

Home Biased Credit Allocations

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- **Bank credit** particularly important.
 - Family settlement, entrepreneurship, investments, job opportunities, innovation, emotional well-being, society orders etc.

"We are proud to make life better for *everyone*."

Anonymous Bank A

"...we are committed to serve every community under our network."

Anonymous Bank B

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⇒ **Our paper:** A systematic CEO "home bias" in credit allocation policies within banks. This has real effects on the local economy.

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- Bottom-line: Counties with a greater exposure to hometown favoritism enjoy better economic developments. Evidence of credit inequality.

⇒ Hometown bias not only matters for investment decisions (Coval & Moskowitz, 1999). Home bias affects a firm's internal business strategy & production outputs (bank credits). Real effects on the economy

- Hand-collected CEO's birth data (county-level)
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- Mortgage loans: Home Mortgage Disclosure Act (HMDA)
 - Borrower's location information
 - Borrower (race, age, sex, income) & loan (purpose, type, amount)
 - Collapsed to bank-county-year level
 - Both accepted & rejected applications
- Others: FR Y-9C forms, SOD database, BoardEx, US Census Bureau

Empirical strategy: Summary

$$\begin{aligned} \text{Outcomes}_{ikt} = & \alpha + \beta_1 \text{Ln}(\text{dist hometown})_{ikt} + \beta_2 \text{Ln}(\text{dist HQ})_{ikt} \\ & + \text{Controls}_{ikt} + \text{Fixed effects} + \varepsilon_{ikt} \end{aligned} \quad (1)$$

- **Prediction:** Banks (a) lend more; (b) open more branches in counties near its CEO's hometown compared to counties further away.
- β_1 compares lending
 - of the same bank (=bank FE)
 - between **close vs. far** counties from CEO's birth county
 - holding local economic conditions, credit demand etc. constant (=county-year FE)

Empirical strategy: Illustration

- Mr. James E Rohr, CEO of PNC Financial Services 5/2000-4/2013



Empirical strategy: Illustration



Empirical strategy: Illustration



Empirical strategy: Illustration



Empirical strategy: Illustration

- William S Demchak replaces James Rohr as PNC CEO in 4/2013



Empirical strategy: Illustration



Lending, branching, & proximity to CEO hometown

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	(1)	(2)	(3)	(4)
Dependent variables:	<i>Ln(originated loan)</i>	<i>Loan growth</i>	<i>Approval rate</i>	<i>Branch growth</i>
Ln(dist home)	-0.244*** (-44.609)	-0.012*** (-15.228)	-0.017*** (-29.227)	-0.028*** (-20.898)
Ln(dist HQ)	-0.924*** (-166.693)	-0.028*** (-41.161)	-0.029*** (-55.481)	-0.175*** (-119.975)
Control variables	Yes	Yes	Yes	Yes
County-Year FE	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes

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- 1 sd. closer to CEO hometown (1200 km): 8% higher mortgage approval rates.

How do CEOs influence local mortgage lending?

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 - 2 Convey 'lending preferences' to local branch managers.
 - 3 Hire acquaintances as branch managers.
- As a test to demonstrate a CEO's influence on local lending: Changes in bank lending in response to natural disaster event.
 - **Intuition:** CEOs need to decide whether to reallocate credits to 'assist' areas affected by disasters.
 - **Hypothesis:** More likely to help if their own hometown is affected.

CEO's influence on local mortgage lending

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Dependent variables:	<i>Ln(originated loan)</i>	<i>Loan growth</i>	<i>Approval rate</i>	<i>Branch growth</i>
Disaster Severity*Ln(dist home)	-0.866*** (-2.134)	-0.158*** (-2.555)	-0.080** (-2.020)	-0.0205** (-2.213)
Ln(dist home)	-0.242*** (-43.773)	-0.011*** (-14.646)	-0.017*** (-28.720)	-0.028*** (-20.388)
Control variables	Yes	Yes	Yes	Yes
County-Year FE	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes

- A greater increase in bank lending in response to natural disasters that occur closer to the CEO's hometown.

Underlying economic explanations

- **Information advantages**

Proximity to hometown \uparrow

\implies Information access \uparrow (Coval & Moskowitz, 2001)

\implies Lending \uparrow (Agarwal & Hauswald, 2010)

\implies If true, **superior** bank outcomes.

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Hometown lending is the result of CEOs seeking private gains (e.g., local directorships) at the expense of shareholders.
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- **Hometown attachment**

Hometown proximity \uparrow
 \implies Emotional attachment \uparrow (Hernandez et al, 2007)
 \implies Invest time & resources (e.g., lending) (Manzo & Perkins, 2006)
 \implies If true, **no effect** on bank outcomes.

Performance analysis

- Hometown lending does **not** explain a bank's: (a) total lending, (b) bad loans, (c) ROA, (d) Stock returns
- Information advantage/agency unlikely

	(1)	(2)	(3)	(4)
Dependent variables:	<i>Loans/Assets</i>	<i>%bad loans</i>	<i>ROA</i>	<i>Stock returns</i>
% mortgage lending birth state	0.009 (0.960)	-0.001 (-1.180)	-0.015 (-0.158)	-0.010 (-0.171)
Bank controls	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

Additional results

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 - CEOs whose cultural heritage places a greater emphasis on selflessness, collectivism, & patriotism \implies more willing to 'help'
 - Traditionally 'marginalized' mortgage applicants: non-white, female, & poor

\implies Emotional attachments to hometown (Hernandez et al. 2007) \implies Little help to the communities

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- County-level analysis.
 - **Prediction:** Counties with a greater exposure to favoritism would enjoy greater economic developments
 - Exposure = fraction of branches located within 400 km (25th) from the bank's CEO birthplace

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 - **Prediction:** Counties with a greater exposure to favoritism would enjoy greater economic developments
 - Exposure = fraction of branches located within 400 km (25th) from the bank's CEO birthplace
- Key advantage: A county's aggregate exposure to home favoritism is plausibly exogenous
 - Banks do not appoint a candidate for CEO position *because of* economic conditions in the candidate's birthplace

Home favoritism & local economic developments

- Counties with greater exposure to favoritism: 5% higher income per capita and 3.1% unemployment rate

	(1)	(2)
Dependent variables:	<i>Ln(Income per capita)</i>	<i>Unemployment</i>
Home favoritism exposure _{t-1}	0.016*** (3.542)	-0.268*** (-4.224)
HQ favoritism exposure _{t-1}	0.016*** (3.039)	-0.193*** (-2.539)
Location controls	Yes	Yes
County FE	Yes	Yes
Year FE	Yes	Yes

Thank you.