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Minority-Owned Depository Institutions: A Market Overview

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Small businesses are the backbone of broad-based economic development and adequate funding for these enterprises is key to ensuring their job-creation role. At the same time, the United States has seen a significant (and growing) underrepresentation of minority-owned small businesses. The Milken Institute has been at the forefront of investigating the root causes of this discrepancy and the related negative effects on job creation and wealth generation within minority communities. Building from initial conversations carried out at the White House, the Milken Institute and the U.S. Small Business Administration formed an initiative to develop actionable solutions to the challenges that limit minority-owned small businesses from accessing capital. The Partnership for Lending in Underserved Markets (PLUM), a two-year pilot program, was launched to this effect in September 2016 and has since completed its first two phases.[1] Building from the initial findings of PLUM, the Milken Institute has committed to delve further into considering market-based solutions that specifically address the identified shortcomings in this space. This paper deals with the opportunities afforded by minority-owned depository institutions (MDIs) to fuel job growth in low- to moderate-income communities.

[1] In May 2018, the Milken Institute released a summary of the second phase of its Partnership for Lending in Underserved Markets, which is available here. The paper provides greater detail to the joint Milken Institute-U.S. Small Business Administration initiative, and the operational activities in two target markets. The paper discusses challenges of minority-owned small businesses in relation to capital access; this paper attempts to build off of these key program learnings while delving specifically into the MDI sector.

Small businesses are the backbone of broad-based economic development; yet, at the same time, the U.S. has seen a significant (and growing) underrepresentation of minority-owned small businesses.

The primary source of startup and acquisition funding for all small businesses is savings and equity investments from personal networks, and secondarily, bank loans.

However, for minority-owned businesses, the second most prevalent source of funding is credit cards, which is typically a higher-cost product designed to fund short-term liquidity, not catalyze long-term growth. This places minority-owned businesses at a disadvantage and also potentially stymies local economic development. Increasing access to bank lending is an important component of improving the potential of minority-owned small businesses and the communities in which they operate

Some communities are not being well served by the banking sector. There is evidence that minority-owned small businesses face negative bias in their interactions with financial institutions. When trying to secure a business loan from a bank, over 80 percent of minority business owners are asked to furnish business financial statements, compared to only 50 percent of white business owners. Furthermore, on average, 72 percent of minorities do not have a bank branch in their neighborhood. Given the challenges faced by small businesses, especially minority-owned small businesses, it is informative to assess which type of banks are more likely to equitably provide access to capital for minority communities.

One particular category of banks worth examining are MDIs. MDIs are designated by the Federal Deposit Insurance Corporation (FDIC) according to criteria which determines minority-ownership of the depository institution. The communities primarily included are the Black, Hispanic, and Native American populations.[2] While further discussion will explore MDI geographic characteristics, they are broadly found across the nation with particular regional concentrations along the coasts. According to data from the Home Mortgage Disclosure Act (HMDA), MDIs are far more effective in both having branches in minority neighborhoods and having a significant portion of their lending activity targeting minorities. The reality is that there are greater opportunities for minority-owned small businesses to secure needed capital when they can seek funding from local MDIs.

[2] "Minority" as defined by Section 308 of FIRREA means any "Black American, Asian American, Hispanic American, or Native American." (source: FDIC Minority Depository Institutions Program)

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The reality is that there are greater opportunities for minority-owned small businesses to secure needed capital when they can seek funding from local MDIs.

Unfortunately, MDIs themselves have experienced a period of significant decline. After the last financial crisis, more than 25 percent of MDIs have exited due to consolidation or insolvency. In addition, MDIs are far smaller than the average non-MDI bank. Compared to commercial banking institutions on average, they are very small—with the largest institution only having $35 billion in total assets. Black and Hispanic[3] MDIs have average assets of $246 million and $2.5 billion respectively compared to an average of $3 billion for all U.S. banks. Wells Fargo alone has over three times more branches than the combined 167 MDIs nationwide.

[3] The Milken Institute recognizes the difference between "Hispanic" and "Latino" designations and the ongoing debate regarding which is most appropriate. However, because this is a data-driven report and the U.S. Census Bureau uses the "Hispanic" classification, for consistency we have chosen to use "Hispanic" throughout this piece, unless source data denotes otherwise. Likewise, we will defer to "Black" versus "African American," again consistent with the Census Bureau classification, unless source data denotes otherwise.

$35 BILLION	$246 MILLION	$2.5 BILLION
MDI's total assets	Average assets for Black MDI's	Average assets for Hispanic MDI's

MDIs' smaller scale translates to difficulty in navigating and operating in a highly regulated, quickly transforming industry. That limits their ability to serve the communities that need their help the most. In order for MDIs to scale up their efforts to provide funds to minority communities, they require funds themselves—equity capital in particular—to invest in their own capabilities. Organizational transformation strategies for these institutions has the potential to unlock much greater mobilization of funds towards their communities.

To that end, this paper documents the role of MDIs in supporting small businesses over the past 15 years.

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According to our analysis, MDI branches are located in census tracts with an average 74 percent minority population, compared to the 28 percent for all FDIC-insured depository institutions. This puts the MDIs in the right location to create an economic multiplier effect for communities of color.

Future research is essential to determine MDIs' ability to act as a catalyst for economic development in underserved communities through lending to minority-owned small businesses. Responsible capitalization and operational transformation of MDIs could spur their growth and, given their location and predisposition to small-business lending, growth in underserved economies across the United States. We believe that by better capitalizing MDIs, especially with Tier 1 capital, these institutions will be better positioned to support small businesses in their communities—often ones that are minority-owned. As such, we view MDIs as a conduit to realizing objectives of job creation and wage growth within low- to moderate-income communities. Further, we believe that MDIs also serve a depository function that will service small businesses within their communities—supporting these institutions as they grow beyond initial debt financing, thereby leading to increased profitability. As a next phase to this initiative, the Milken Institute will investigate whether these hypotheses hold empirical truth by assessing capacity constraints of MDIs and conducting quantitative analysis around their potential impact.

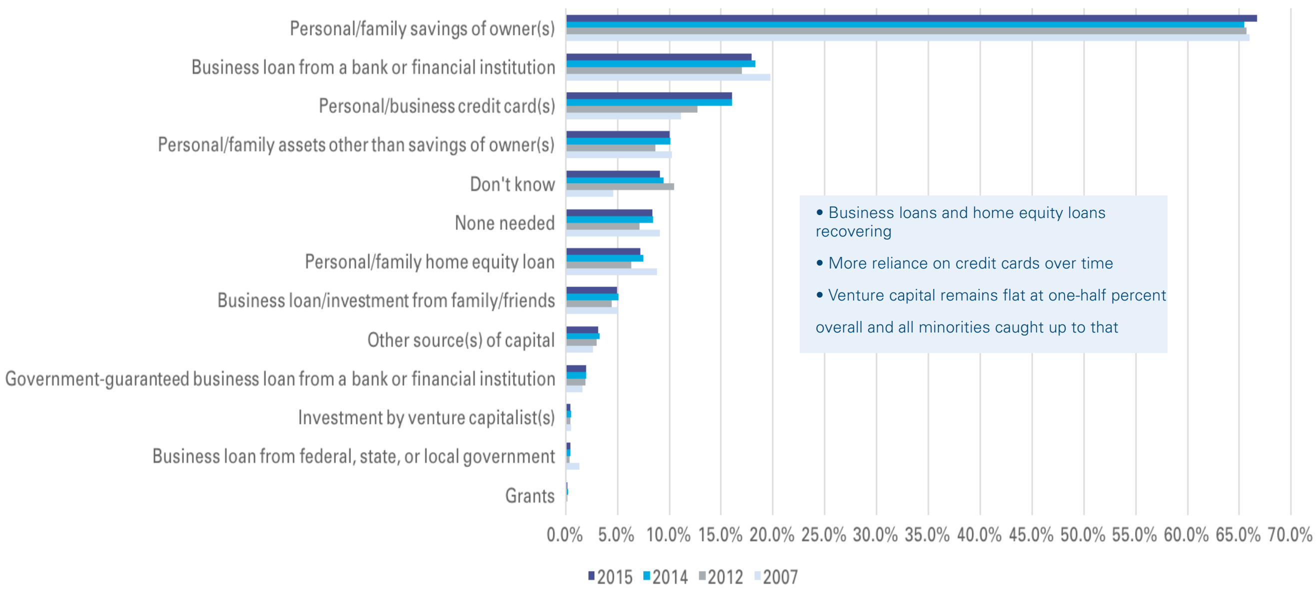
BACKGROUND OF MINORITY-OWNED SMALL BUSINESSES IN THE U.S.

