-a-plurality-but-some-areas-already-are.html

4. Federal Deposit Insurance Corporation (FDIC). (2019). How America Banks: Household Use of Banking and Financial Services. FDIC EconomicInclusion.gov. Retrieved from: fdic.gov/analysis/household-survey/index.html

5. Federal Reserve System. (2019). Report on the Economic Well-Being of U.S. Households in 2019 - May 2020. Board of Governors of the Federal Reserve System. Retrieved from: https://www.federalreserve.gov/publications/2020-economic-well-being-of-us-households-in-2019-banking-and-credit.htm

6. Flores, A. & Noe-Bustamante, L. (2019). Facts on Latinos in the U.S. Pew Research Center. Retrieved from: https://www.pewresearch.org/hispanic/fact-sheet/latinos-in-the-u-s-fact-sheet/

7. Fry, R. & Parker, K. (2018). Early Benchmarks Show 'Post-millennials' on Track to Be Most Diverse, Best-Educated Generation Yet. Pew Research Center. Retrieved from: https://www.pewsocialtrends.org/2018/11/15/early-benchmarks-show-post-millennials-on-track-to-be-most-diverse-best-educated-generation-yet/

8. Nielsen. (2019). La Oportunidad Latinx: Cultural Currency and The Consumer Journey. Nielsen. Retrieved from: https://www.nielsen.com/wp-content/uploads/sites/3/2019/09/nielsen-2019-latinx-DIS-report.pdf

9. Meara, B. (2018). Delivering Excellent Customer Service Part 2: Why Digital Engagement Will No Longer Be Optional. Celent. Print.

10. Melancon, J.M (2021). Consumer buying power is more diverse than ever. UGA Today. Retrieved from: https://news.uga.edu/selig-multicultural-economy-report-2021/

11. Meraji, S.M. (2014). Lending Circles Help Latinas Pay Bills And Invest. WAMC, NPR. Retrieved from: https://www.wamc.org/post/lending-circles-help-latinas-pay-bills-and-invest

12. Patten, E. (2016). The Nation's Latino Population Is Defined by Its Youth. Pew Research Center. Retrieved from: https://www.pewresearch.org/hispanic/2016/04/20/the-nations-latino-population-is-defined-by-its-youth/

AUTHOR

Maleni Palacios, Associate
maleni.palaciosdelgado@capco.com

ABOUT CAPCO

Capco, a Wipro company, is a global technology and management consultancy specializing in driving digital transformation in the financial services industry. With a growing client portfolio comprising of over 100 global organizations, Capco operates at the intersection of business and technology by combining innovative thinking with unrivalled industry knowledge to deliver end-to-end data-driven solutions and fast-track digital initiatives for banking and payments, capital markets, wealth and asset management, insurance, and the energy sector. Capco's cutting-edge ingenuity is brought to life through its Innovation Labs and award-winning Be Yourself At Work culture and diverse talent.

To learn more, visit www.capco.com or follow us on Twitter, Facebook, YouTube, LinkedIn Instagram, and Xing.

WORLDWIDE OFFICES

APAC
Bangalore
Bangkok
Gurgaon
Hong Kong
Kuala Lumpur
Mumbai
Pune
Singapore

EUROPE
Berlin
Bratislava
Brussels
Dusseldorf
Edinburgh
Frankfurt
Geneva
London
Munich
Paris
Vienna
Warsaw
Zurich

NORTH AMERICA
Charlotte
Chicago
Dallas
Hartford
Houston
New York
Orlando
Toronto
Tysons Corner
Washington, DC

SOUTH AMERICA
São Paulo

WWW.CAPCO.COM

CAPCO
a wipro company

JN_3583