

Bank Competition and Entrepreneurial Gaps: Evidence from Bank Deregulation

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Summary

Bank competition reduces gender and racial gaps in entrepreneurship by improving banking services and reducing discrimination:

- I take advantage of the legislative history of bank deregulation from 1994 to 2021 to construct the bank deregulation index
- Stronger bank competition increases the quantity and quality of banking services provided to minority borrowers
- I develop a direct measure of bank discrimination based on the narrative information extracted from the complaints filed to the Consumer Financial Protection Bureau (CFPB) using textual analysis. Using this measure, I find that bank competition reduces complaints about discrimination
- Bank competition reduces the entrepreneurial gaps by loosening the financial constraints of female and minority entrepreneurs

1. Motivation

- It is important to reduce pronounced and persistent gender and racial gaps in entrepreneurship
- The lack of startup capital has long been recognized as the most important factor impeding the success of minority entrepreneurs
- Entrepreneurial firms rely heavily on bank financing but female and minority entrepreneurs are more likely to be credit rationed by banks because of discrimination or bias
- It is hard to identify discrimination. Current methods to identify discrimination rely on the racial gaps in the interest rate and rejection rate, which suffer from problems of omitted variables.
- Theoretical foundation: Becker (1957) argues that competition eliminates discrimination

2. Bank Deregulation Index

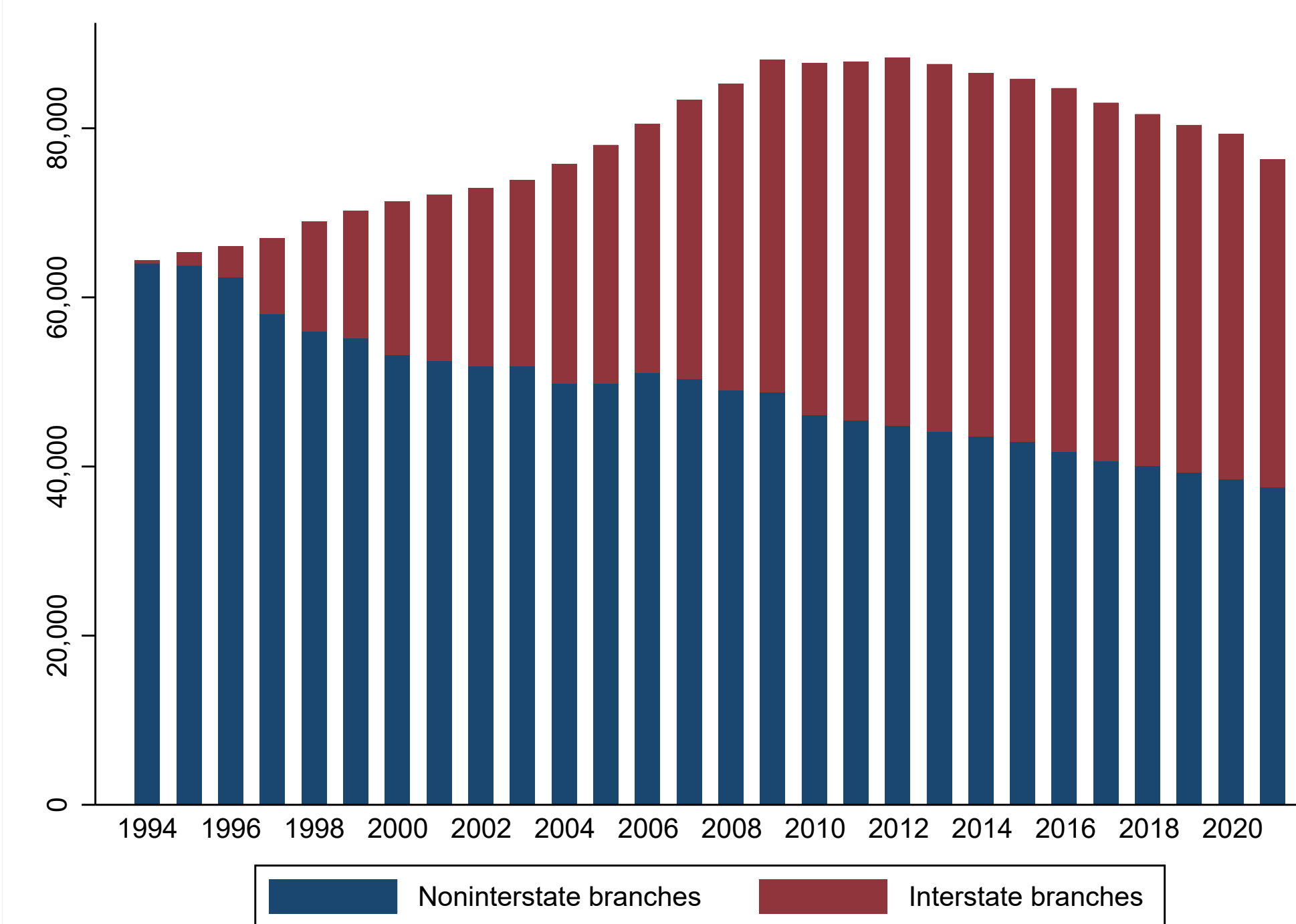
The Riegle-Neal Interstate Banking and Branching Efficiency Act (IBBEA) allows the following four restrictions:

