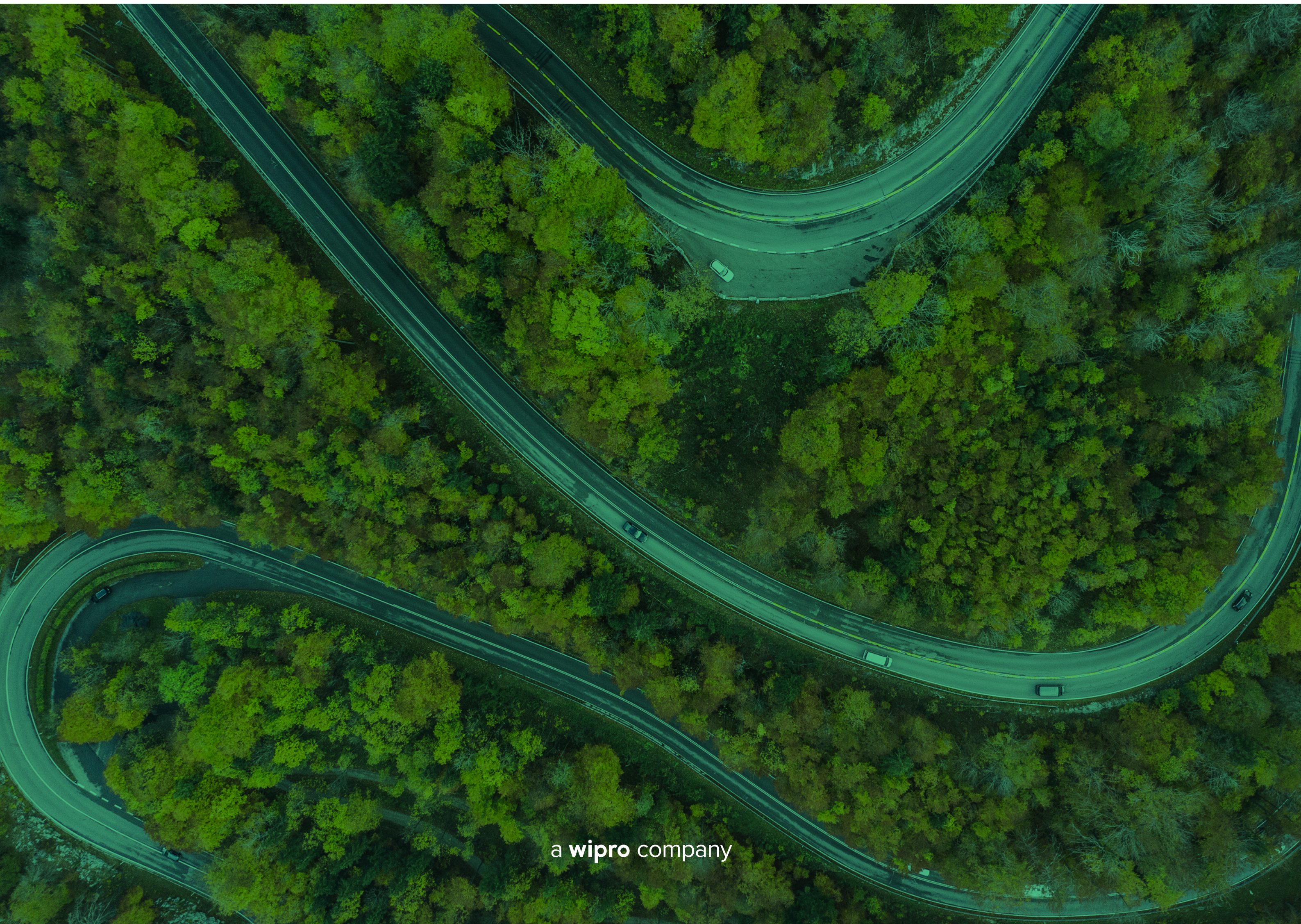
CAPCO

BANKING FOR THE GREATER GOOD



A LOOK AT THE UNBANKED AND UNDERBANKED (U-U) WHILE SUPPORTING ESG

As of 2021, 13% of adults are underbanked, while 6% are unbanked.[1] The unbanked are those where no one in a household has access to a checking or saving account.[1] The underbanked includes households which may have a checking and/or savings account but go outside of the bank for other financial services, such as money orders, check cashing and payday loans.[2]

Examination of the socio-economic backgrounds of the U-U community shows that those in the Black community, as well as the Hispanic community, fall into the U-U Community, between two to four times more frequently than their white counterparts (Figure 1). However, this should not be interpreted as a lack of need for financial services. An overwhelming majority, close to 88% of the U-U population, use alternative financial services like pawn shop and auto title loan for transaction activity, such as check cashing or money order. Similarly, 29% turn to alternative financial services for borrowing activity.[1]

Additionally, and not surprisingly, income and education also play key roles when looking at the placement of minorities in finance.

Minorities make up the overwhelming majority of the U-U Community, largely due to their lack of education and/or assets lend itself to minorities being in the U-U Community. The numbers are in front of us, so the question then is, "what can financial institutions do to address this apparent social disparity?"