Undeniably, the United States' prosperity over time has occurred through steady economic growth and ongoing job creation. Ensuring that all segments of society have the opportunity to contribute and benefit when the economy grows and more people find employment is critical to an equitable and just society. In this respect, small businesses play an important role because they represent 99.9 percent of all businesses and account for 47.8 percent of the private workforce throughout the nation, according to the U.S. Small Business Administration (SBA).[4]

Ample funds are always necessary to support the creation of new small businesses and the continued growth of existing small businesses. For small businesses overall, the initial source of funds to start or acquire a business comes mainly from personal or family savings, at 65 percent. The second-most common form of funding is bank loans, at slightly more than 15 percent, as shown in Figure 1. The figure also shows that personal/business credit cards have become almost as important as loans from banks and are growing with time. Further sources of funds, such as venture capital investment, are utilized far less than personal or family savings, banks, and credit cards.

[4] SBA, https://www.sba.gov/sites/default/files/advocacy/United_States_1.pdf, accessed April 13, 2018.

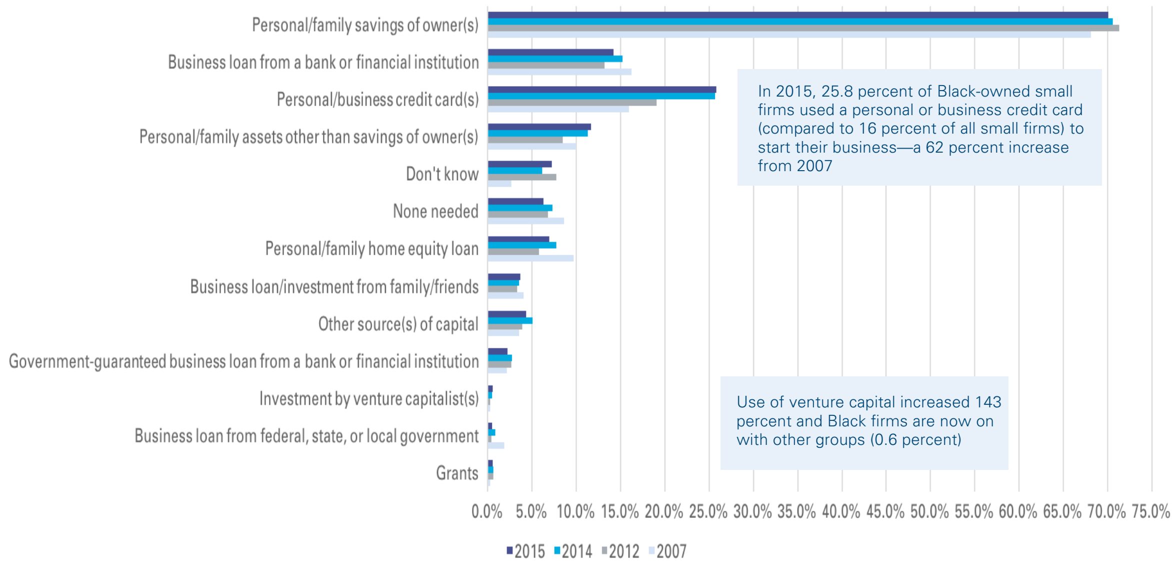
Figure 1: Share of Sources of Capital Used to Start or Acquire a Business, 2007-2015



Source: U.S. Census Bureau, 2015 Annual Survey of Entrepreneurs

Focusing on Black-owned businesses, Figure 2 shows that personal or family savings also rank first as a source of funds, at 70 percent. In contrast to the full small-business community, however, personal/business credit cards rank second, at 25 percent, and become more utilized than bank loans, at 15 percent, over the period shown. Moreover, in 2015, 26 percent of Black-owned small businesses used credit cards as a source of startup funds, as compared to 16 percent of all small businesses. Although sources of capital for existing businesses may differ, the initial inability to secure lower-cost commercial bank loans for a startup poses a material barrier. Interestingly, in the same year, funds from venture capitalists put Black-owned business on par with the full small-business sector. However, at less than 1 percent, such funds were relatively unimportant.

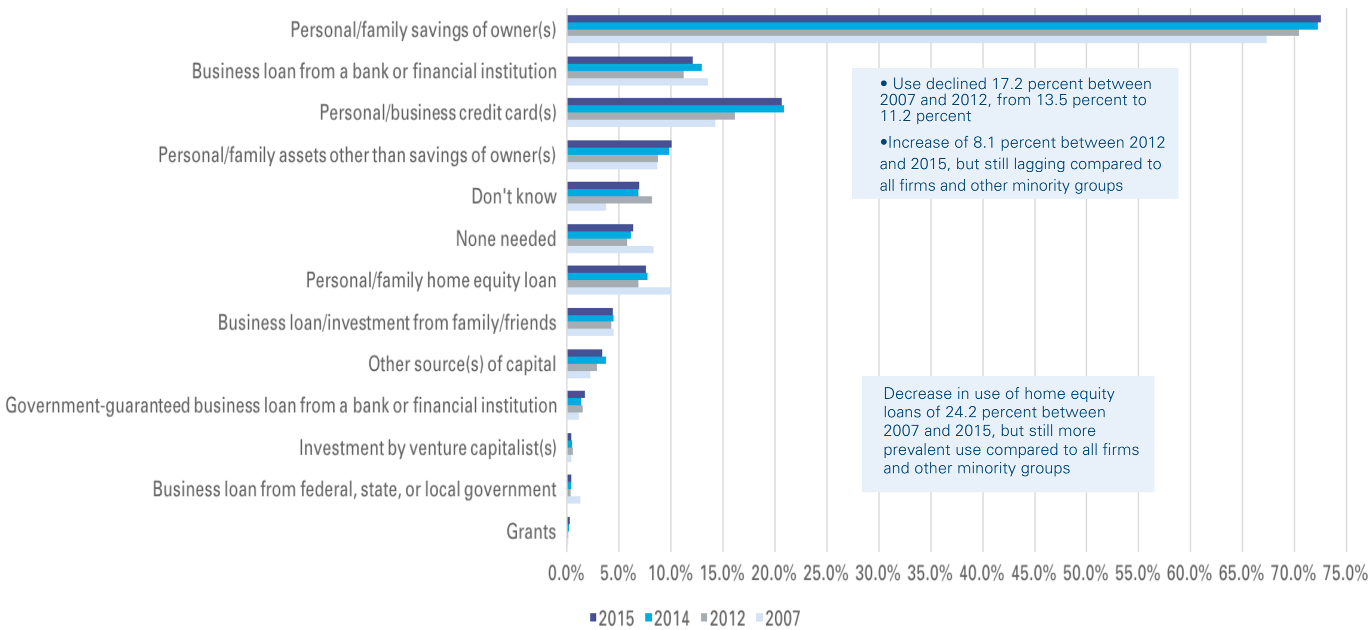
Figure 2: Share of Sources of Capital Used to Start or Acquire a Black-Owned Business, 2007-2015



Source: U.S. Census Bureau, 2015 Annual Survey of Entrepreneurs

Figure 3 provides similar information for Hispanic-owned businesses. Once again, the most utilized source of funds is from personal or family savings, at more than 70 percent. As was the case with Black-owned businesses, personal/business credit cards are the second-most utilized source of funds to start or acquire a business, but to a much smaller degree, at 20 percent. These two sources of funds are followed in utilization by loans from banks, at slightly more than 12 percent.

