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

For decades, distressed communities struggled to obtain credit from private banks. In the absence of private bank credit, distressed communities must demand from their politicians at all levels, state, county, or city, the establishment of public banks, such as The Bank of North Dakota.

Without a 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. An influx of investments or bank credit leads 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, as well as 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 and upgrading of existing physical assets and negatively affects employment and living standards in 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 the 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 household savings create investments and blame residents of distressed communities for their living conditions. However, high savings by consumers imply lower consumption levels and fewer investments by firms and entrepreneurs. According to Dullien, high savings rates were not the reasons for the economic successes in Germany and China; both embarked on the growth process without any net capital exports; they relied on strong credit creation.

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 add value in the production processes, to expand and upgrade the capital stock.

Through the credit channel, aggregate household income, savings, consumption, and employment increase. Moreover, with increasing community income, individuals, firms, and entrepreneurs' profits and savings also increase.

Private banks often stymie the growth process of 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 the economic conditions of 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 the financial needs underserved by 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 provides 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's 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 two viable financial institutions are credit unions and public banks.