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UNBANKED BY CHOICE:

A look at how low-income Los Angeles households manage the money they earn



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UNBANKED BY CHOICE:

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EXECUTIVE SUMMARY

American families without a bank account live in a dangerous financial world.¹ Lacking access to government-insured savings or opportunities to build credit, they not only incur risks of theft, fraud and loss, but by using alternative financial service (AFS) providers such as check cashers or payday lenders, they also become prey to expensive predatory products and services that make it harder for them to achieve financial security. Prior research by the Pew Health Group (PHG) on California families confirms the widely shared view that having a bank account generally provides access to basic financial services at a lower cost than using AFS.²

To reduce these risks and costs, PHG's Financial Security Portfolio has helped unbanked households open a safe and affordable bank account as the first step in joining the financial mainstream. The PHG Safe Banking Opportunities Project provided research and technical assistance to help more than 50 cities and localities kick off "Bank On" programs that bring together banks, local government and community groups to promote responsible bank account ownership. More recently, we investigated the products and services that banks might provide to attract and serve more unbanked individuals.³

In 2009, we began an in-depth study of the financial behaviors of similarly situated unbanked and banked low-income families to inform policy solutions that would bring more Americans into the financial mainstream. This is the first report from a multi-phase survey of 1,000 banked and 1,000 unbanked households in greater Los Angeles, randomly selected from eight low-income study areas for in-person interviews at several intervals over the course of a year (July 2009 to July 2010). Our findings from the first wave, or phase, of this study suggest several policy directions for further investigation to help unbanked families shift to the safer world of the banked. The data shows different patterns of financial behavior between the Banked and the Unbanked in our study. Moreover, it reveals that the Banked and Unbanked further

segment into distinct sub-groups based on their usage of financial services and providers: a banked only group, a cross-over group that has bank accounts but also uses AFS, an unbanked AFS-only group, and an unbanked cash economy group that uses cash only.

Banked Only: households with at least one bank account that use banks for all financial services and transactions.

Cross-Over: households with at least one bank account that regularly use non-bank providers for some financial services or transactions (sometimes popularly referred to as "underbanked").

AFS Only: households that do not have a bank account and rely on non-bank alternative financial service providers for financial services or transactions.

Cash Economy: households that do not have a bank account and conduct all their financial dealings in cash.

We found some demographic differences between the two groups. The banked respondents in our study are older (40 years) on average than their unbanked counterparts (34.5 years). Both types of respondents are likely to be foreign born (65% for the Banked and 69% for the Unbanked), but each has resided in the United States for many years (21 years on average for the Banked, 14 for the Unbanked). Members of both groups tend to be employed in similar non-technical professions and have similar unemployment rates (12–13%), but the Banked earn higher wages and salaries (an average of \$29,400 annually compared to an average of \$17,300 for the Unbanked). With average family sizes of 4.4 and 4.7 persons, respectively, this puts the Banked just above the federal poverty line, and the Unbanked below it. Close to two-thirds of the Banked (60%) have completed high school, compared to less than half (48%) of the Unbanked (Appendix A).

SUMMARY OF FINDINGS

- **Having a bank account correlates with saving.** All the neighborhoods surveyed are low income. Still, more than twice as many Banked (24%) as Unbanked (11%) report they are earning enough to pay their bills *and* save for the future. The Banked are more likely to save no matter what form their income takes—direct deposit, check or cash. About half of all surveyed, Banked or Unbanked, are making enough to pay bills but not to save.
- **How workers are paid strongly influences banking status.** Direct deposit requires a bank account, but payment by check also strongly correlates with being banked. The Unbanked are twice as likely as the Banked to be paid in cash on their primary job.
- **The low-income Banked maintain long-term banking relationships.** More than two-thirds have been banked five years or more, overwhelmingly with a single institution. Forty percent have been banked more than 10 years. Being charged fees without explanation is the major reason cited by the Banked that would cause them to leave their current bank.
- **About one-third of the Banked also use AFS.** Sixty-three percent of the banked population uses banking institutions exclusively, while the rest turn to check cashers, supermarkets, liquor stores and other AFS providers in addition to banks. Of these cross-over, or “underbanked,” users, 78% use AFS services at least once a month.
- **Most Unbanked have never had a bank account.** Nearly two-thirds (63%) of unbanked respondents in this study have never had a bank account. Almost one-quarter of the Unbanked (22%) previously had an account, but later opted to close it and remain unbanked. Some Unbanked (9%) previously had an account, but say they cannot now qualify for one.⁴ Three percent of those unbanked in the United States had bank accounts in another country.
- **Many of the Unbanked conduct their financial transactions exclusively in cash.** Almost one-third (29%) of the surveyed Unbanked exist in the cash economy. As discussed below, we conservatively estimate there are at least a million unbanked persons in the Los Angeles Metropolitan Statistical Area (MSA), making the cash economy segment some 300,000 strong. The other two-thirds of the Unbanked rely on AFS providers for financial transactions.
- **Members of the cash economy segment “save” by remitting.** Even though the Banked earn more on average than the Unbanked, those in the cash economy group send as much or more money to their families abroad each month than the Banked, while those in the AFS-only group remit the least on average.
- **All respondents tend to like and trust the financial provider they have.** The Banked are not more satisfied than the Unbanked. Those in the cash economy segment trust banks more than AFS providers, though they use neither. Most of these respondents, particularly Latinos, do not place high trust in credit unions.

