Improving the Economy of Distressed Communities
By Byron A. Ellis – February 06, 2019

For decades, distressed communities struggled to obtained credit from private banks.

Without significant influx of credit, economically distressed communities will remain poor. The nonprofit Economic Innovation Group indicated that more than 50 million Americans live in economically distressed communities. Florida and Bendix mapped the most distressed communities in the United States and noted that "In the average distressed ZIP code, around 25 percent of adults lack a high school diploma, and a whopping 55 percent are not working."

Lack of schooling and jobs leads to economically distressed communities. However, schooling and jobs are a function of the influx of funds or access to bank credit by firms, entrepreneurs and consumers. Influx of investments or bank credit lead to purchasing power, economic growth and rising standards of living.

Money circulating through communities creates demand for goods and services, as well as jobs, increased individual and community income and physical capital expansion; new factories, homes and quality schools.

Often, private bank credit is not available for investments in distressed communities, such as Appalachia and Central Cities. Many private banks seldom adhere to the Community Reinvestment Act (CRA) of 1977; they have long ignored the credit needs of distressed communities and have red-lined them.

The lack of funding decapitates capital expansion or upgrading of existing physical assets and negatively affects employment and living standards of distressed communities.

Ensign and Tracy noted that when Steven Mnuchin wanted to sell his OneWest Bank for $3.4 billion in 2014, community groups opposed the sale based on CRA of 1977. They noted that Mnuchin is the Treasury secretary and his fellow executive at the bank, Joseph Otting, is now comptroller of the currency. And one of their big agenda items is an overhaul of the CRA, a law passed to combat redlining, a practice where private banks provide credit in distressed communities.

Many economists and politicians believe that it is household savings that creates investments and hence place blame on the residents of distressed communities for their living conditions. However, high savings by consumers implies lower consumption levels and less investments by firms and entrepreneurs. Furthermore, high savings rates were not the reason for the economic successes in Germany and China; both, embarked on the growth process without any net capital exports.

When banks lend to firms, entrepreneurs and consumers, they create bank money out of thin air (ex nihilo). Firms, entrepreneurs and consumers use the loaned money to purchase capital and non-capital goods, to hire employees, to expand and upgrade capital stock.

It is through the credit channel that aggregate household income, savings, consumption and employment increases. Moreover, with increasing community income, firms and entrepreneurs' profits and savings increases.

Private banks often stymie the growth process in distressed communities by not lending to firms, entrepreneurs and residents. Domar in his 1947 "Expansion and Unemployment" paper argued that rising employment is contingent on increases in real income and it is credit that increases income.

Credit to firms, entrepreneurs and consumers is necessary to improve economic conditions in distressed communities. In the absence of private bank credit, distressed communities must demand from their politicians at all levels, state, county or city, to establish public banks.

The Bank of North Dakota (BND) is a public bank, established 100 years ago due to the exploitation of North Dakota farmers by private banks. It fulfills financial needs underserved by the private banks. BND is a major factor in North Dakota's economy.

A government body and not private investors control and principally funds public banks, they are an extension of the entity that created them, state, county, or city governments. The entity deposits all its revenue, taxes, fees, and other earnings in the bank and can borrow from it.

Distressed communities should follow North Dakota's example and launch a Nonpartisan League to pressure their public officials to establish a public bank that provide credit to distressed communities in their state, county or city. Additionally, they should set up local credit unions that can provide credit to people of small means for provident purposes.

The first credit union was in Belgium in 1848 during a period of severe economic depression. The ability to pool savings in a federal credit union would be advantageous to residents of distressed communities, if the credit union money turnover rate in the community is high. The Federal Credit Union Act established an administrative structure within the federal government for the supervision of federal credit unions.

Distressed communities can increase community employment by ensuring capital influx and money creation by financial institutions within their communities and the two viable institutions are credit unions and public banks.