Figure 3: Share of Sources of Capital Used to Start or Acquire a Hispanic-Owned Business, 2007-2015



Source: U.S. Census Bureau, 2015 Annual Survey of Entrepreneurs

More generally, these two ethnic groups are not represented in the private sector as their percentages in the population might suggest. For example, in 2015, 12.7 percent of the population was Black, 17.6 percent was Hispanic, and 5.4 percent was Asian.[5] Yet, Table 1 shows that Blacks' shares of firms, sales, employees, and payroll are far below their share of the population.[6] The same is the case for Hispanics, though to a lesser degree as compared to Blacks. Asians, however, have a larger percentage in the case of firms than their share of the population might indicate.

[5] U.S. Census Bureau, https://www.census.gov/quickfacts/fact/table/US/PST045217, accessed May 29, 2018.

[6] Of the total number of businesses, or 29.6 million, 99.9 percent are small businesses. Of the small businesses, 5.4 million have paid employees. See U.S. Census Bureau, 2014 Annual Survey of Entrepreneurs.

Table 1. Firms, Sales, Employees, Payroll, and Shares by Ethnic Group (%), 2015

	Number of firms with paid employees	Sales, receipts, or value of shipments of firms with paid employees ($1,000)	Number of paid employees for pay period	Annual payroll ($1,000)
Total	**5,531,169**	**33,597,636,520**	**118,402,027**	**5,930,504,233**
Minority Share	**18.0%**	**3.5%**	**6.8%**	**4.3%**
Black	2.1%	0.3%	0.8%	0.5%
Hispanic	5.7%	1.1%	2.2%	1.4%
Asian	9.6%	1.9%	3.5%	2.2%

Source: U.S. Census Bureau, 2015 Annual Survey of Entrepreneurs

Table 2 shows the extent to which the three ethnic groups are overrepresented or underrepresented based on their shares in the population relative to their shares in the various segments of the private workforce. All the ethnic groups are underweighted across the different segments with the exception of Asians in terms of the number of firms. Blacks are the group most underweighted.

Table 2. Overrepresented (+) vs. Underrepresented (-) Share of Firms, Sales, Employees, and Payroll by Ethnic Group Based on Percentage of U.S. Population, 2015

	Number of firms with paid employees	Sales, receipts, or value of shipments of firms with paid employees	Number of paid employees for pay period	Annual payroll
Black	-83.8	-97.7	-93.3	-96.3
Hispanic	-67.8	-93.9	-87.6	-92.1
Asian	78.4	-63.9	-35.1	-59.3

Source: Milken Institute analysis, U.S. Census Bureau, 2015 Annual Survey of Entrepreneurs

The figures in these tables raise the issue as to whether minorities desiring to start a small business or expand an existing small business are at a disadvantage as compared to non-minorities in the same position when it comes to obtaining funding. If this is the case, then the opportunity to contribute to and benefit from economic growth and job creation is not available to everyone throughout society.

In this regard, Table 3 further suggests that a bias problem exists more broadly, even for individual consumers.[7] As is seen, the required documentation from minority business owners to obtain a loan is stricter than that required of white business owners. In addition, the assistance provided by loan officers to minority business owners is significantly less than that offered to non-minority business owners. While this finding does not reflect that there is less bias at MDIs, we can assume that the issue of minority bias is less prevalent at institutions which are largely servicing minority communities, and thus have a more homogenous (i.e., minority-oriented) customer base.

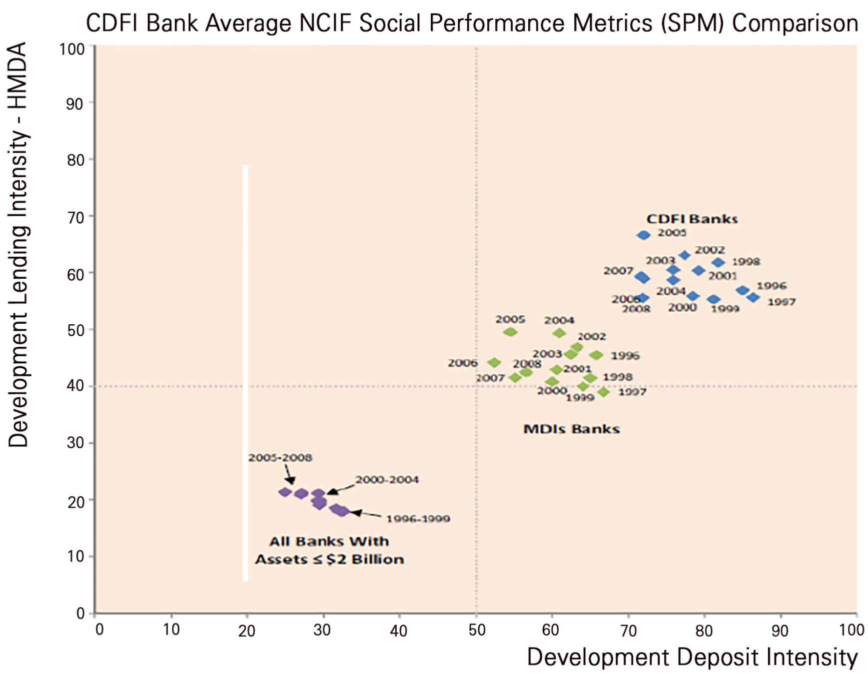
	Activity	Minority Business Owners	White Business Owners	Delta
A. Requested loan documentation	Income tax returns	86%	52%	**1.7x**
	Business financial statements	83%	50%	**1.7x**
	Credit card debt	42%	13%	**3.2x**
	Personal financial assets	60%	22%	**2.7x**
B. Loan officer assistance offered	Assistance completing loan application	18%	59%	**31%**
	Offered business card	43%	82%	**52%**

Source: Bone, S., Christensen, G., and Williams, J. (2014). Rejected, shackled and alone: The impact of systemic restricted consumer choice among minority customers' construction of self, Journal of Consumer Research, 41: 451-474

[7] What we do not know is the riskiness of potential borrowers and the interest rates that would be charged for individuals in the two groups.

Furthermore, based on data from the HMDA, the National Community Investment Fund (NCIF) analyzed the relative difference between the proportion of different types of financial institutions' mortgage activities and branch locations in low- and moderate-income census tracks. As shown in Figure 4, the analysis[8] compared the Development Depository Intensity (DDI)[9] and Development Lending Intensity (DLI)[10] of community development financial institutions (CDFIs)[11], MDIs, and all other banks (assets less than or equal to $2 billion) and found that for the decade preceding the financial crisis, CDFIs, followed closely by MDIs, were more likely to locate and provide mortgages to disadvantaged communities compared to other banks with assets less than $2 billion. Later in the paper, we explore a similar relationship as related to small-business lending. Although most MDIs are CDFIs, not all CDFIs are MDIs. In addition, while MDIs are for profit, not all CDFIs are for-profit enterprises, and as such, MDIs are a key focus for this paper.

Figure 4. CDFI Bank Average NCIF Social Performance Metrics (SPM) Comparison (1996-2008)



Source: National Community Investment Fund, Social Performance Metrics, http://www.ncif.org/inform/social-performance-metrics

[8] Risk and Efficiency among CDFIs: A Statistical Evaluation using Multiple Methods, Office of Financial Strategies and Research, CDFI Fund, U.S. Department of Treasury, August 2014, by Gregory Fairchild and Ruo Jai https://www.cdfifund.gov/Documents/Risk%20and%20Efficiency%20among%20CDFIs%20Report.pdf.

[9] DDI: The percent of branches located in Investment Area census tracts as defined by the CDFI Fund. Census tracts are defined as Investment Areas if they have a poverty rate greater than 20 percent, an unemployment rate greater than 1.5 times the national average, or a median family income that is less than 80 percent of the relevant statistical area. To calculate DDI, bank branch addresses from the FDIC are geocoded and compared to Investment Area census tracts.

[10] DLI-HMDA (Development Lending Intensity-HMDA): The percentage of HMDA-reported loans located in CDFI Investment Areas. To calculate DLI-HMDA, loan information is collected from FFIEC, geocoded, and compared to CDFI Fund Investment Areas.