INTRODUCTION

Through research and advocacy, PHG's Financial Security Portfolio helps American families gain access to safe and affordable financial products and services that empower them to manage their money, pay their bills and develop a credit rating. Our latest and ongoing effort, a multi-phase survey of 1,000 banked and 1,000 unbanked households in greater Los Angeles, examines the financial behavior of these two groups at a level of detail not previously attained.

The objectives of this study are:

- ***To identify and measure the financial service needs, perceptions and behaviors of low- and moderate-income households in specific neighborhoods of Los Angeles.***

This new data will fill a gap in knowledge about the potential of this population to actively utilize bank accounts and financial products and services. Our findings in this study to date demonstrate that market opportunities do exist, but that there are significant barriers to market growth. Such information can help banks and credit unions develop effective products and services to serve the unbanked and "underbanked" communities.

- ***To inform and evaluate the efficacy of publicly-led programs to "bank the unbanked," especially Los Angeles' Bank On programs, which aim to connect qualified unbanked households to specific banking opportunities.***

Half of the households interviewed in the study are in communities that have been targeted by a "Bank On" campaign, and half are in socio-economically similar communities that have not been targeted. In this study's final wave, now in the field, survey takers will assess the impact of these programs.

- ***To provide a basis for policy solutions on a local, state or national scale.*** Just as this data can help financial institutions provide for traditionally underserved sectors of the community, it can also help policy makers identify legislative or regulatory changes that support safer and more accessible banking products and services. Such changes could open regulated financial institutions to more Americans, providing them safer and more affordable contexts for building savings, credit and wealth. The survey reveals the need for policy intervention and suggests the benefits that proactive initiatives could confer not only for these populations but for society at large.

Study Design

For this study, we selected a set of eight low-income neighborhoods in the City of Los Angeles representing a mix of banked and unbanked residents. The City previously had selected four of these areas as targets for the Bank On Los Angeles campaign because research had shown that they had a high percentage of unbanked households. We added to the study four other neighborhoods with similar socio-economic traits that were not targets of Bank On Los Angeles, enabling us to measure, among other things, the effect of that campaign. We also factored in whether the neighborhood had previously been the subject of industry or non-profit study yielding additional data that we can use to corroborate our findings or put them in context. Maps of the study areas may be found in Appendix D.

While all eight study neighborhoods are low income, they are geographically and ethnically diverse and represent a variety of economic segments of Los Angeles. Some of the neighborhoods have a long history of red-lining and disinvestment; others are dynamic immigrant enclaves; others are underutilized urban spaces experiencing gentrification pressures; and others are stable, working-class communities. In selecting these study areas, we attempted to represent not only a sample of Los Angeles' low-income neighborhoods but also a sample of America's low-income population.

In these eight neighborhoods, we conducted a door-to-door survey of households chosen through a random sampling protocol. Respondents were targeted to represent 1,000 unbanked households and 1,000 households with at least one bank account. The methodology (detailed later in this report) was designed to reach a population that is often missed by conventional telephone or online surveys and to gather a depth of data that phone or online surveys cannot. We began the first wave of the survey in July 2009. To discern trends or changes of financial behavior over time, we are resurveying the same households with a second wave that was fielded starting in May 2010 and will be completed by July 2010, with a report to follow later this year.