Figure 1 Socio-Economic Disparities of the U-U Community[1]

CHARACTERISTICS	UNBANKED	UNDERBANKED	FULLY BANKED
FAMILY INCOME			
Less than $40,000	14	23	63
$40,000 - $100,000	1	16	83
Greater than $100,000	*	6	94
EDUCATION			
High school degree or less	12	21	67
Some college/technical or associate degree	3	17	79
Bachelor's degree or more	1	9	90
RACE/ETHNICITY			
White	3	11	86
Black	14	32	54
Hispanic	10	22	68
OVERALL	6	16	79

OVERCOMING HISTORICAL EXCLUSION

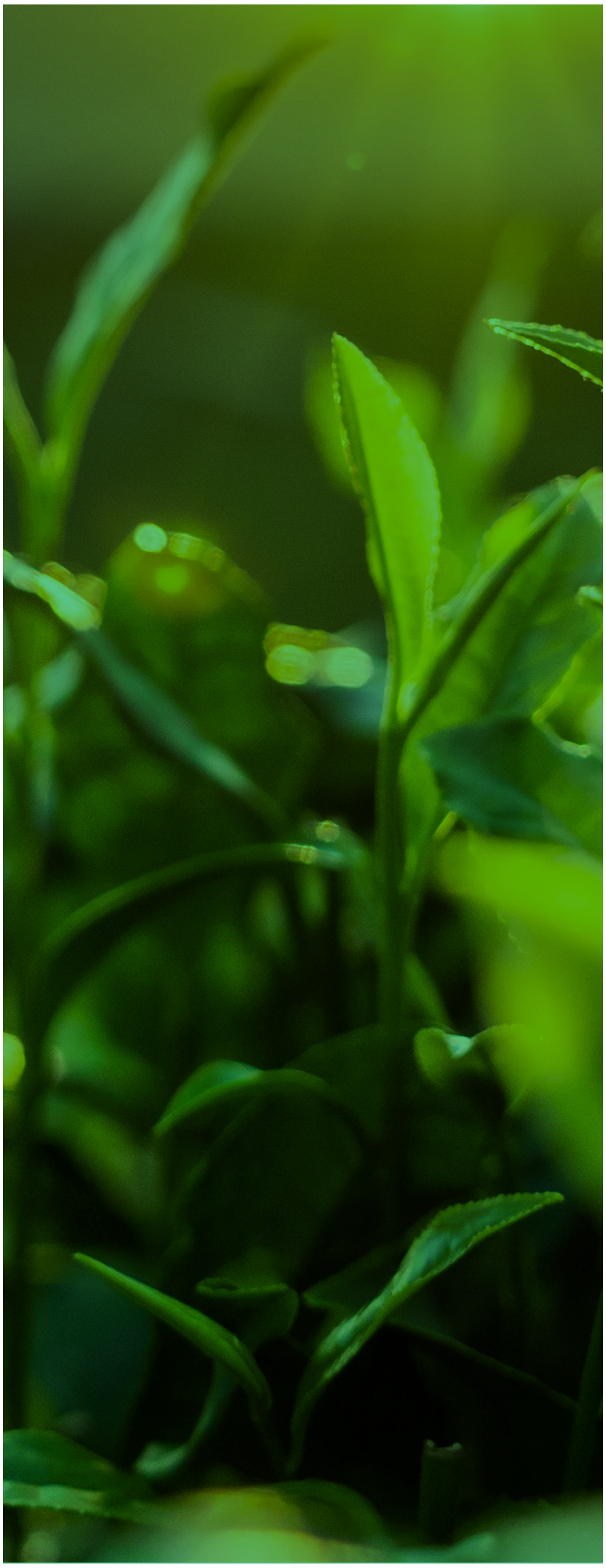
Although the U-U population remains relatively high, the percentage has been steadily decreasing. Since 2015, there has been a 7% decrease in the underbanked population. Yet, in the same period, there has only been a 2% increase in the share of U.S. adults who open a bank account.[1] While the trends suggest that financial inclusion has not necessarily improved significantly during this time, it does indicate that the U-U population is open to trying new financial services.

In considering why the increase in bank accounts over the past five years does not align with the decrease in the underbanked community, it is important to understand historical factors that have contributed to the persistence of a U-U population. Most notably, of course, are exclusionary and discriminatory practices that trace back decades, even centuries, in the United States. Although, the government has worked hard to ensure fair practices through different legislative acts, subtle manifestations continue to exist, often driven by lack of access and education and access.

Traditional financial institutions are up to four times less likely to open branches in predominantly non-white communities, due to perceived increased risks. This negatively affects these communities, geographically excluding them from accessing traditional financial services and forces them to rely on alternative financial services.[3] This lack of access also contributes to a generational absence of knowledge of these services, as well as fuels uncertainty and distrust.

