

Community Banks and the Local Economy

Comments by
Greg Nini, Drexel University

Community Banking Research Conference, October 2024

Three Fantastic Papers

Each paper is clever.

- Deposit rates contain information and are available for individual banks.
- Acquisitions offer an opportunity to see a market value of private banks.
- Community banks can be linked to their broader geographic areas.

Each paper has fantastic data and offers careful analysis.

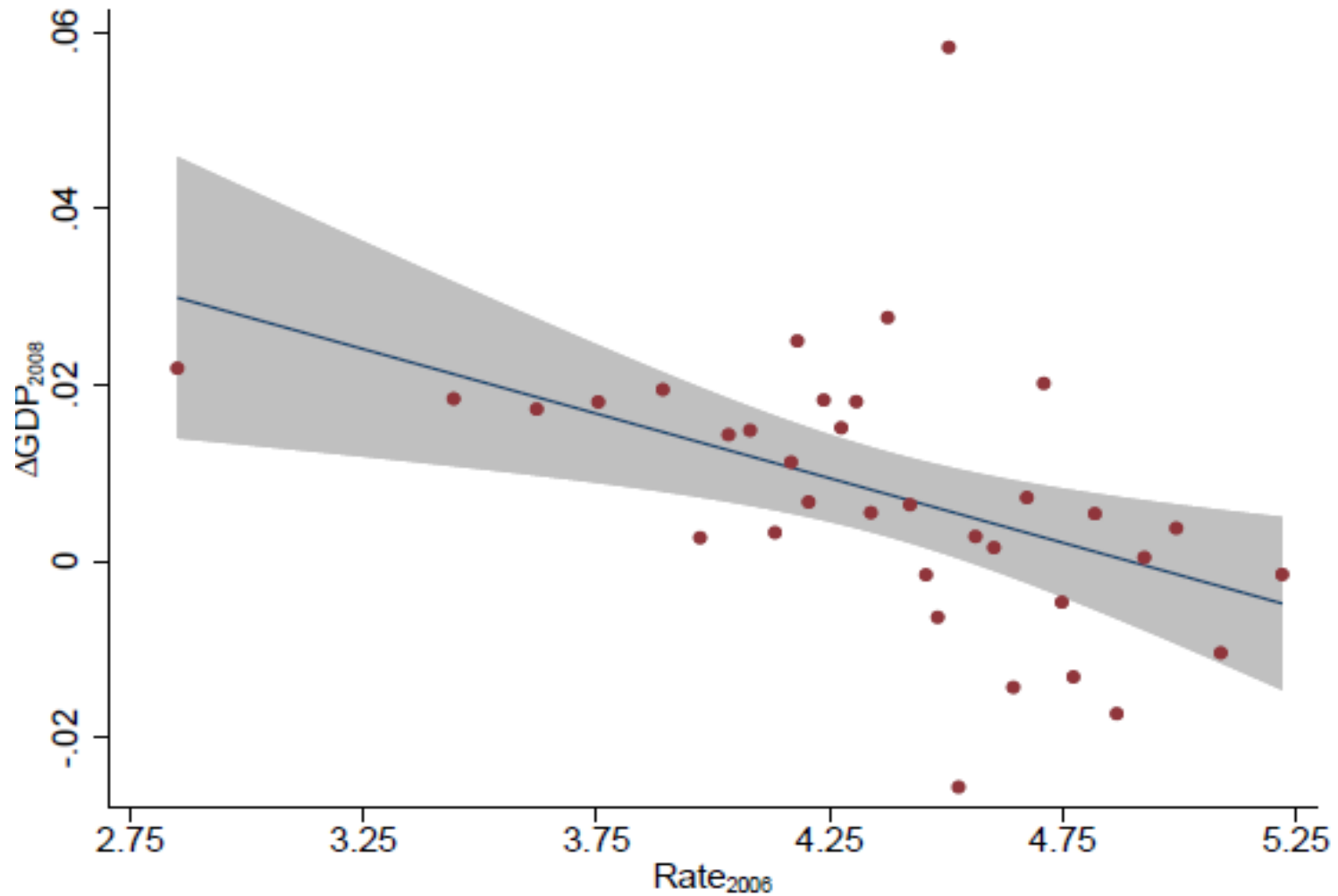
A Through Line... Community **Bankers** are Valuable

The value of a bank is mostly derived from its **employees**.

- Salaries and benefits account for 55% of noninterest expenses.
- Relationships are, at least partly, between people.
- Employees have access to information and good incentives to make good decisions.

Result 1: Deposit Rates Predict Subsequent GDP Growth

Figure 4: 2006 Deposit Rates Predict 2008 GDP Growth



The Fed Already Looks for the Canary... Sort Of

The Fed's **Beige Book** summarizes anecdotal information about economic conditions in each district.

- St. Louis, September 2024: “Contacts provided mixed reports on deposits. A Memphis banker reported competition for deposits is easing slightly, while a Louisville banker reported the competitive landscape for core deposits has intensified.”

This paper shows how to formalize the canary.

- Perhaps aggregating the country-level forecasts can improve overall GDP forecasting.

Result 2: Small C&I Loan Portfolios are Valuable

Acquired Bank's Small C&I Book	Fraction of Small C&I Loans	Premium relative to Book Value
Low	3%	103%
<u>High</u>	<u>8%</u>	<u>109%</u>
Difference	5%	6%

Premium is even larger if the loans are **very small**.

Acquirers are Willing to Pay for Small C&I Loans

The acquisition price (probably) reflects the value of the C&I portfolio to the acquirer.

- Relationship benefits pass to the acquirer.

Who are the acquirers and what happens to the employees of the acquired bank?

- My hypothesis: The relationship lender is the **banker**, who often stays post acquisition.
- And maybe the banker is given more resources to expand the relationship.

Result 3: Counties “Losing” a Bank Grow Faster

	Change in Small Business Lending	Change in Employment
Loss vs. No Loss	+7.1%	+0.6%

Larger effects when:

- Many other community banks in the county
- Acquirer is smaller

But the effect is never negative.

Perhaps this Result is NOT Surprising

Theory and evidence suggests that acquisitions have two competing effects on local economies:

- Reallocation of resources to more productive banks.
- More concentrated banking sector.

Evidence suggests that “losing” a bank is better interpreted as **gaining** the synergies from the reallocation of resources that increases the productivity of bankers.

Back to the Through Line...

Bankers are valuable:

- Bankers set deposit rates strategically with **foresight** about future supply of deposits.
- Lending **relationships** are with bankers and persist when a bank is sold.
- The acquisition of a bank benefits the local community, perhaps because bankers become more **productive**.