- The minimum age requirement on target banks of interstate acquisition
- De novo interstate branching
- Acquisition of branches
- The deposit cap

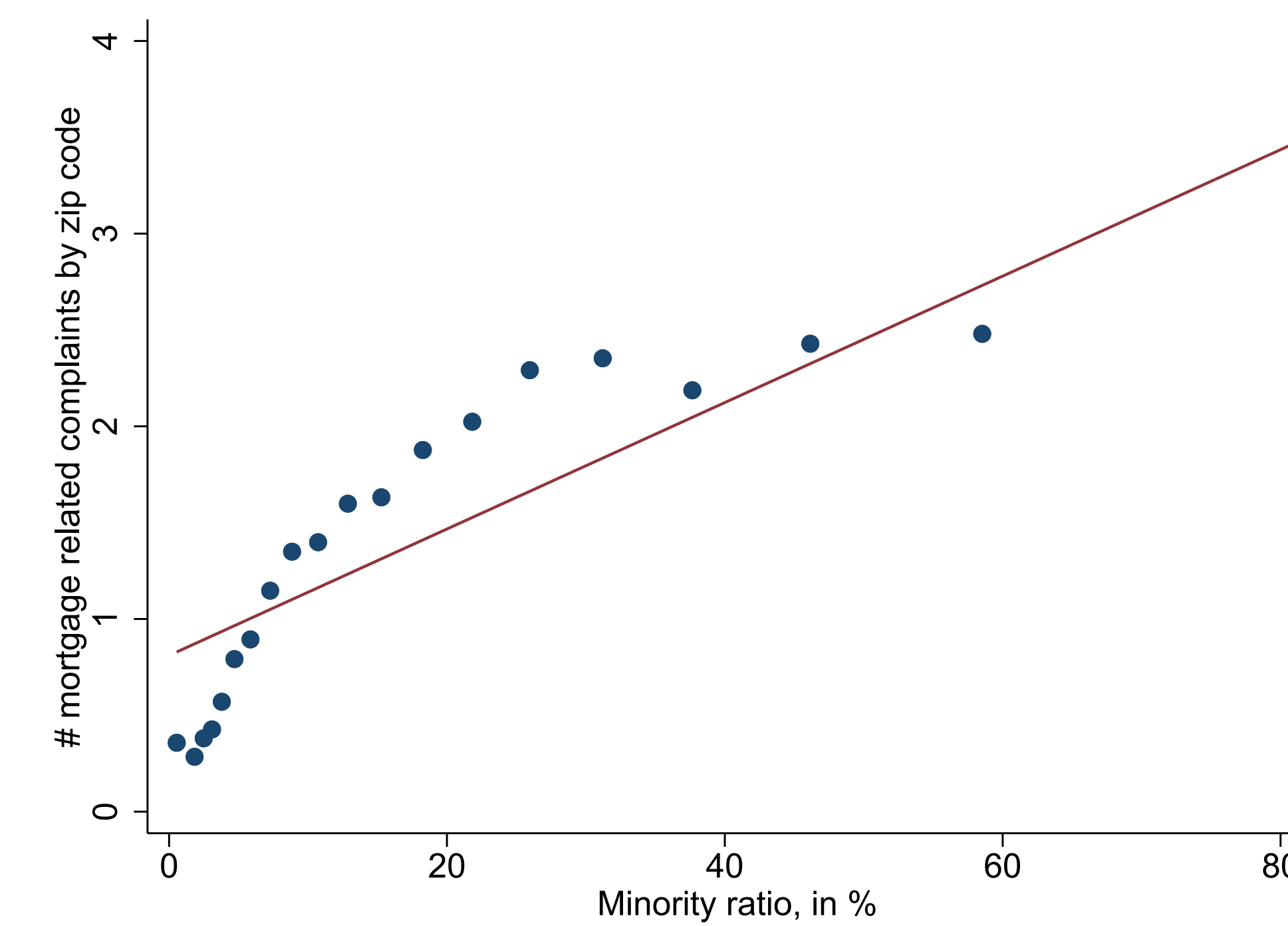
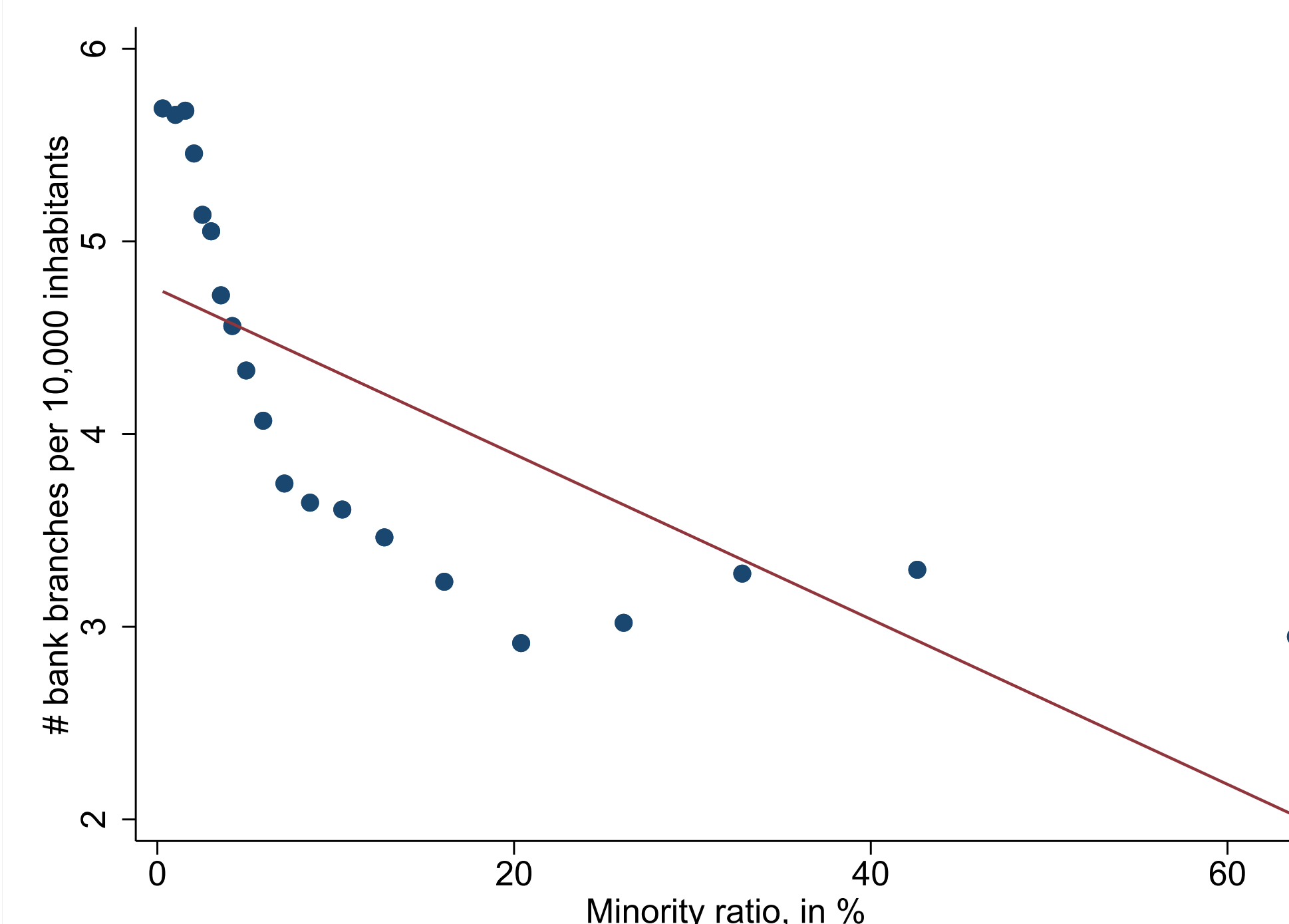
The Dodd-Frank Act:

