



The Impact of CRA Agreements



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What is a CRA Agreement?

- A pledge by a lending institution to increase the level of financial services
 - Financial services are targeted to a particular population and/or geographic area



What is in a CRA Agreement?

- Types of agreements
 - Unilateral or multilateral
- Types of lending
 - Mortgages
 - Small business
 - Consumer
 - Agricultural
 - Community development
- Other forms of support
 - Lower interest rates
 - Loan size
 - Loan counseling
 - Technical support
- Loan review committees
- Increase banking services
 - Branches
 - Products
 - Staffing
- Outreach



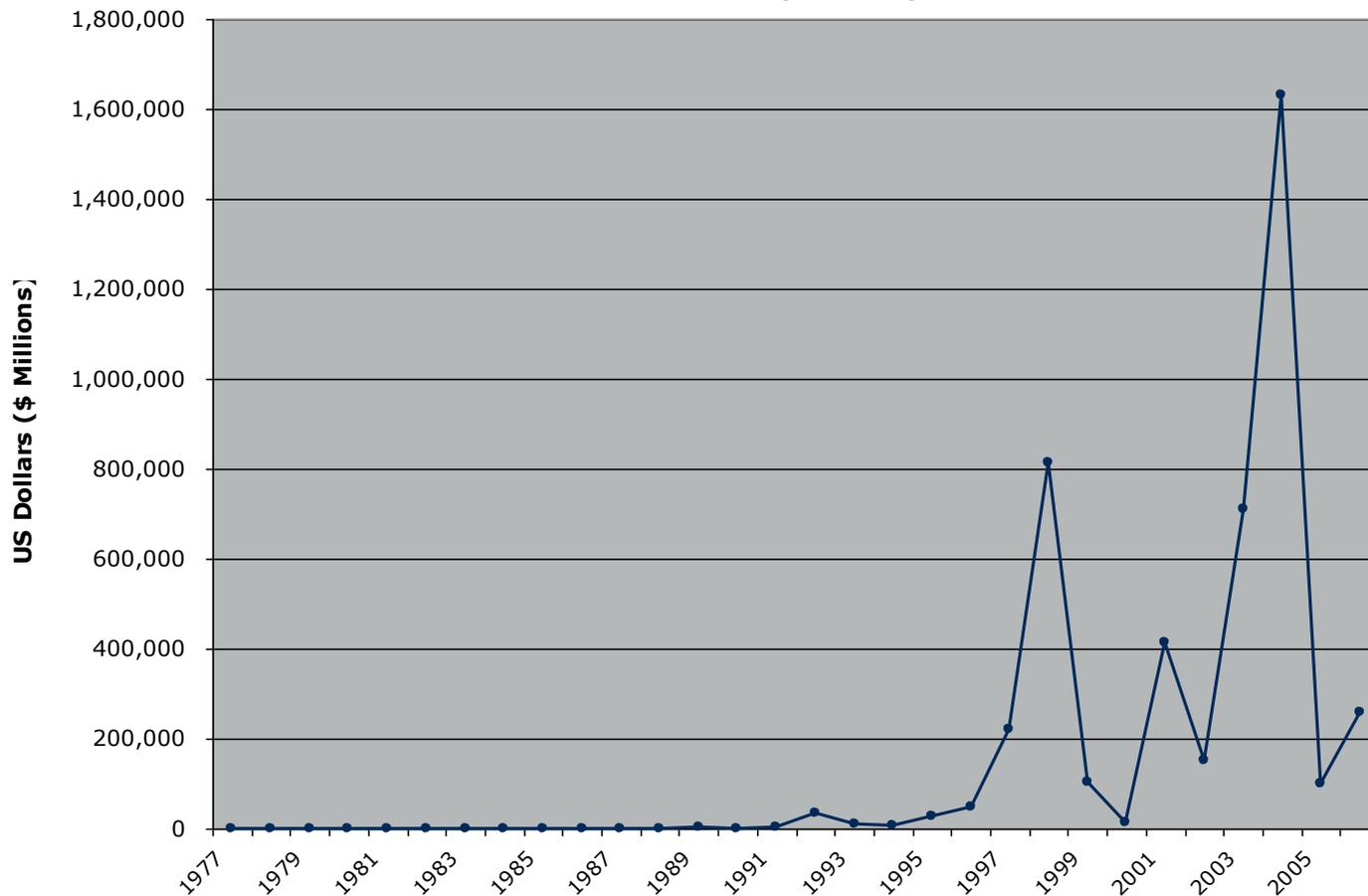
CRA Agreement Facts

- Consolidation in the banking industry in the 1990s helped facilitate the growth in CRA agreements
 - There have been over 446 CRA agreements
 - Over \$4.5 trillion in total lending
- The structure of CRA agreements has changed as lenders have become larger in size
 - Increased use of voluntary or unilateral agreements
 - Increased use of multi state agreements for tens or hundreds of billions of dollars
 - Problem:
 - No enforcement mechanism to ensure compliance with CRA agreement pledges
 - Community groups must have the ability to monitor CRA agreements in order to ensure success



Annual Dollar Amount of CRA Commitments

Annual CRA Commitments
US Dollars (\$ Millions)