The study compares the banked and unbanked groups across several categories, including financial behavior, economic status and perceptions of the financial service industry. We divided the banked

population into two subgroups: households using only mainstream banks or credit unions (“banked only”) and households that regularly supplement their financial transactions with alternative financial services. Members of the latter population are often referred to as “underbanked;” we prefer to call them “cross-overs.” We also divided the unbanked population between households that transact with AFS providers like check cashers but not with banks (“AFS only”) and the sizeable population of households that operate exclusively with cash (“cash economy”). Unbanked individuals who previously had bank accounts were also identified for analysis (“previously banked”). By digging into the financial patterns of these sub-segments, we were able to develop a more nuanced and complete picture of banking behaviors in low-income neighborhoods.

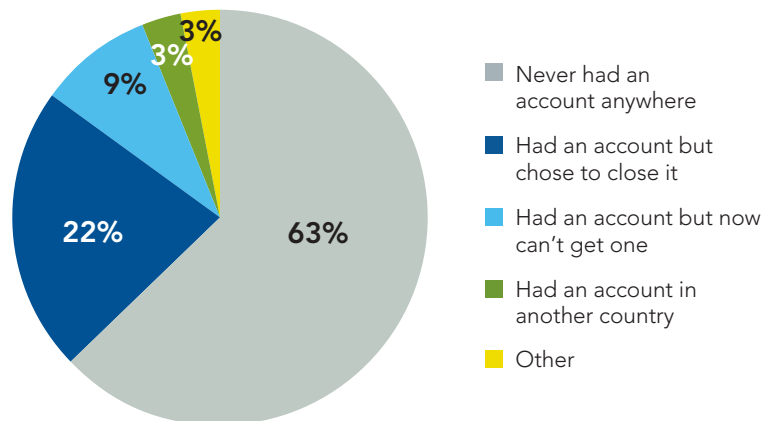
There are few similarly detailed studies of other parts of the country to which these findings can be compared.⁵ However, we can contrast the results of this study with those of nationwide surveys of the Banked and Unbanked, including a recent study by the Federal Deposit Insurance Corporation (FDIC) with estimated data on the unbanked populations

for the Los Angeles–Long Beach MSA.⁶ Those comparisons suggest that prior nationwide surveys do not exaggerate and if anything understate the extent to which Angelenos are unbanked, use AFS services or live in the cash economy. For example, the FDIC study estimates that in Los Angeles, 25% of the unbanked population uses only cash; the PHG survey confirms that the cash economy segment is 29% of the unbanked population in the survey neighborhoods. In our next report, we will place the longitudinal findings of the survey in a larger context that might help refine local, state and national understanding of the financial behavior and needs of society’s urban, low-income sectors.

Additionally, our findings may have specific implications for other locations with large immigrant populations.⁷ Although our foreign-born survey respondents have been in this country over 17 years on average, a large percentage of them remain outside of the American financial mainstream. The picture that has begun to emerge in this study could represent the future of Atlanta, Raleigh or other cities with growing immigrant populations. Thus, our policy recommendations may have particular relevance for these localities.

FIGURE 1

ACCOUNT HISTORY OF THE UNBANKED



SURVEY QUESTION: You said you do not currently have any accounts at a bank or credit union. Which one of the following statements best describes you?

SURVEY BASE: Total unbanked respondents, N=1,021

KEY FINDINGS

WHO ARE THE UNBANKED?

- Most of the Unbanked have never had a bank account.** Almost two-thirds of unbanked individuals in our survey (63%) have never had a bank account. Thus, they constitute an untapped market for banks. More than one-fifth (22%) of the Unbanked who have had accounts have voluntarily left the mainstream banking system, indicating a high level of customer dissatisfaction. Some of the Unbanked (9%) were expelled from their banks and are now unable to get an account. Only 3% of those unbanked in the United States were banked in another country (Figure 1).
- About two-thirds of the Unbanked use AFS exclusively.** The most popular AFS service for this group is bill payment (74%). A smaller, but substantial group (40%) uses check-cashing services. Other common transactions at Los Angeles' AFS providers by the Unbanked include purchasing prepaid calling cards (56%) and money orders (51%).
- Nearly one-third of the Unbanked use cash only.** Fully 29% of the surveyed Unbanked live and transact without the assistance of a bank or an