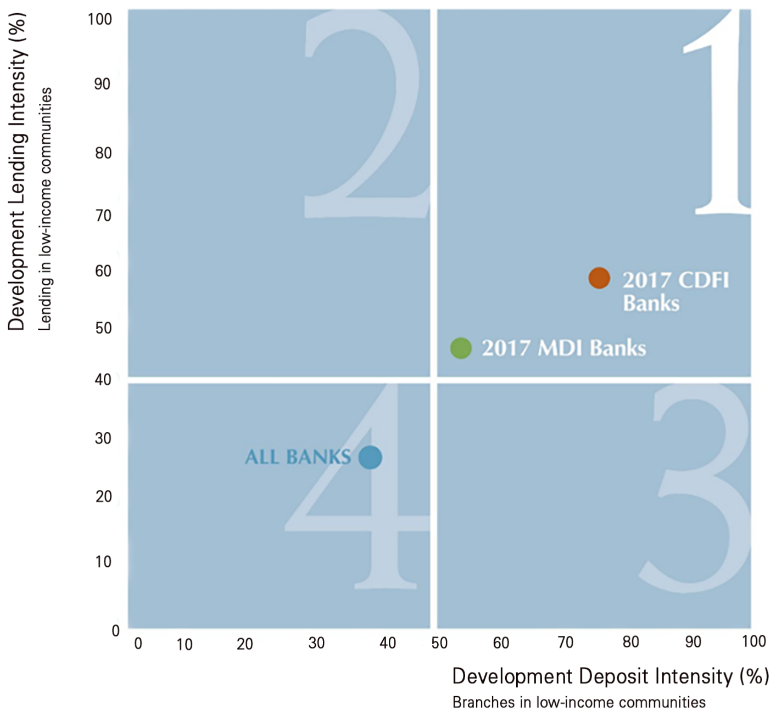
[11] CDFIs are mission-driven financial institutions that create economic opportunity for individuals and small businesses, quality affordable housing, and essential community services throughout the United States. There were 141 CDFI banks as of December 31, 2017.

Post crisis, as shown in Figure 5, NCIF analysis reveals that this relationship still holds today.[12] CDFIs and MDIs are far more likely to locate and support disadvantaged communities compared to all other banks.

[12] One nuance is that while the pre-crisis view only captures banks with assets less than or equal to $2 billion, the post-crisis view includes all banks regardless of assets. This should not influence the overall conclusion of the comparison.

Figure 5. CDFI Bank Average NCIF Social Performance Metrics (SPM) Comparison (2017)[13]

[13] NCIF SPM Quadrant Analysis as of April 26, 2018, provided by NCIF.



Source: National Community Investment Fund, Social Performance Metrics

OVERVIEW OF MINORITY-OWNED DEPOSITORY INSTITUTIONS

A key benefit of banks to communities in which they are headquartered or have branches is that economic growth fueled by bank lending can be recycled back into the bank, not only due to loan payments but also savings deposits. These can fuel additional opportunities for other individuals and businesses who bank with the same provider and therefore contribute to local economic development that benefits the entire community.

An MDI is, according to the FDIC, "any depository institution where 51 percent or more of the stock is owned by one or more 'socially and economically disadvantaged individuals.' These are defined to primarily include members of the Black, Hispanic and Native American populations."[14] In addition, an MDI designation could also apply if the above ownership test is not met, but the board of directors has more than half of its members from minority populations and serves a predominantly minority community. The FDIC maintains a database of institutions meeting the MDI designation and updates it on a quarterly basis.

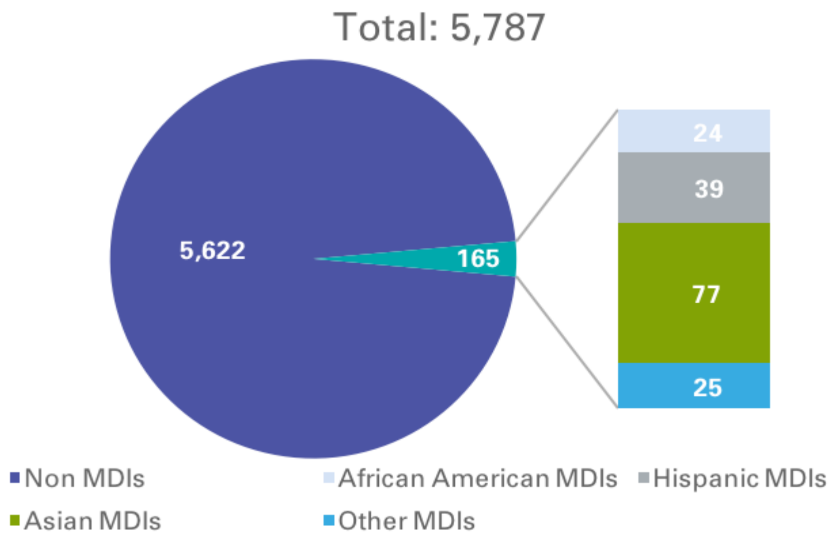
A key distinction that arises is the extent to which MDIs, given their direct relationship to minority communities, are able to promote greater economic growth and job creation for the minority communities they serve by providing loans to small businesses, especially minority-owned small businesses. If successful, the funding provided by MDIs could contribute to more opportunities and benefits for those living within their communities, which is particularly helpful in minority communities. Mutually, the MDIs themselves could grow and prosper to a greater degree as the communities in which they operate do the same. Other sources of capital provided to small businesses may not come from entities within such communities and therefore do not necessarily contribute to a local cycle of wealth creation.

[14] "Minority" as defined by Section 308 of FIRREA means any "Black American, Asian American, Hispanic American, or Native American." (source: FDIC Minority Depository Institutions Program)

OVERVIEW OF MINORITY-OWNED DEPOSITORY INSTITUTIONS

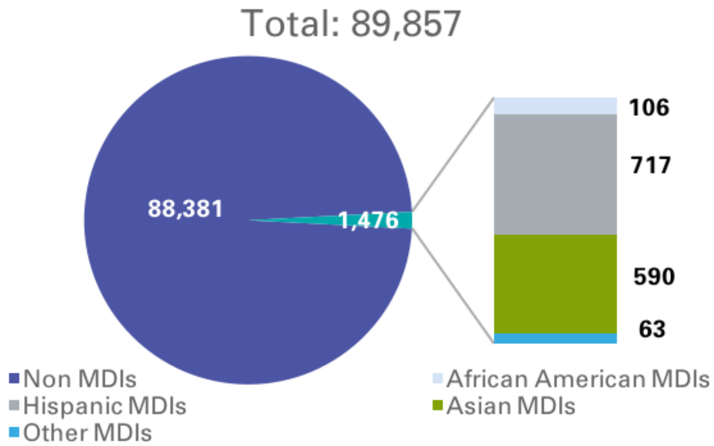
Given the funding challenges faced by small businesses, especially minority-owned small businesses, it is informative to examine the extent to which banks owned by minorities can be more equitable in their financing decisions. Based on the most recent data, which is from 2012, the percentage of all minority-owned small businesses was as follows: Blacks 9.1 percent, Hispanics 11.6 percent, and Asians 6.7 percent. Yet, as Figure 6a shows, of the roughly 5,700 FDIC-insured depository institutions, only a small portion are owned by these minority groups. Specifically, only 0.4 percent of banks are Black owned, 0.7 percent are Hispanic owned, and 1.3 percent are Asian owned, as of 2017. The gaps between these respective percentages are important. Figure 6b shows the situation is similar for branches. There are more than 89,000 branches, but only 106, 717, and 590 are operated by Black-, Hispanic-, and Asian-owned banks. Collectively, this means only 1.6 percent of bank branches nationwide are MDIs, compared to the 27.4 percent of small businesses, which are owned by the three in-focus minority groups.

