COMMUNITY BANKS AND SMALL BUSINESSES: SHARED DESTINIES

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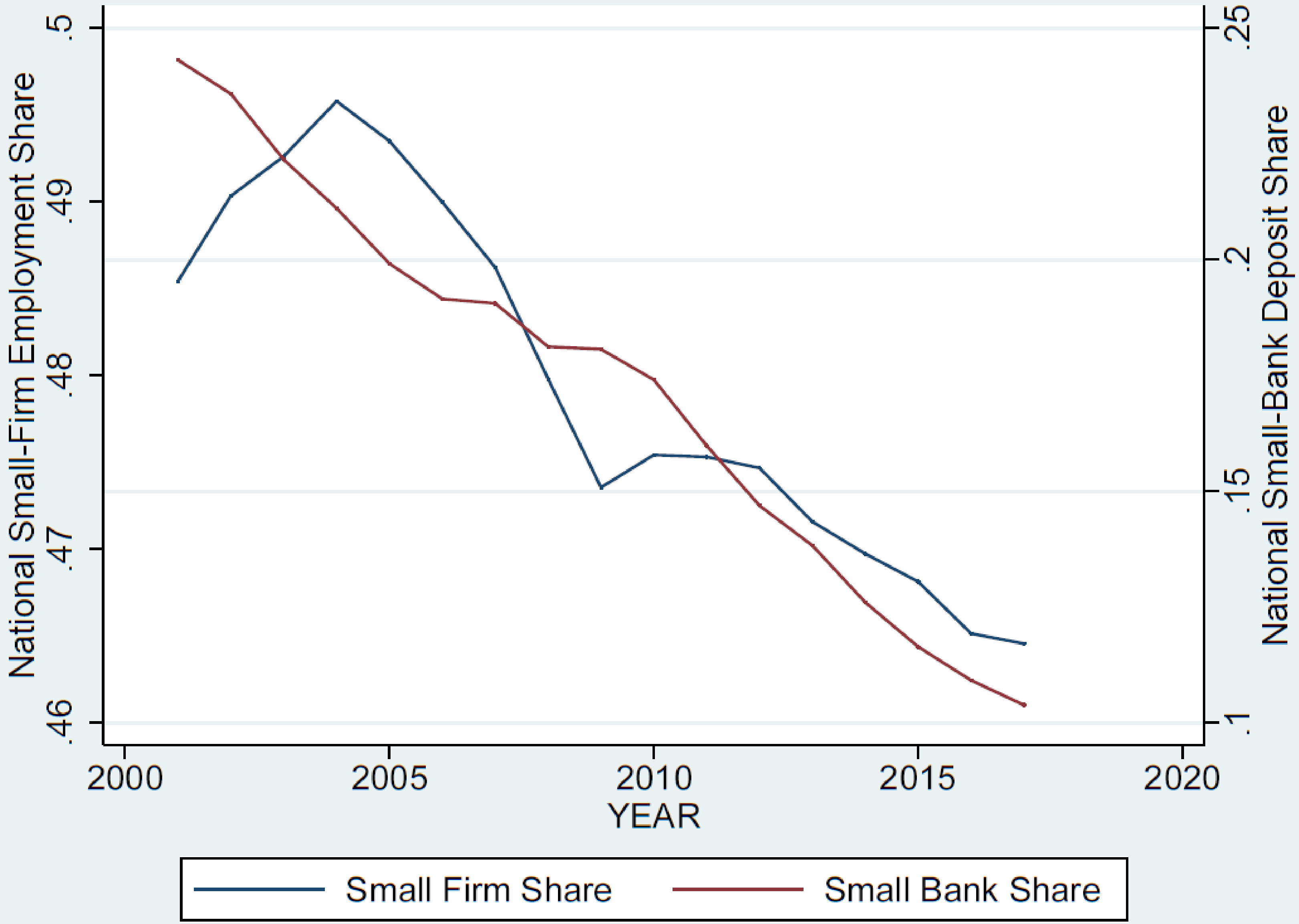
Research and Policy Conference