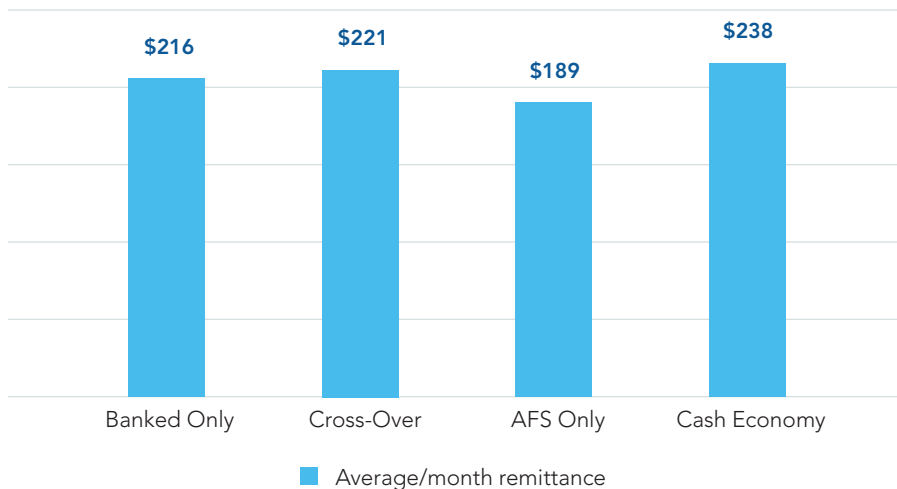
AFS provider, making the cash economy segment in Los Angeles' neighborhoods even larger than previous national, state or regional estimates.⁸ Given the size and demographics of the overall Los Angeles market,⁹ this suggests that hundreds of thousands of Angelenos live "off the grid" of the mainstream economy.

- The cash economy remits more than any other sub-segment, despite having the lowest incomes.**

Most unbanked households live below the federal poverty line, with a median annual income between \$10,000 and \$14,999 for a typical family of five. Unbanked households purchase less housing and amenities than their banked counterparts, but the cash economy segment sends similar or greater amounts of money to their families in other countries than the banked segment. Remittance services to send money overseas continue to be highly used in Los Angeles by both banked (29%) and unbanked (33%) residents. Average monthly remittance amounts range from \$189 (AFS only) to \$238 (cash economy) per transfer. Members of the cash-only segment make the highest average monthly transfer, sending nearly \$50 per month more abroad than their unbanked counterparts who use AFS (Figure 2).

FIGURE 2

REMITTANCES BY SEGMENT



SURVEY QUESTION: Approximately how much money do you send to family or friends in a typical month?

SURVEY BASE: Total banked remittance respondents, N=250, Total unbanked remittance respondents, N=333

WHO ARE THE BANKED?

• **Banked families are more financially secure.**

While all these respondents are low income, banking correlates with a somewhat increased income. The Banked have a median annual income range between \$15,000 and \$24,999, while the Unbanked have a median annual income range between \$10,000 and \$14,999. The average estimated monthly expenditures for Banked households is \$1,712, whereas for Unbanked households it is \$1,329, for families averaging 4.4 and 4.7 persons, respectively.

• **More of the Banked save than the Unbanked.**

More than twice as many banked (24%) as unbanked (11%) respondents report they are earning enough to pay their bills and save for the future. About half of all surveyed, Banked or Unbanked, say they are making enough to pay bills, but not to save. The Unbanked say they “cannot make enough money to pay their bills” at a higher rate (38%) than the Banked (27%) (Figure 3). Among the Banked, nearly all (91%) safeguard at least some of their cash savings in a bank. Nearly half (47%) keep all of their savings in a bank. The survey did not ask where the Unbanked keep their savings.

• **The Banked are loyal bank customers who consume a variety of bank services.** More than 80%

of the Banked patronize a single financial institution. Their banking relationships are long term: 40% have been banked more than 10 years, 69% have been banked for five years or more and 88% have been banked more than one year (Appendix B). They regularly use an average of five products or services, including ATMs, debit cards, checking accounts, check-cashing services (at either a bank or AFS provider) and savings accounts (Figure 4). Roughly one-third (34%) of bank customers in the study’s low-income markets use credit cards, less than half the national average (73%).¹⁰ Those in the cross-over sub-segment also are apt to use money order and remittance services.