Figure 6a. Number of FDIC Insured Institutions and MDIs by Ethnic Group, June 2017



Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figure 6b. Number of Branches of FDIC-Insured Institutions and MDIs by Ethnic Group, June 2017



Source: Federal Reserve Board and Federal Deposit Insurance Corporation

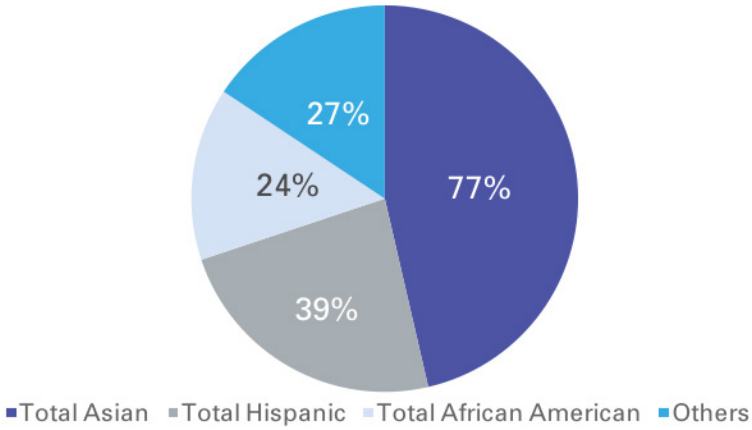
The following sections of this report document the role MDIs have played in supporting small businesses over the past 15 years. More specifically, we discuss the number of MDIs and their branches, as well as their location in census districts throughout the country. In addition, we discuss the relative importance of the different types of MDIs including the extent of their funding of small businesses. Furthermore, we identify the proportion of the population accounted for by different ethnic groups and income levels of the census tracts of the headquarters in which the MDIs are located. Lastly, this information, raises the issue as to whether an effective way to better help some communities financially and economically—particularly minority communities—may be to inject more capital into MDIs so that they can lend more to small businesses based on return and risk considerations. To the extent that MDIs are more likely to use their capital in such a way, they become high-potential job-creation catalysts in those local communities that could surely benefit from this type of boost.

OWNERSHIP ETHNICITIES VS. BOARD OF DIRECTOR ETHNICITIES

As already noted, there are different types of MDIs with respect to ethnicity. Figure 7 shows the largest number of MDIs are classified as Asian, at 77 institutions. Hispanic MDIs are second in number, at 39 institutions. Black MDIs are third in number, at 24 institutions. The remaining 27 MDIs are classified as having ethnicities different than these three groups.[15] The three largest ethnic groups identified account for 84 percent of all the MDIs.

[15] The remaining MDIs include Multi-Racial American, Caucasian Women, and Native American or Alaskan Native American.

Figure 7. Number of MDIs by Ethnic Group, June 2017

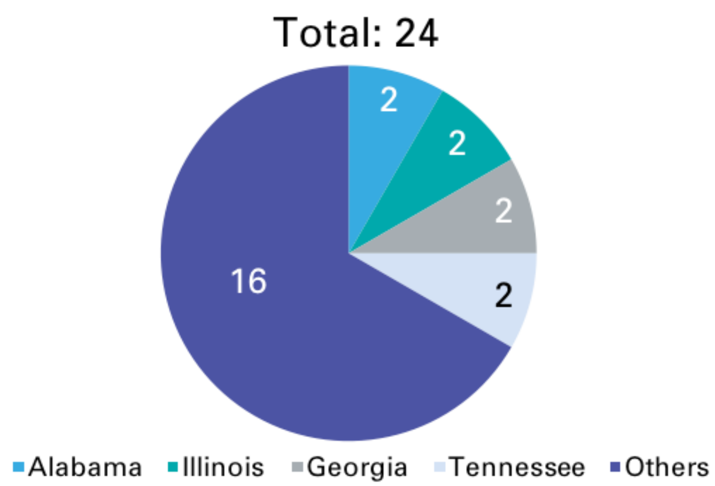


Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figures 8, 9, and 10 illustrate the breakdown of the overall MDIs by ethnic group to specifics concerning each of the three largest ethnic groups by the top four states. Figure 8 shows that there are 24 Black MDIs, with the top four states being Alabama, Illinois, Georgia, and Tennessee. Each of these states has two Black MDIs, while each of the other 16 states has one Black MDI. These MDIs are nearly evenly distributed across the 20 states in which they are headquartered. Figure 9 shows that there are 39 Hispanic MDIs, with 13 in Texas, 12 in Florida, five in Puerto Rico, and three in California. The remaining six MDIs are headquartered in other states.

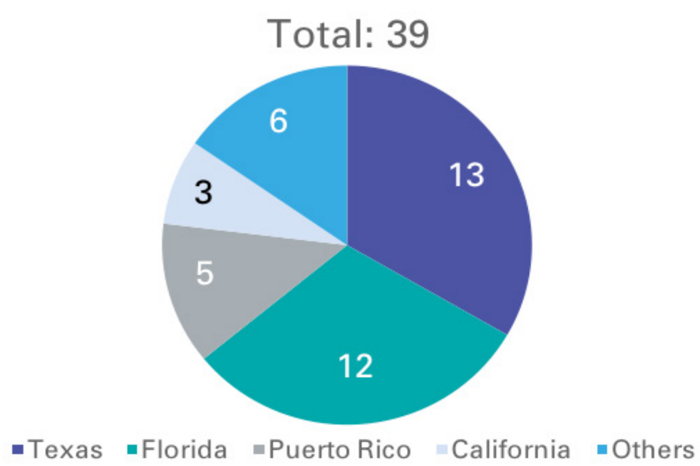
Lastly, Figure 10 shows there are 77 Asian MDIs, with 36 in California, eight in New York, seven in Texas, and six in Georgia. The remaining 20 MDIs are in other states. Once again, it is clear that there is not much of an overlap in terms of where the three different ethnic groups have their MDIs headquartered.

Figure 8. Number of Black MDIs by State, June 2017



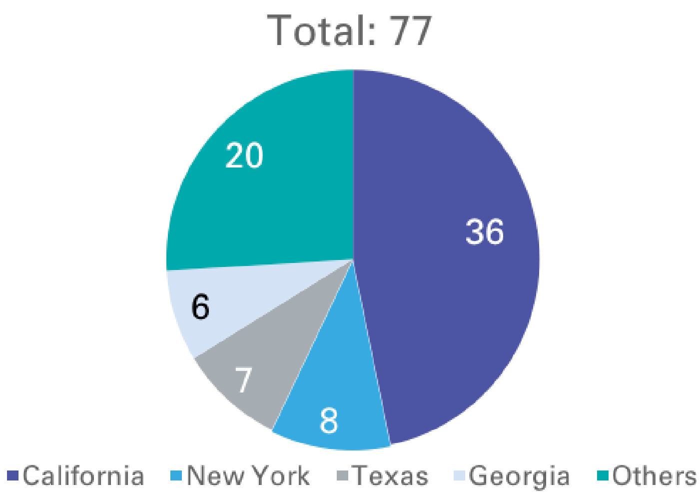
Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figure 9. Number of Hispanic MDIs by State, June 2017



Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figure 10. Number of Asian MDIs by State, June 2017



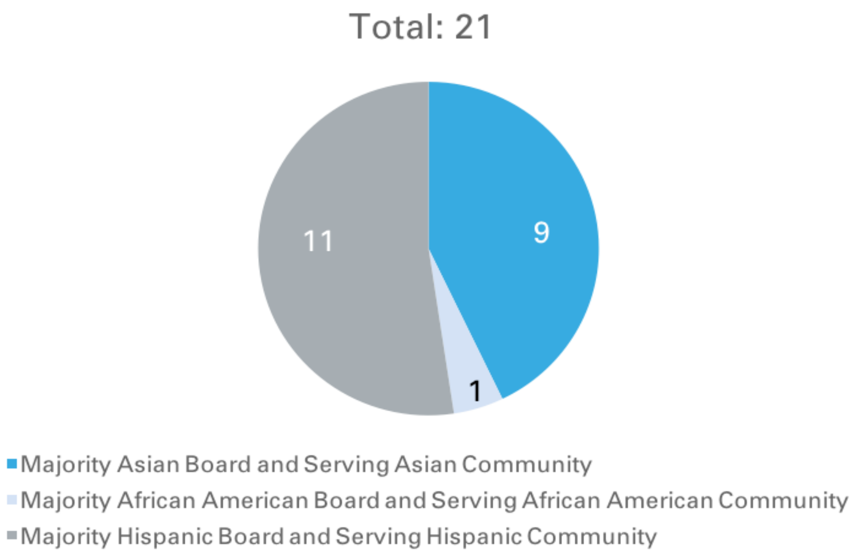
Source: Federal Reserve Board and Federal Deposit Insurance Corporation

It is also important to distinguish between MDIs based on the ethnicity of ownership vs. the ethnicity of the board of directors.[16] Figures 11 and 12 provide this information. There are 21 MDIs classified based on the board having a majority of one of three ethnic groups. Of the 21 MDIs, 11 have a majority Hispanic board, nine have a majority Asian board, and one has a majority Black board. In terms of MDIs classified based on majority ownership by one of the three ethnic groups, there are 119 MDIs. Of these, 68 are Asian, 28 are Hispanic, and 23 are Black.