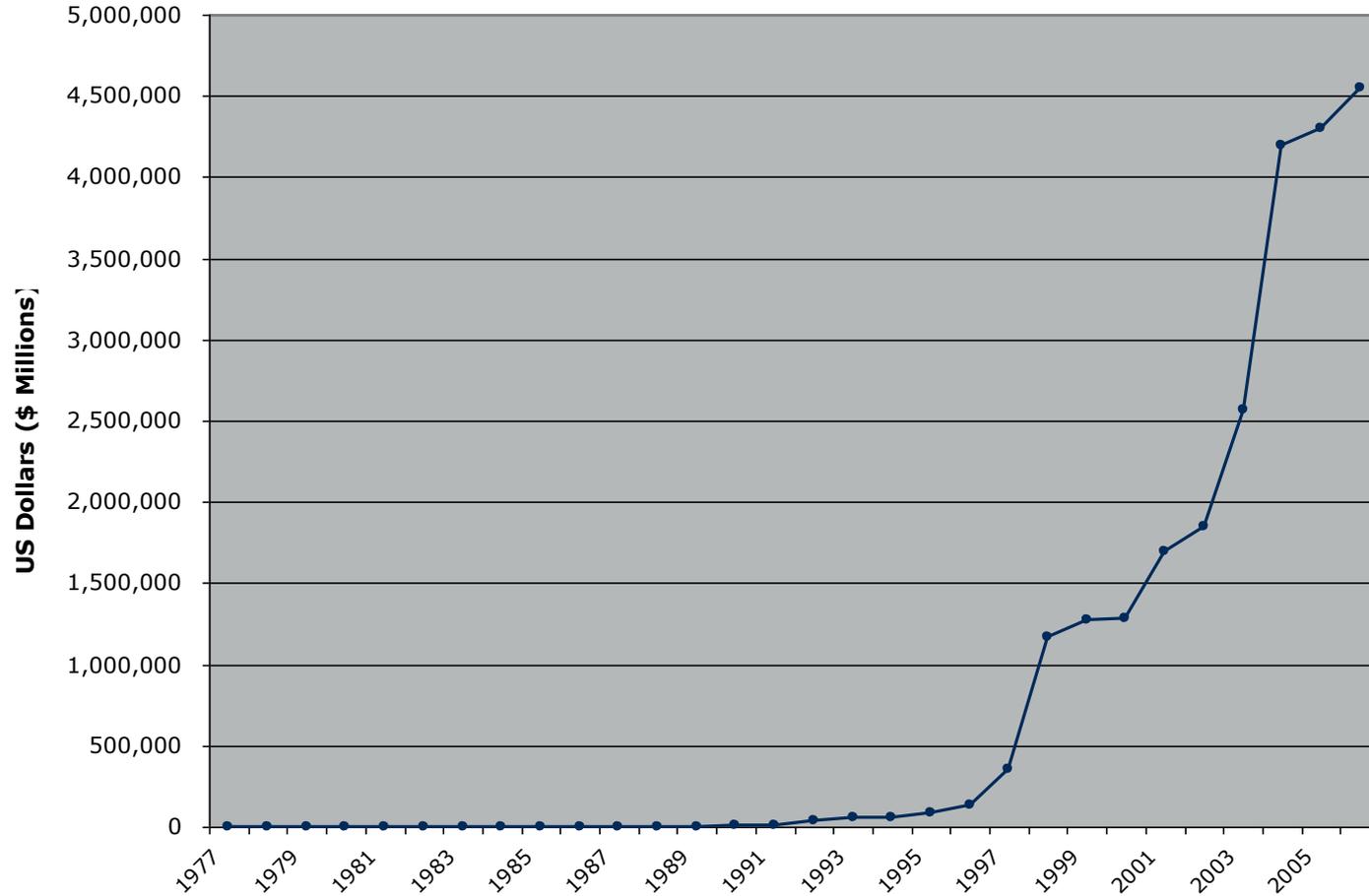


Source: National Community Reinvestment Corporation



Total Dollar Amount of CRA Agreements

Total CRA Commitments
US Dollars (\$ Millions)