• **Many of the Banked also use AFS regularly.**

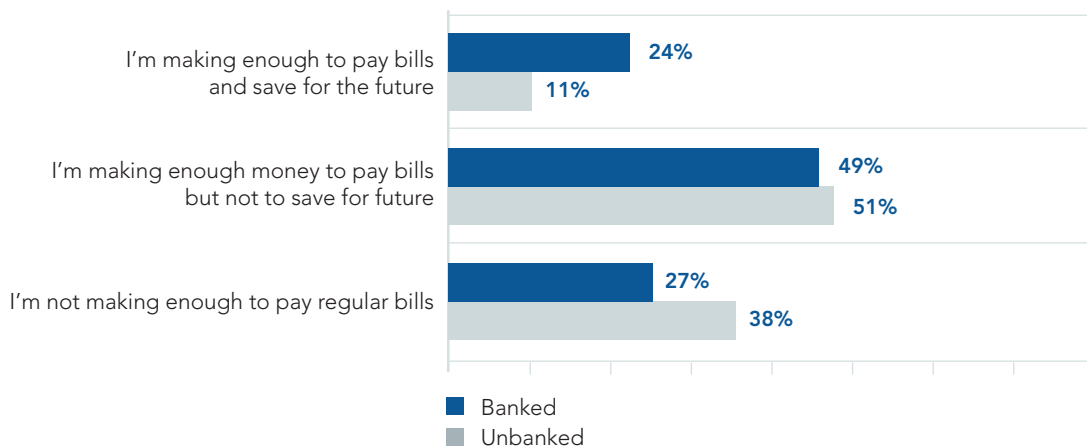
Over one-third (37%) of the Banked willingly and regularly use AFS to supplement banking services. Our findings suggest that this cross-over segment is substantially larger in low-income Los Angeles neighborhoods than prior national, state or regional estimates indicate.¹¹ Most of the cross-over segment (78%) use AFS at least once a month, most often (15%) for cashing checks.

• **Even if paid in cash, banked persons are more likely to save.**

If paid in cash, 88% of the Unbanked will spend with no intent to save. Among banked individuals paid in cash, however, 41% will deposit some or all of the wages into a bank (Figure 9).

FIGURE 3

PERCEPTIONS OF PERSONAL FINANCIAL HEALTH



SURVEY QUESTION: Which of the following best characterizes your financial situation?

SURVEY BASE: Total banked respondents, N=1,000, Total unbanked respondents, N=1,021

WHAT CAUSES A HOUSEHOLD TO BE BANKED OR UNBANKED?

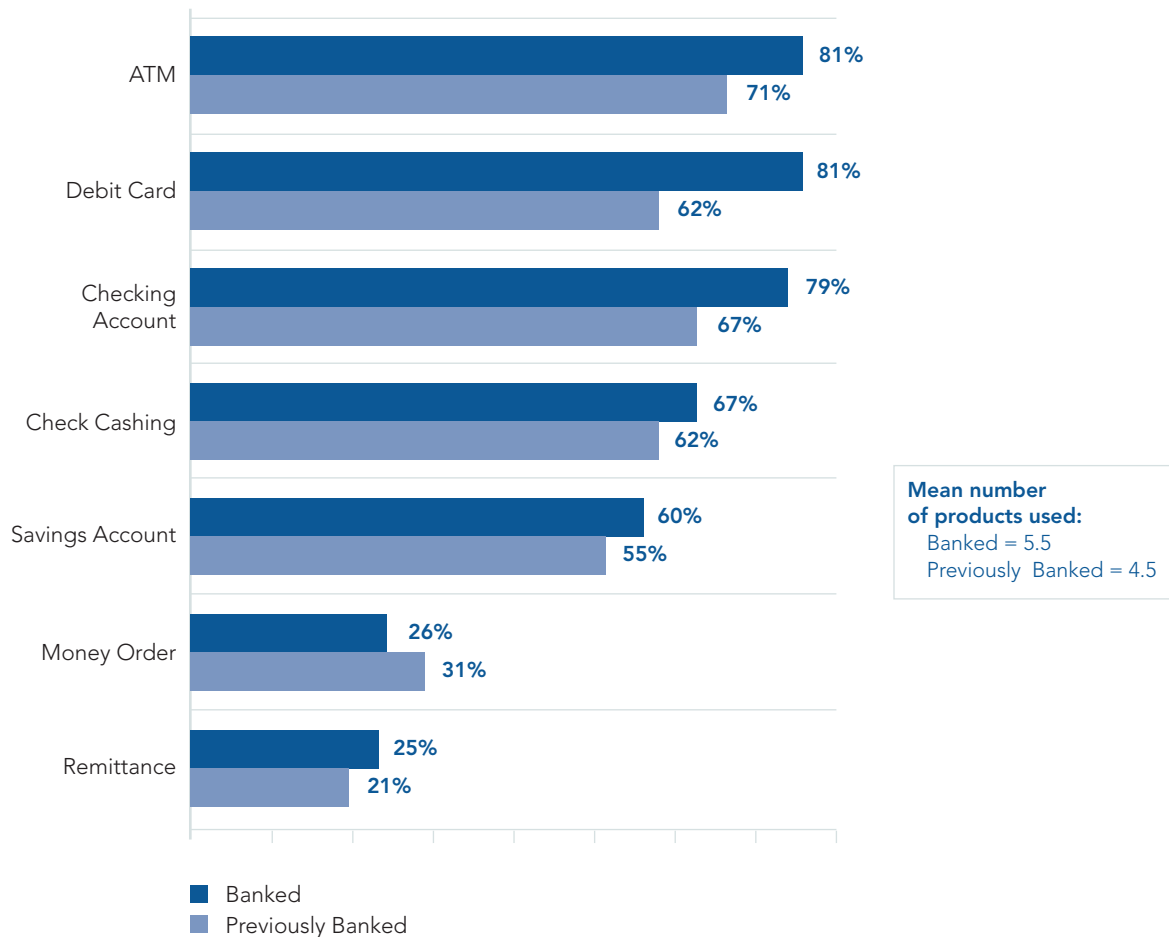
- **Form of household income is a significant indicator of banking status.** Bank accounts strongly correlate with non-cash payments from employers. Direct-deposit payment requires the recipient to maintain a bank account, but payment by check also strongly correlates with being banked. The Unbanked are twice as likely to be paid wages in cash as the Banked. Among the Unbanked, 40% are paid in cash on their primary job (Figure 5).¹² In the banked-only group, 19% are paid in cash;

