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Consumer credit on American Indian reservations



Valentina Dimitrova-Grajzl ^{a,b}, Peter Grajzl ^{c,b,*},
A. Joseph Guse ^{c,b}, Richard M. Todd ^d

^a Department of Economics and Business, Virginia Military Institute, Lexington, VA 24450, USA

^b Federal Reserve Bank of Minneapolis, USA

^c Department of Economics, The Williams School of Commerce, Economics, and Politics, Washington and Lee University, Lexington, VA 24450, USA

^d Federal Reserve Bank of Minneapolis, Community Development Department, USA

ARTICLE INFO

Article history:

Received 26 March 2014

Received in revised form 12 September 2014

Accepted 8 January 2015

Available online 2 July 2015

JEL classification:

G21

P43

O16

R11

Keywords:

American Indian reservations

Consumer credit

Credit conditions

Credit usage

ABSTRACT

This paper provides the first encompassing quantitative picture of consumer credit in Indian Country. Drawing on a unique large-scale consumer credit database, we find that Equifax Risk Scores and the use of certain forms of credit, especially mortgages, are low on reservations. However, usage of other forms of credit on reservations is not always low. Moreover, the gaps in credit usage on versus off reservations differ significantly across states and can change notably over time. Among predictors of consumer credit outcomes, the percentage of American Indian residents is robustly negatively associated with favorable credit outcomes. Furthermore, once controlling for racial composition, the effect of an area's location vis-à-vis a reservation often becomes statistically insignificant. Other socio-economic variables are generally poor predictors of credit outcomes on reservations. State jurisdiction over legal matters is, at least on average, associated with favorable credit outcomes on reservations.

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* Corresponding author at: Department of Economics, The Williams School of Commerce, Economics, and Politics, Washington and Lee University, Lexington, VA 24450, USA.

E-mail addresses: dimitrova-grajzlp@vmi.edu (V. Dimitrova-Grajzl), grajzlp@wlu.edu (P. Grajzl), gusej@wlu.edu (A.J. Guse), dick.todd@mpls.frb.org (R.M. Todd).

1. Introduction

American Indian reservations are “islands of poverty in a sea of wealth” (Anderson and Parker, 2008, p. 641) and “America’s domestic emerging market” (Clarkson, 2009, p. 287). A comprehensive explanation of why all but a few reservations are economically underdeveloped remains elusive (Anderson and Parker, 2008). Among the many potential barriers to economic growth and prosperity on the reservations, undersupply of consumer credit has been a particularly pervasive concern.

In 2001, the Native American Lending Study (Community Development Financial Institutions Fund, 2001), relying on a one-time survey and interviews with experts, expressed widespread views that a general lack of capital and financial services impedes economic opportunity on American Indian reservations. The study reported frequent difficulty in obtaining mortgages and using land as collateral; a dearth of financial institutions located on or near reservations; discrimination against or stereotyping of American Indian borrowers; lack of understanding by reservation residents of credit standards and credit reports; limited or poor credit histories among reservation residents; high loan default rates among reservation residents; and significant need for personal finance education on reservations.¹ Similar concerns about credit on reservations were voiced during a series of recent “Growing Economies in Indian Country” workshops held by the Federal Reserve System and several federal agency partners (Board of Governors of the Federal Reserve System, 2012).

Despite these persistent concerns, our knowledge about credit on reservations remains highly incomplete. Data on consumer credit conditions on reservations are particularly scarce (Todd, 2012). An exception is data on mortgage credit, due to the availability of the Home Mortgage Disclosure Act (HMDA) data. The HMDA dataset, however, has noteworthy limitations, such as incomplete coverage in rural areas and the imperfect match of Census tract and reservation boundaries. Comparably extensive data on the use of other forms of consumer credit on reservations have simply not been available up to this point.²

This paper contributes to the sparse existing empirical literature on credit in Indian Country (Cyree et al., 2004; Laderman and Reid, 2010; Parker, 2012; Angadjivand et al., 2012) by providing a first encompassing empirical characterization of consumer credit on American Indian reservations.³ What are the basic patterns in consumer credit usage and conditions on versus off the reservations, across states, and over time? How do credit outcomes vary with demographic, socio-economic, and institutional factors? To address these questions, we draw on a unique and in the context of Indian Country thus far unutilized large-scale sample of consumer credit histories: the Federal Reserve Bank of New York/Equifax Consumer Credit Panel (CCP).⁴ There are three major advantages of the CCP dataset over previously used datasets for examining credit in Indian Country. First, the CCP dataset provides information for mortgage and non-mortgage loans, enabling us to fill a gap in the existing literature on consumer credit in Indian Country, which has focused primarily on mortgage loans (see, e.g., Cyree et al., 2004; Laderman and Reid, 2010). Second, CCP records include Census block codes, allowing us to use Census geographic data to determine whether credit files originate from reservations, areas adjacent to reservations or other nearby areas. The stratification into these geographic groups allows us to analyze patterns in consumer credit on and off reservations in a cross section as well as over time. Third, the Census block codes allow us to link the CCP data with the corresponding demographic and socio-economic data from the Census as well as with information on the allocation of jurisdiction over legal matters, which has been suggested to affect credit (Anderson and Parker, 2008; Parker, 2012), and on the proximity of financial lending institutions.

¹ Other smaller-scale studies provide further evidence of significant use of high-cost consumer credit products (Smith, 2003; Pickering and Mushinski, 1999), limited access to banks and formal credit, real or perceived discrimination (Pickering and Mushinski, 1999), and high mortgage denial rates on reservations (Schumacher, 2006).

² A small sample of American Indian consumer credit histories was also analyzed in a 2007 “Report to Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit” (Board of Governors of the Federal Reserve System).

³ Other studies about credit in Indian Country, which either maintain a narrower focus or are primarily descriptive in character, include Listokin (2001), Pickering and Mushinski (1999), Manchester (2001), Jorgensen (2004), and Angadjivand et al. (2012).

⁴ In a new and ongoing project, Brown et al. (2014) follow our lead and draw on the CCP dataset in a subset of their analysis of the impact of credit on economic activity on reservations.

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