- Removes de novo interstate branching restriction

Deregulation index = 4 - number of restrictions



3. Minority Borrowers Are Underserved



4. The Effect of Competition on Bank Services

- Competition increases the quantity of services

Log(branch density per capita)	(1)	(2)
Index × Minority	0.030*** (0.011)	0.029*** (0.011)
Controls	No	Yes
State × Year FE	Yes	Yes
County FE	Yes	Yes

- Competition reduces the racial gap in accounts

Holds a bank account	(1)	(2)
Minority	-0.133*** (0.014)	-0.055*** (0.011)
Index × Minority	0.019*** (0.005)	0.011** (0.004)
State × Year × Income decile FE	No	Yes
Sociodemographics	No	Yes

- Competition improves the quality of bank services

Log(complaints)	(1)	(2)
Index × Minority	-0.055** (0.024)	-0.054*** (0.019)
Control	Yes	Yes
Zip code FE	Yes	Yes
State × Year FE	No	Yes
MSA × Year FE	No	Yes

5. The Effect of Competition on Discrimination

	Log(discrimination) (1)	1(discrimination) (2)
Index × Minority	-0.028*** (0.007)	-0.040*** (0.008)
Control	Yes	Yes
Zip code FE	Yes	Yes
State × Year FE	Yes	Yes
MSA × Year FE	Yes	Yes

Discrimination: the narrative including the words “discrimination”, “unfair”, “inequity”, “prejudice”, “injustice” or other related words

6. The Effect of Competition on Entrepreneurial Gaps

Entrepreneur	(1)	(2)
Female	-0.022*** (0.002)	-0.030*** (0.001)
Minority	-0.014*** (0.002)	-0.022*** (0.002)
Index × Female		0.003*** (0.001)
Index × Minority		0.003** (0.001)
State × Year × Income decile FE	No	Yes
MSA × Year × Income decile FE	No	Yes
Sociodemographics	No	Yes

7. Additional Results

Bank competition reduces the gaps in:

- raised funding
- business performance and business equity
- access to the Paycheck Protection Program (PPP) loans

These effects are stronger in areas with high discrimination