However, it is possible for financial institutions to become more accessible to these communities. In September 2020, JP Morgan Chase opened a Chase branch in the Cherry Hill neighborhood of South Baltimore, becoming the first national bank to open in this historically Black community.[4] With the promise of providing full bank services and offering educational seminars with community partners and local business owners to the neighborhood, this opening reinvigorated and brought dignity to the community.

Not only is providing financial services to the U-U population a worthy cause which would lead to increasing financial inclusion, but it can also serve to motivate communities and stimulate economic activity through this newfound access to traditional financial services.



BRINGING ESG INTO THE FOLD

ESG is becoming increasingly important for financial institutions and requires explicit articulation and promotion. Now, more than before, investors, consumers and employees are increasing their awareness of ESG behaviours and considering those factors in their decision-making processes.[5]

The U-U market offers a good opportunity for financial institutions to showcase their commitment to ESG. Financial institutions, specifically banks, are best positioned to help address the needs of minorities in the U-U community and ultimately help reduce the U-U population.

Financial institutions are ideally positioned to take on the U-U market as an ESG initiative and drive meaningful social impact. As the providers of traditional financial services, they hold the knowledge and capital to be able to bring the U-U population to be fully banked and help them make secure financial decisions to promote the financial health of themselves and their communities.

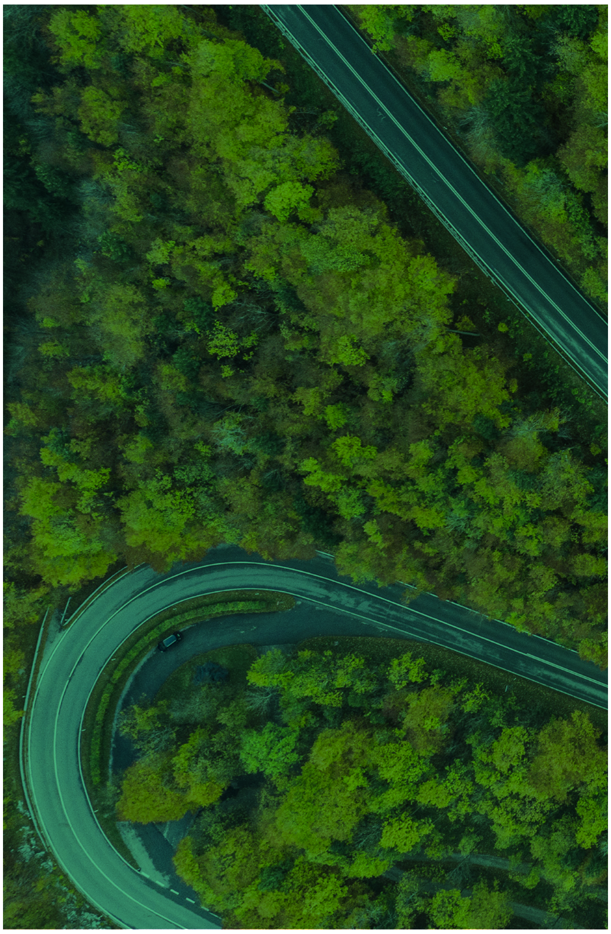
POTENTIAL ESG-DRIVEN BENEFITS:

- Investors are investing a lot of capital in corporations that govern and operate in a sustainable manner, with sustainable investing growing at double digit rates.[5]
- In an analysis of over 2,000 studies, McKinsey discovered that ESG propositions overall had a positive impact on equity concerns 63% of the time.[6]
- According to a recent Voya survey, 42% of respondents said that they will more than likely to stay with an employer who applies ESG principles to workplace benefits.[7]

A FEW WAYS IN WHICH FINANCIAL INSTITUTIONS CAN ADDRESS THIS MARKET ARE:

1. Open branches in these communities to increase accessibility to traditional financial services, raise brand awareness, and build a presence.
2. Design products tailored for the U-U community Understand behaviours and constraints of the community to design products tailored for their needs.
3. Offer educational programming to answer questions and educate the community on services available, financial health, and benefits. Education can be tailored by age group or need to cover all stages of an individual's financial journey.
4. Partner with community leaders to understand ways to best serve the community, invest in it, and help ease distrust and skepticism.

Other mechanisms to serve the U-U population are typically through technology and digital banking. These avenues could grant financial institutions access to this demographic at a lower cost of entry, while still providing this cohort the resources they need to enter the traditional financial environment and reduce their dependence on alternative financial services.



CONCLUSION

In an environment where ESG is becoming more critical to the reputation and success of an organization, it is important for financial institutions to align themselves with causes where they can have a real effect for the "greater good." The U-U segment offers a good opportunity for financial institutions do just that and demonstrate their support and commitment to ESG.

As the subject matter experts, financial institutions can help the U-U population gain access to financial services in a secure way and even provide educational resources to promote healthy financial decisions. There is opportunity for financial institutions to tailor investment in this space based on their risk tolerance, ranging from opening a branch to leveraging community outreach channels to start a dialogue with the U-U population. And the rewards are substantial – while engaging with this segment, financial institutions are playing an active role in closing the racial wealth gap, improving financial equity, and of course, reducing financial exclusion.

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