[16] As stated earlier, those MDIs which do not qualify based on the ownership test have to meet criteria based on their board of directors, as well as having involvement in communities with prevalent minority populations.

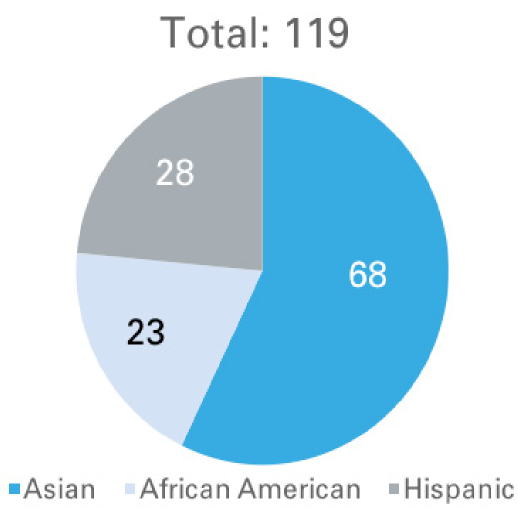
OWNERSHIP ETHNICITIES VS. BOARD OF DIRECTOR ETHNICITIES

Figure 11. Number of MDIs by Selected Ethnicity of Minority Boards, June 2017



Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figure 12. Number of MDIs by Selected Ownership Ethnicity, June 2017



Source: Federal Reserve Board and Federal Deposit Insurance Corporation

NUMBER, LOCATION, AND OWNERSHIP TYPE

Table 4 provides information on the number of MDIs and their branches by state and other locations outside the United States. According to our analysis, there were 167 MDIs with 1,476 branches as of June 2017. Although the number of branches may seem large, one should consider that Wells Fargo alone, with its 6,000 branches, has more branches than the entire MDI sector. Of the 59 locations, there are MDI headquarters in 34 of them, with branches located in the remaining locations. Specifically, some of the locations—including American Samoa, Micronesia, the Marshall Islands, the Northern Mariana Islands, Palau, and the Virgin Islands—have no MDI headquarters, but still have branches located there. For these locations, a "0" is in the table for the number of MDIs, while the number of branches is also indicated. The branches belong to MDIs headquartered elsewhere. Remarkably, there are 19 states without a single MDI headquarters. These include Arizona and Nevada, both of which have relatively high minority populations.[17] California has the most MDIs, at 40 institutions, as well as the most branches, at 324. Texas ranks second, with 21 MDIs and 287 branches. Interestingly, Puerto Rico has the second largest number of branches, at 317, but with only five MDIs headquartered there.

Given the importance of small businesses, Table 4 also presents information on the overall friendliness to such firms by states, based on the 2017 Thumbtack Small Business Friendliness Survey.[18] The survey grades states on a scale from A+ to F. Twenty-one of the states have A scores, 12 have B scores, nine have C scores, three have D scores, and three have F scores. It is noteworthy, though, that there does not seem to be a significant connection between a state's score and its prevalence of MDIs. For example, the state with the most MDIs, California, has a score of C-, while the state with the second largest number of MDIs, Texas, has a score of A+. Moreover, two of the three states with F scores have MDIs located there.

[17] U.S Census Bureau, QuickFacts,

[18] Federal Reserve Board, Federal Deposit Insurance Corporation, and Thumbtack.com Small Business Friendliness Survey, https://www.thumbtack.com/survey#/2017/1/states, accessed April 13, 2018.

There is no similar information for the MDIs located outside the United States.

Table 4. Number of MDIs, MDI Branches, and Small Business Friendliness Score, by State or Other U.S. Territory, June 2017

Name	Number of MDIs	Number of MDIs Branches	Small Business Overall Friendliness Score
Alaska	0	0	F
Alabama	3	12	B+
Arkansas	0	0	A
American Samoa	0	2	N.A.
Arizona	0	0	B+
California	40	324	C-
Colorado	1	0	A
Connecticut	0	0	C-
District of Columbia	1	5	N.A.
Delaware	0	0	A+
Florida	14	119	B+
Micronesia	0	4	N.A.
Georgia	9	25	A
Guam	3	16	N.A.
Hawaii	3	27	C-
Iowa	2	1	A
Idaho	0	0	A+
Illinois	7	34	F
Indiana	0	0	A+
Kansas	1	1	B+
Kentucky	1	0	A-
Louisiana	1	10	A+
Massachusetts	2	11	A-
Maryland	1	9	B-
Maine	0	0	A+
Marshall Islands	0	1	N.A.
Michigan	1	4	C
Minnesota	2	9	C+
Missouri	2	5	B-
Northern Mariana Islands	0	5	N.A.
Mississippi	1	1	A-
Montana	1	1	B

Name	Number of MDIs	Number of MDIs Branches	Small Business Overall Friendliness Score
North Carolina	2	20	C+
North Dakota	1	0	B
Nebraska	0	0	A-
New Hampshire	0	0	A
New Jersey	4	27	C-
New Mexico	2	5	F
Nevada	0	6	C
New York	12	109	D+
Ohio	0	0	B+
Oklahoma	12	30	A-
Oregon	0	0	C
Pennsylvania	3	4	C-
Puerto Rico	5	317	N.A.
Palau	0	2	N.A.
Rhode Island	0	0	D+
South Carolina	1	0	A
South Dakota	0	0	B+
Tennessee	2	3	B
Texas	21	287	A+
Utah	0	0	A+
Virginia	2	7	A
Virgin Islands	0	18	N.A.
Vermont	0	0	A-
Washington	2	14	B+
Wisconsin	2	1	C+
West Virginia	0	0	D+
Wyoming	0	0	A+
Total	**167**	**1,476**	**N.A.**

Notes: Some locations have branches of MDIs headquartered in other locations.

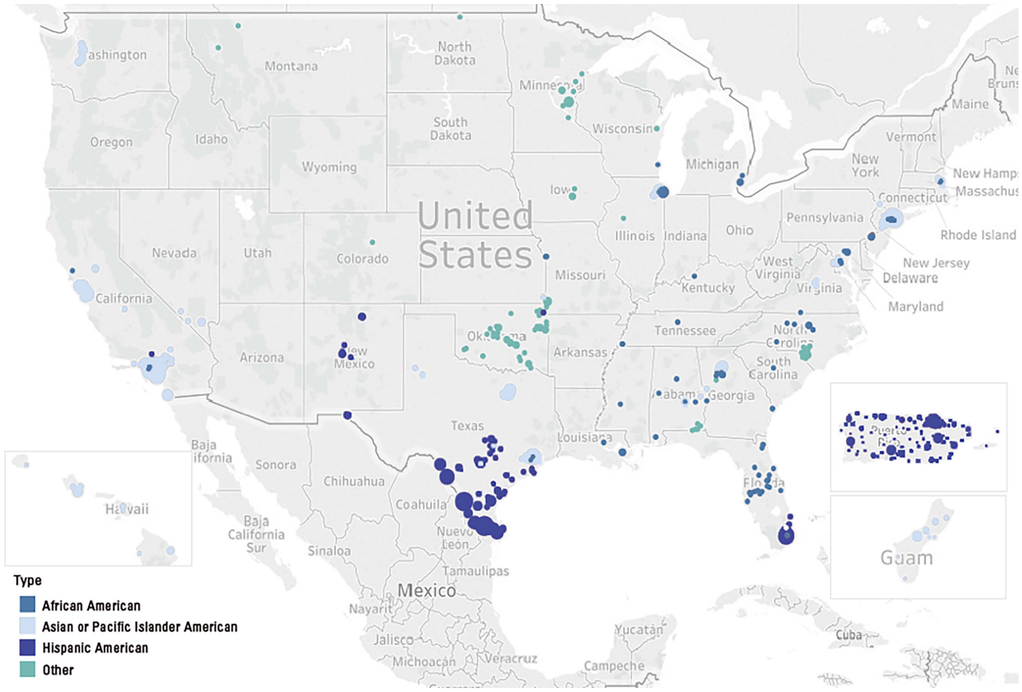
Source: Federal Reserve Board, Federal Deposit Insurance Corporation, and Thumbtack.com Small Business Friendliness Survey

Figure 13 provides a graphical and more detailed visualization of the location of all MDI headquarters and branches. The location for each of the 167 MDIs and their 1,476 branches at the census district level is shown in the figure.