REFLECTIONS ON

- "Shared Destinies? Small Banks and Small Business Consolidation"
  - By Claire Brennecke, Stefan Jacewitz, and Jonathan Pogach

- "Bank Entrepreneurs"
  - By Kristoph Kleiner, Manju Puri, and Chiwon Yom

SHARED DESTINIES



"SHARED DESTINIES? SMALL BANKS AND SMALL BUSINESS CONSOLIDATION"

- Consolidation in the non-financial industry <u>causes</u> consolidation in the banking industry.

- For every 1% decline in small firms' employment growth, community banks see:
  - 0.8%–1.2% decline in deposits.
  - 1.5%– 2.1% percent decline in small business lending.

- Yet the growth in employment at small firms does not affect large banks' deposits or lending.

DEBATE IN ACADEMIA

- **The demise of community banks contributes to the demise of small businesses.**
  - E.g., Cettorelli and Strahan (2006): The acquisition of smaller banks leads to changes in lending practices and adversely affects smaller firms.
- VS
- **Conglomeration in the non-financial industry erodes the financial stability of community banks and contributes to conglomeration in the banking sector.**
  - Pogach and coauthors.

POLICY IMPLICATIONS

- **The demise of community banks contributes to the demise of small businesses.**
  - We need to develop policy interventions to foster a better banking environment for community banks (without sacrificing financial stability).
- **Conglomeration in the non-financial industry erodes the financial stability of community banks and contributes to conglomeration in the banking sector.**
  - Questions the need for the intervention
  - Consolidation in the non-financial industry is nothing new

GLASS HALF EMPTY

DOES SMALL BUSINESS MATTER?

- What are implications of the conglomerations and death of small businesses?
  - Does the labor force shift frictionlessly to larger firms?

  or

  - Do we live in an era of disparity between GDP growth and employment growth due to the death of small businesses?

- <u>COVID crisis</u>
  - Unprecedented collapse of small businesses across the country
  - The financial markets are doing well

GLASS HALF EMPTY

FINANCIAL TECHNOLOGY

- Significant economies of scale enjoyed by large banks
  - Community banks have few capabilities to compete in the long run
- Rapid changes in the job market lead to the evolution of winners that nearly monopolize industries
  - Community banks cannot support industry leaders

DE NOVO COMMUNITY BANKS

- **"Bank Entrepreneurs"**
  by Kristoph Kleiner, Manju Puri, and Chiwon Yom
  - De novo banks illustrate the niche that large banks do not (cannot) occupy
  - Need for local services and expertise provided by community banks
  - Once a community banker, always a community banker

