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Community Investment: It's Time to Get Serious

Good morning, and welcome. I'm Bob Parry, President of the Federal Reserve Bank of San Francisco, one of the co-sponsors of this conference on community investment. In the next day and a half, you'll hear a lot about the recent changes in the CRA and what they mean for community investment. For example, you're going to hear about CRA's new teeth -- that is, the tougher regulatory standards and the new requirement that CRA evaluations be disclosed publicly. You're also going to hear about how you can implement an effective CRA program. And you're going to hear about how community groups can act as watchdogs to improve access to financial services in low-income communities.

One message that should come through loud and clear in all the sessions you attend is that there is a renewed sense of urgency about community investment. The changes in laws and regulations governing lenders' obligations in this area have been more sweeping in the last 18 months than at any time since the CRA was passed in 1977.

So, today, what I'd like to do is step back a bit and ask, why now? Which is really another way of asking why we have the CRA at all, and why it's important to get serious about community investment. I believe there are four concerns that have led to the growing emphasis on the CRA.

First, there's a perception that even though the CRA is on the books, lenders still are not doing an adequate job of providing credit to low- and moderate-income neighborhoods. Many are concerned that this lack of credit in low- and moderate-income communities is stunting economic growth, limiting opportunities for advancement, and contributing to decay in these areas. This isn't a new argument, but it's taken on new force in light of the recent slowdown in the economy and the speculation that a nationwide credit crunch is partly to blame for the slowdown.

A second reason community investment has become so important is that the need for affordable housing has grown tremendously since the CRA was passed. In the past decade, the median price of housing in major metropolitan areas has risen nationwide, while the (real) income of the bottom *40 percent* of the population has declined. Indeed, the decade of the '80s was none too kind to the poorest households: their income declined 12.5 percent, compared to a 14.3 percent gain for the richest households.

And when you look at who's among the poorer households, it's clear that they're not only the unemployed. There are many so-called working poor who are priced out of housing. In the San Francisco Bay Area, for example, a family of four attempting to live on a starting teacher's salary would easily qualify as a low-income household.

A third factor that has led to the heightened emphasis on CRA is the increasing scarcity of public monies for community development. This is coupled with a growing belief that the government's efforts to solve the problem of neighborhood decay have been largely unsuccessful. So, it's no surprise that Congress and community groups have turned up the heat on the private sector as a source of capital for community investment.

A final consideration is that, whether you agree with the proposition or not, in the mind of the public, depository institutions share a public trust to meet the credit and financial services needs of all communities. This perception has grown stronger over time. It's been evident in the Congressional debate about the need for "lifeline" banking services, among other things.

For all these reasons, the obligation of lenders to reinvest in their communities has come under increased scrutiny in recent years. So have the regulators' efforts to enforce the CRA.

In March last year, the federal regulatory agencies published new guidelines to clarify what is acceptable performance under the CRA. The revised guidelines don't change the basic framework for evaluating that performance, but they do recognize that a successful CRA program now requires more than loans; a successful program also frequently involves familiarity with federal, state, and local assistance programs. It also usually involves the provision of low-cost checking accounts and a willingness to provide technical and administrative support to community development organizations.

The most important requirement for a successful CRA program, however, is top-management involvement. Without support from the top, community investment can never be integrated into an institution's decision-making and planning processes the way it needs to be. In this regard, I've been encouraged to see that more and more chief executives of the banks we supervise have become involved in developing and shaping their institution's CRA program.

The tougher compliance standards embodied in the revised CRA policy are one sign that financial institutions need to get serious about community investment. Public disclosure of CRA examination findings is another. As you know, following every examination conducted after July 1 of this year, the CRA rating and written evaluation must be made available to the public. Not only will this subject individual institutions to heightened public scrutiny, it will also subject the regulators to closer scrutiny. And you'd better believe we have an incentive not to allow grade inflation in our ratings!

Some of these ratings have come out already. None of them has caused much stir. Indeed, for most institutions, disclosure probably will be a non-event in the sense that their record is pretty good. At any rate, for every institution, the new policy offers the opportunity and the incentive to improve communications with community groups. Public disclosure of the CRA evaluation is one way to tell potential customers about the services and products your institution provides. This sort of communication should help to increase lenders' awareness of the needs of the communities they serve.

It also should help dispel some misconceptions about community-based lending. For example, some lenders seem to think that when there's very little lending going on in certain low- and moderate-income neighborhoods, there can't be any profitable lending opportunities in those areas. This sort of thinking reminds me of the joke about the guy who wouldn't pick up the 100 dollar bill he saw on the sidewalk; he figured that if it were genuine, it would have been picked up by someone else before he saw it.

Some lenders also seem to think that the CRA requires them to make loans only on concessionary terms. Community investment is not charity. Charity may be commendable in its own right, but it will never be sufficient to meet the need for capital in low-income neighborhoods. Loans made according to prudent underwriting standards are the backbone of a successful CRA program.

But I don't want to give the impression that a successful program is always easy or straightforward to implement. Sometimes it means rethinking delivery systems to make services more accessible. It may also mean working with inexperienced nonprofit developers. And it may mean redesigning tests of creditworthiness to take into account the needs and circumstances of a new and different clientele.

At times, it means finding more economical ways to underwrite and service relatively small loans. The California Community Reinvestment Corporation is an example of this. Forty-six of the state's banks formed the CCRC to provide long-term financing for low-income rental housing developments. CCRC has approved $53 million in loans during its first nine months of operation. Ultimately, it intends to find secondary market investors for its loans, so that its $100 million loan pool can be recycled many times over.

I'm proud to say that the San Francisco Fed played a role in seeing that the CCRC got off the ground. And we're now working with bankers to develop similar organizations in Hawaii, Nevada, and Washington.

The goal of the San Francisco Fed is to promote community investment by encouraging the establishment of such consortia, by sponsoring conferences like this one, by serving as a clearinghouse of information on community lending programs, and by publishing a quarterly newsletter on community investment issues.

Our Community Affairs staff also helps lenders identify market opportunities by preparing "Needs Assessment Reports" on selected metropolitan areas in the West. In these reports, we provide a review of the economic health of the targeted community, a description of its housing stock, the availability of banking, shopping, and other commercial services, as well as suggestions regarding ways lenders can help meet the community's need for financial services.

At the Federal Reserve Bank of San Francisco, we're serious about community investment. We want to help financial institutions and community groups work together to meet the needs for affordable housing and economic development, both urban and rural. Together, we can make our communities better places to live in. Improving our communities and helping them to prosper makes good business sense.

Now, I'd like to turn the program over to John Cardemone. John is Vice President of Credit Services at the Federal Home Loan Bank here in San Francisco -- the other co-sponsor of this conference. He will be moderating our program today. John, ...