As shown in the figure, MDIs and their branches tend to be clustered in relatively few places across the nation, but not necessarily where there are high minority concentrations. Most MDIs are clustered along the Gulf Coast, Texas border, and East and West Coasts. There is limited overlap in location with respect to Black, Hispanic, Asian, and other MDIs. Of course, the thousands of non-MDIs and their branches are located in cities, counties, and states where there are both MDIs and non-MDIs. Oklahoma provides an interesting view. It has 12 MDIs and 30 branches, with 10 of the MDIs owned by Native Americans (understandable, given around 9 percent of the state population is Native American). In juxtaposition, Arizona, another of the states with the highest Native American population (more than 5 percent of its population), does not have a single MDI.

MDIs and their branches tend to be clustered in relatively few places across the nation, but not necessarily where there are high minority concentrations.

Figure 13. Location of MDIs and Branches, June 2017



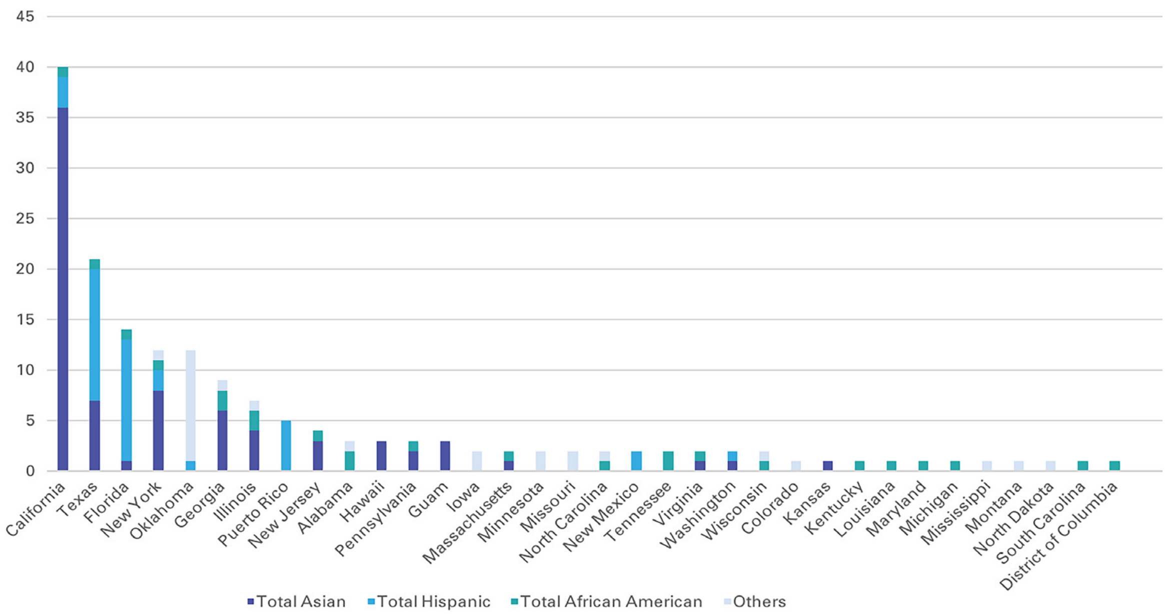
Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figures 14 and 15 provide additional visualization of both the number of MDIs and the number of branches of MDIs at the state level. Five states (California, Texas, Florida, New York, and Oklahoma) account for just over 50 percent of the total number of MDIs, while almost the same five states (Illinois replaces Oklahoma) also account for just over 50 percent of the total number of branches.

[19] States with zero MDIs are omitted from Figure 14.

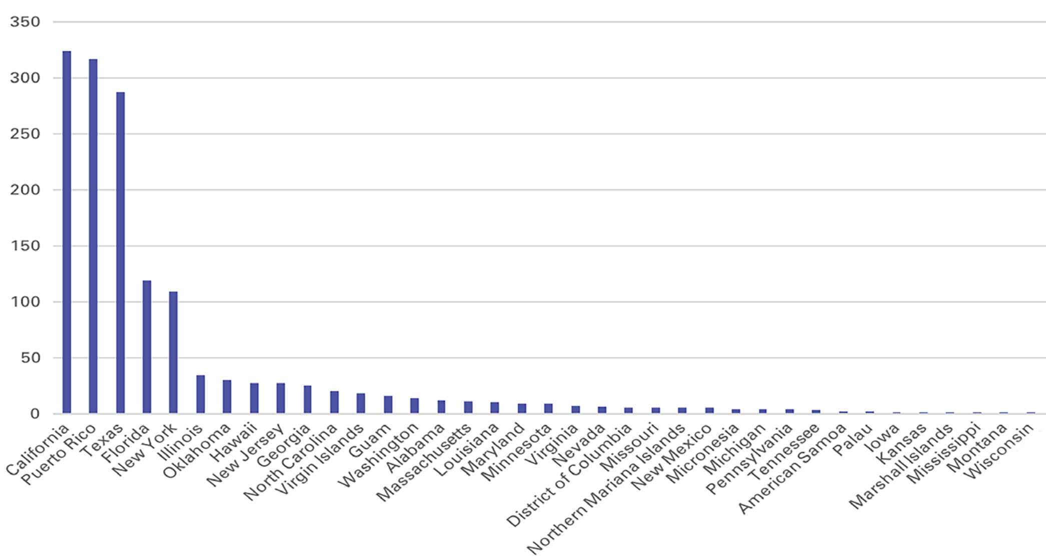
[20] States with zero MDI branches are omitted from Figure 15.

Figure 14. Number of MDIs by State, June 2017[19]



Source: Federal Reserve Board and Federal Deposit Insurance Corporation

Figure 15. Number of MDI Branches by State, June 2017[20]



NEW ENTRANTS AND EXITS

Table 5 presents information on the evolution of MDIs from the second quarter of 2003 to the third quarter of 2017. It shows that the number of MDIs increased from 111 institutions at the beginning of the period to 168 institutions at the end of the period. The maximum number of MDIs was 233 institutions in both Q4 2007 and Q4 2008, which coincided with the onset of the worst recession since the Great Depression (December 2007 to July 2009). The number of MDIs tended to decline thereafter, reaching a low of 111 institutions in Q2 2003. Regarding new MDIs, the maximum number was 71 institutions in Q4 2003. During the period Q1 2015 to Q3 2017, there was only one new MDI, which occurred in the last quarter. The maximum number of exits of MDIs was 28 institutions in Q1 2007, while there were quite a few quarters in which there were no exits. In addition, it is important to note that not all of the exits were due to failures. Some exits were due to mergers and acquisitions, and at times, some non-MDIs became MDIs and vice versa.