GLASS HALF FULL

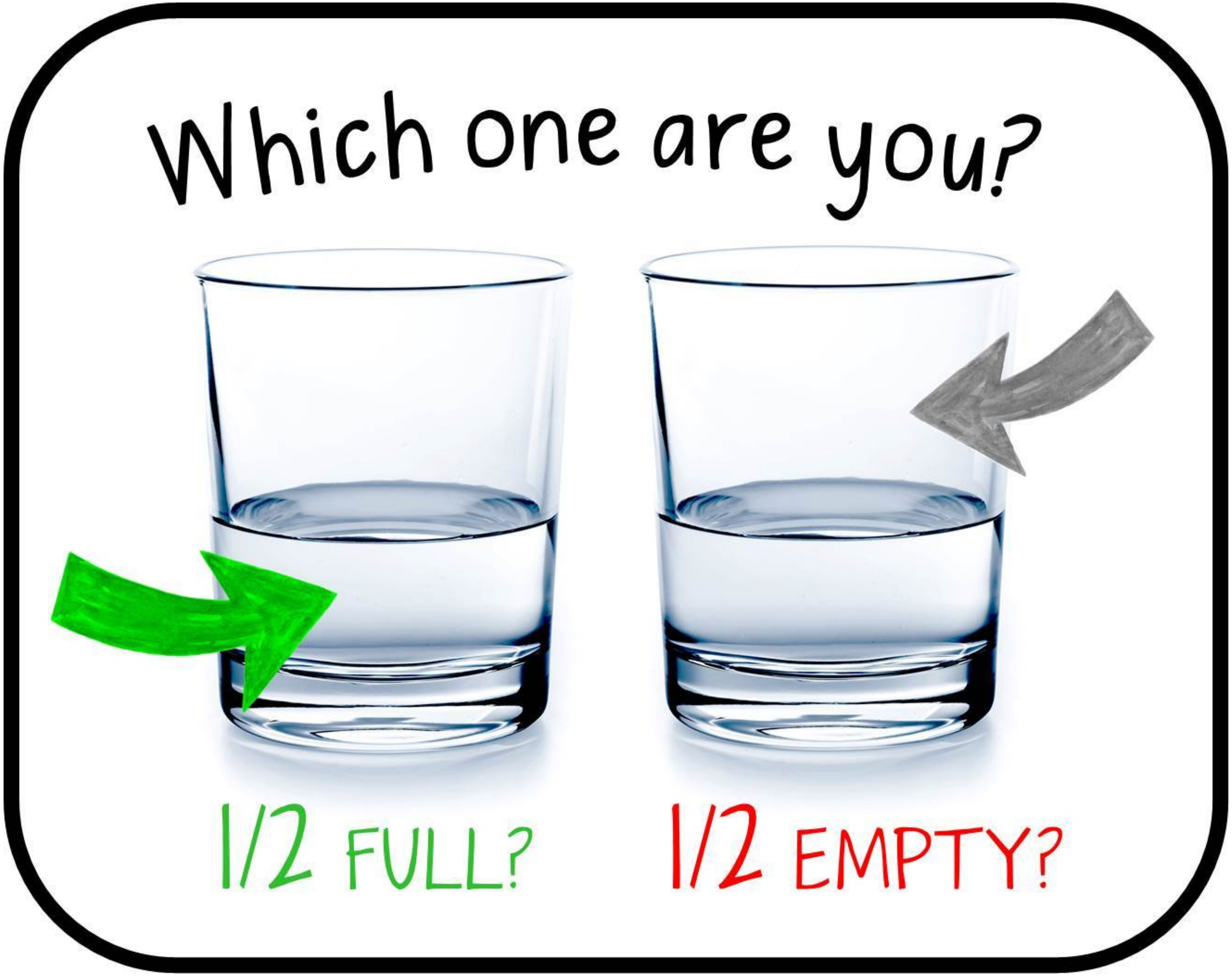
FINANCIAL TECHNOLOGY

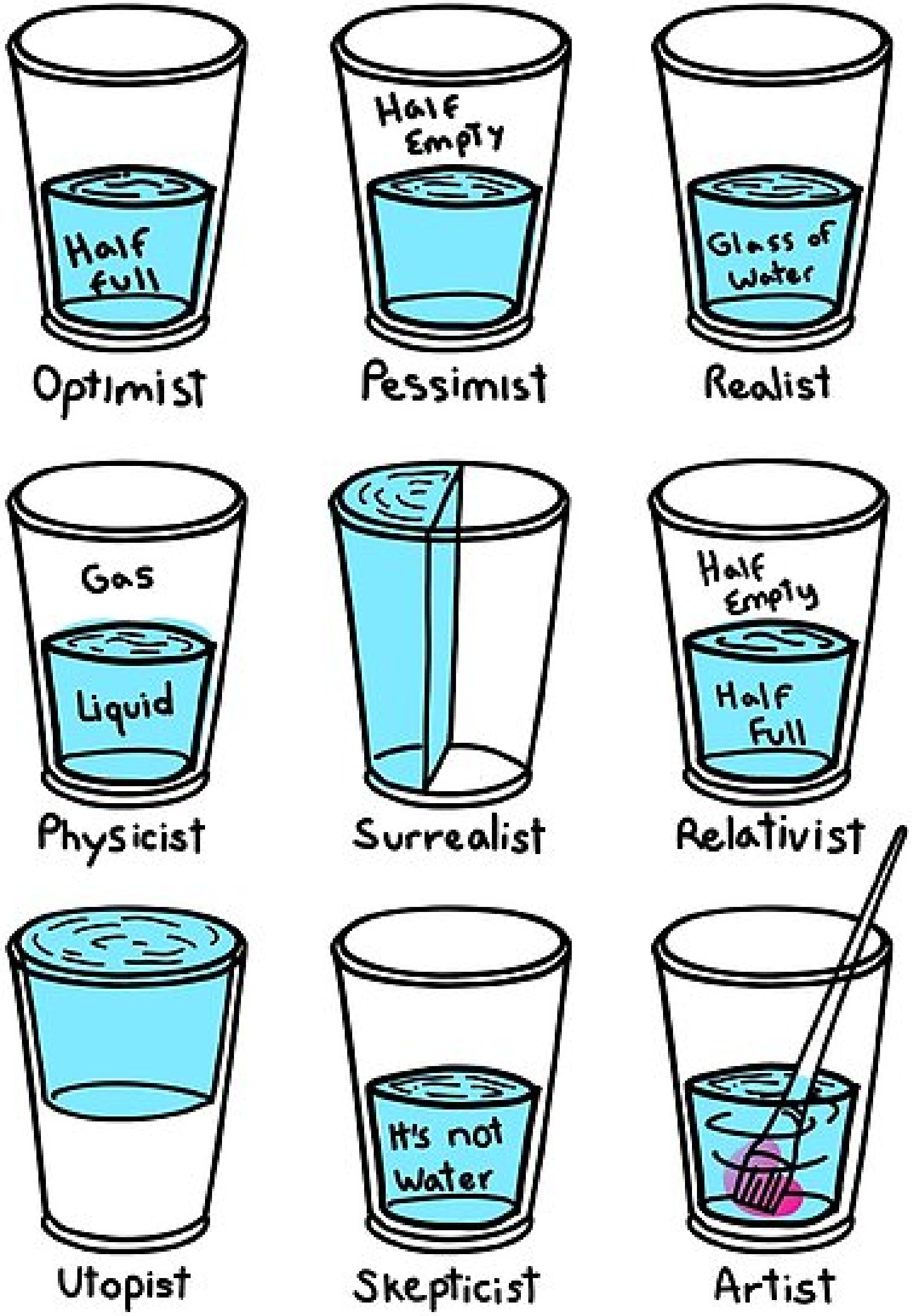
- Technology is flexible
  - Banking as a service (BaaS) solutions.
  - Capitalize on Durbin Amendment

- Technology is sharable
  - Community bank consortiums can potentially share the same technology to cover a specific function and capitalize on their unique local market knowledge

- FinTech industry versus banking regulations
  - A match made in…?

GLASS HALF FULL


Which one are you?
1/2 FULL?
1/2 EMPTY?



I KNOW… IT IS NOT THAT SIMPLE

I AM HOPEFUL: SMALL BUSINESS MATTERS

- **99.7**% of US employer firms
- **64**% of net new private-sector jobs
- **49.2**% of private-sector employment
- **42.9**% of private-sector payroll
- **46**% of private-sector output
- **43**% of high-tech employment
- **98**% of firms exporting goods

- Community banks <u>support</u> these businesses.
- About a thousand new bank charters issued since 2008 suggests that community bank services are needed.
- How can policy enable bank entrepreneurs?

I AM HOPEFUL: FINANCIAL TECHNOLOGY

- Is democratizing consumer access to financial services
- Has a potential to democratize community banks' access to technology-enabled services
- FinTech firms need community banks' insights into local markets
- Can we find a way to support each other?

THANK YOU