Source: National Community Reinvestment Corporation

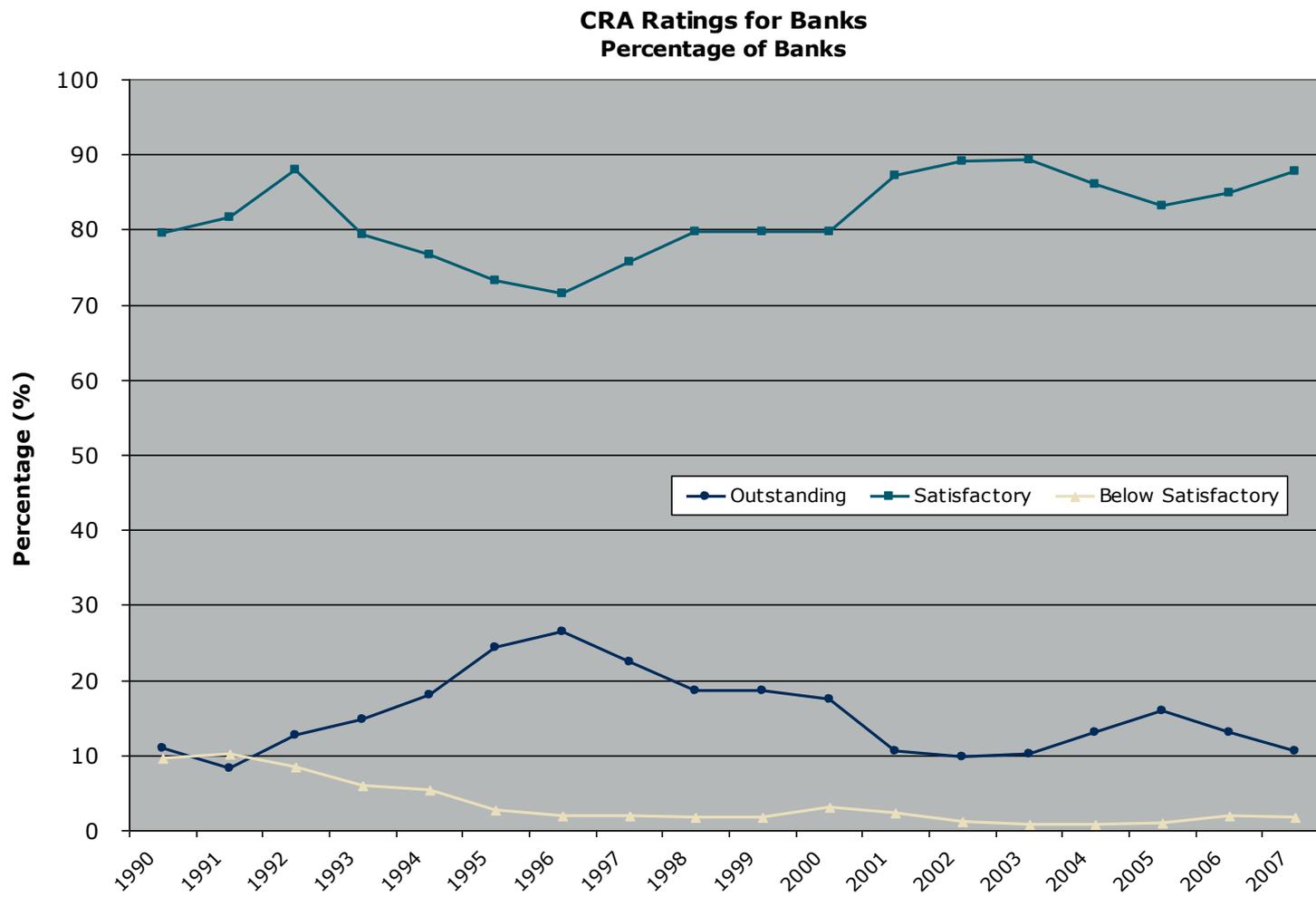


CRA and CRA Agreements

- CRA impacts banks primarily in two ways:
 - CRA ratings are a numerical evaluation of how well a bank is meeting the financial service needs of its community
 - Public release of CRA ratings
 - Public pressure on poorly rated banks
- Regulators must consider CRA ratings when reviewing applications for mergers, acquisitions and branching
 - Poor CRA performance may encourage community groups to protest merger application
 - Merger can be delayed or blocked
 - Delays could lead to a rival bidder
 - Increase cost of merger



CRA Ratings For Banks



Source: National Community Reinvestment Corporation



Should CRA Agreements Impact Lending?

- If markets are imperfect or market failure:
 - CRA agreements should lead to an increase in the number and dollar amount of loans
 - More innovative products
 - Accessing new markets
 - Insurance
 - Known cost (CRA agreement) vs. unknown cost (CRA protest)
- If markets are perfect:
 - CRA agreements should not lead to an increase in the number or dollar amount of loans
 - All loans that are profitable should be originated
 - Loans could be redistributed among the lenders within the market



Should CRA Agreements Impact Lending?

- How about lending institutions that do not initiate CRA agreements?
 - CRA agreements may cause other lenders to:
 - Reduce the number of loans originated
 - Lenders get pushed out by larger lenders
 - Originate the same number of loans
 - Lenders may be able to maintain market share, but get pushed into a riskier segment of the market
 - Originate more loans
 - Identify new markets
 - Create new products



What Does The Research Say?

- CRA Agreements may lead to positive outcomes
 - Lenders that enter into CRA Agreements originate more mortgages and small business loans during the time period the agreement is active and after the agreement has expired
 - Institutions that initiate CRA agreements increase mortgage lending activity within their service area, but not outside their service area
 - CRA agreements can be structured to increase the probability that increases in financial services are more likely to occur
 - Stock price for merging banks do not respond to CRA protests around a merger announcement
 - Policy Implications:
 - Mortgages and small business loans are profitable
 - Market inefficiencies may exist in mortgage and small business markets
 - CRA protests do not represent a significant cost to merging institutions



What Does The Research Say?

- CRA Agreements may lead to negative outcomes:
 - CRA agreements do not cause a significant increase in small business lending in the communities where the agreements are active
 - In communities where CRA agreements are active, mortgage lending tends to increase, but the increase in lending does not persist
 - In communities where CRA agreements are active, community banks originate fewer mortgages overall, but maintain their share of CRA and minority mortgages originated
- Policy Implications:
 - The market for small business loans may be efficient
 - Small business loans have unique characteristics such that information generated from one loan is not easily transferable to other small business loans
 - CRA agreements may be a form of insurance to protect lenders against a poor CRA rating or CRA protests
 - Increased competition from larger lenders force out smaller lenders that are tied to the community



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