Table 5. MDIs: Total Number, New Entrants and Exits, Q2 2003 to Q3 2017

Quarter	Total	New	Exits	Quarter	Total	New	Exits
200302	111	N.A.	N.A.	200602	191	1	2
200303	113	4	2	200603	189	0	2
200304	183	71	1	200604	208	20	1
200401	179	2	6	200701	180	0	28
200402	179	0	0	200702	190	11	1
200403	181	2	0	200703	178	4	16
200404	191	10	0	200704	233	55	0
200501	185	0	6	200801	208	2	27
200502	185	0	0	200802	207	0	1
200503	185	1	1	200803	210	4	1
200504	207	22	0	200804	233	25	2
200601	192	0	15	200901	222	0	11

NEW ENTRANTS AND EXITS

Quarter	Total	New	Exits	Quarter	Total	New	Exits
200902	221	0	1	201303	188	3	4
200903	221	1	1	201304	184	0	4
200904	223	5	3	201401	184	2	2
201001	206	0	17	201402	184	1	1
201002	205	0	1	201403	184	1	1
201003	203	0	2	201404	185	2	1
201004	211	10	2	201501	180	0	5
201101	197	0	14	201502	178	0	2
201102	195	0	2	201503	175	0	3
201103	202	7	0	201504	173	0	2
201104	200	1	3	201601	171	0	2
201201	197	1	4	201602	169	0	2
201202	197	0	0	201603	168	0	1
201203	194	0	3	201604	168	0	0
201204	192	0	2	201701	167	0	1
201301	189	2	5	201702	167	0	0
201302	189	2	2	201703	168	1	0

Source: Federal Reserve Board and Federal Deposit Insurance Corporation

CHARACTERISTICS OF MDIS AND THE MARKETS THEY SERVE

Of all the MDIs, the largest is East West Bank located in Pasadena, California, with $36 billion in assets. The smallest MDI is Columbia Savings and Loan Association located in Milwaukee, Wisconsin, with $25 million in assets. Additional information is provided in Tables 6a and 6b, comparing MDIs and all FDIC-insured depository institutions based on selected bank, demographic, and income items. Table 6a shows the median values for the variables, while table 6b shows the mean values. In table 6a, one sees that, as expected, MDIs have the largest median percentage (74 percent) of minorities in the census tracts in which they are located as compared to all FDIC-insured depository institutions (28 percent). MDIs also have a higher median ratio of small-business loans to total assets and a higher median capital-to-asset ratio.

Black MDIs have the highest median percentage of small-business loans to total assets but have the lowest median capital-to-asset ratio. Although small in scale, MDIs are a meaningful contributor in providing access to capital for small businesses. Additionally, Black MDIs also have the highest median percentage of small-business loans to total assets as compared to the rest of financial institutions. They also have the lowest median family income amongst their customers. Black MDIs, moreover, have the lowest median total assets, except for “other MDIs.”

Although small in scale, MDIs are a meaningful contributor in providing access to capital for small businesses.

Hispanic MDIs have the highest median total assets, but the lowest median percentage of assets that are small-business loans. Also, these institutions are headquartered in census tracts in which the median percentage of the population that is Hispanic is 83 percent.

Like Black MDIs, Hispanic MDIs also have a median family income that is lower than the median of all the other groups of institutions, except for Black institutions.

Asian MDIs are located in census tracts in which the largest median percentage of population is Asian, at 37 percent. These MDIs also have the second-lowest median ratio of small-business loan to total assets, but the highest median capital-to-asset ratio of all groups of institutions.

The results tend to be similar when focusing on means rather than medians—that is, when comparing Tables 6a and 6b.

Table 6a. Medians for Selected Bank, Demographic, and Income Items by Type of Bank and Census Tract, 2017

	Total Assets ($'000)	Number of Small-Business Loans	Small-Business Loans to Total Assets (%)	Tier 1 Capital to Total Assets (%)	Percentage of Total Population				Median Family Income ($)
					Minority	Hispanic	Black	Asian	
All FDIC-Insured Institutions	207,898	243	11.80	10.39	28.22	6.83	4.01	1.33	61,071
All MDIs	255,610	189	12.65	11.23	74.13	15.33	4.52	7.07	51,161
Black MDIs	165,908	159	19.26	9.22	80.93	1.34	64.97	1.67	39,415
Hispanic MDIs	473,262	254	8.31	11.17	89.77	82.52	1.74	1.22	49,699
Asian MDIs	329,774	146	13.43	11.74	74.63	17.20	5.33	36.99	51,607
Other MDIs	102,453	170	13.92	10.28	29.32	3.72	1.79	0.78	55,274

Source: FDIC and U.S. Census Bureau

Table 6b. Means for Selected Bank, Demographic, and Income Items by Type of Bank and Census Tract, 2017

	Total Assets ($'000)	Number of Small-Business Loans	Small-Business Loans to Total Assets (%)	Tier 1 Capital to Total Assets (%)	Percentage of Total Population				Median Family Income ($)
					Minority	Hispanic	Black	Asian	
All FDIC-Insured Institutions	2,959,908	4,558	12.80	11.62	37.61	16.67	13.57	4.54	67,966
All MDIs	1,305,490	487	15.30	12.15	67.82	28.35	14.10	20.38	60,784
Black MDIs	246,307	192	20.10	10.28	74.02	7.73	58.78	4.33	51,143
Hispanic MDIs	2,537,413	813	11.04	11.97	77.60	69.57	3.21	4.49	58,835
Asian MDIs	1,389,501	499	15.54	13.27	71.97	21.67	7.49	40.06	64,261
Other MDIs	141,753	224	16.63	10.77	34.74	5.30	7.33	1.68	59,404

Source: FDIC and U.S. Census Bureau

CONCLUSION

The findings of this report illuminate that MDIs, although small in scale, are positioned to be key funding sources for minority-owned small businesses, and therefore, important economic development engines.

One important finding from the paper is that where a limited number of MDIs exist (and where their branches are located), the ownership of the MDI often corresponds to the minority population of the relevant census tract. As discussed, this coupled with the assumption that minority ownership enables reduced levels of customer bias against similar minorities, minority small-business customers are interacting with a financial institution that is better suited to meet their needs in an equitable way. Due to the community-oriented nature of MDIs, they are more likely to recycle capital within their community of operation.

The findings from this paper highlight that MDIs allocate a higher proportion of their capital to small-business relative to non-MDI banks. The implication is that a potentially effective way to create economic development in minority communities would be to inject more equity capital into MDIs so that they can lend more to small businesses.

MDIs allocate a higher proportion of their capital to small-business relative to non-MDI banks and the implication is that a potentially effective way to create economic development in minority communities would be to inject more equity capital into MDIs so that they can lend more to small businesses.

To the extent that MDIs are more likely to use their capital in such a way, they become job-creation catalysts in underserved communities.

CONCLUSION

With a host of national policy initiatives seeking to address the lack of capital in low- and moderate-income communities, we suggest additional research into the opportunity presented by MDIs. While this report presents data on MDIs' inclination toward local small-business lending, assessing MDI capacity to serve as fulcrums of economic development in underserved communities requires an understanding of their operational capabilities. MDIs are small in the broader commercial banking context and are more susceptible to challenges associated with increasing compliance costs, operational complexity, and a fast-paced, technology-enabled market. Responsibly deploying more capital through these institutions, therefore, is inextricably linked to organizational transformation strategies.

Assessing MDI capacity to serve as fulcrums of economic development in underserved communities requires an understanding of their operational capabilities.

Determining the answers to the following questions is imperative to assessing MDIs' potential:

- What are the capital constraints of such institutions?
- How would MDIs react to more equity on their balance sheets?
- What additional capacity improvements—human and technological—are required for MDIs to increase both their scale and efficiency to ensure prudent activities in their communities?

The Milken Institute plans to explore these questions during the next phase of our program. In doing so, we hypothesize that MDIs will react positively to equity infusions and that they already have market understandings sophisticated enough to responsibly deploy higher levels of equity capital within their communities. Further, we believe that through a limited number of organizational transformations,

CONCLUSION

MDIs are well poised to dramatically increase their efficiency and profitability. Ultimately, we know answering these questions will reveal the best ways of supporting MDIs to reach their potential to serve as job-creator conduits within underserved communities.

The Milken Institute hypothesizes that MDIs will react positively to equity infusions and that they already have market understandings sophisticated enough to responsibly deploy higher levels of equity capital within their communities.

ABOUT US

ABOUT THE MILKEN INSTITUTE

The Milken Institute is a nonprofit, nonpartisan think tank determined to increase global prosperity by advancing collaborative solutions that widen access to capital, create jobs, and improve health. We do this through independent, data-driven research, action-oriented meetings, and meaningful policy initiatives.
The Center for Financial Markets promotes financial market understanding and works to expand access to capital, strengthen—and deepen—financial markets, and develop innovative financial solutions to the most pressing global challenges.

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