the remainder are paid by check (75%) or direct deposit (28%). Those in the cross-over group are generally paid via check (72%) or direct deposit (25%). AFS-only users avoid direct deposit but are typically paid by check (64%). Cash economy respondents are most often paid in cash (53%) or with checks that they cash through friends, family or unlicensed third parties.

- **Low-income consumers choose a financial service provider largely on the basis of physical convenience (Figure 6).** The main reason by far for selecting a financial institution is geographic proximity (i.e., “located close to where I work or live”). The vast

FIGURE 4

PRODUCT/SERVICE USAGE (BANKED)



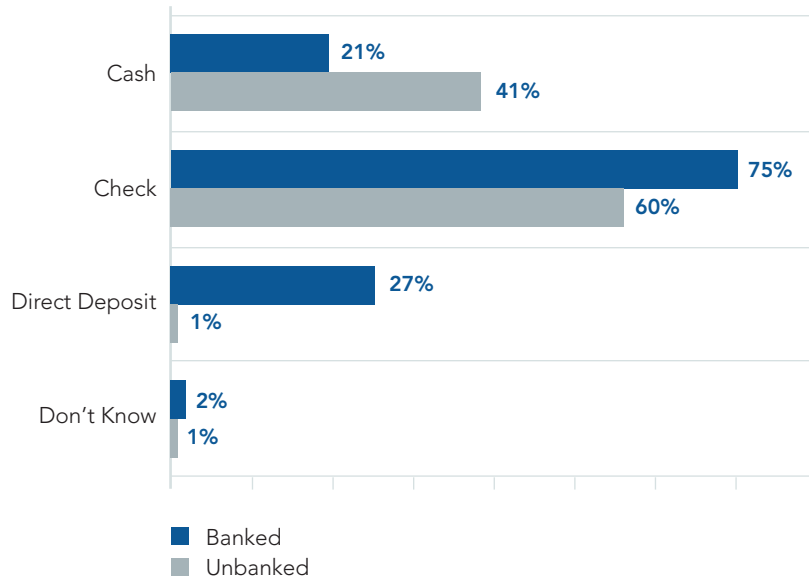
SURVEY QUESTION: Which of the following types of financial products or services do you currently have or use at a [bank or credit union/at any institution]?

SURVEY BASE: Total banked respondents, N=1,000, Total unbanked/previous banked respondents, N=313

FIGURE 5

FORM OF HOUSEHOLD INCOME

(See Endnote 12)



SURVEY QUESTION: How are you paid in each job? Is it by cash, check or direct deposit to your bank?

SURVEY BASE: Total banked respondents, N=459, Total unbanked respondents, N=356

FIGURE 6

PRIMARY REASON FOR USING PARTICULAR FINANCIAL INSTITUTION

	Banked	TOTAL		Unbanked (ASF)	TOTAL
Located close to where I live/work		60%	Located close to where I live/work		84%
Has a lot of branches		27%	Open at convenient hours		16%
Has environment I feel comfortable in		19%	Environment		15%
Has employees who speak my native language		17%	Close to where I shop		13%
Recommended by family/friends		13%	Has employees who speak my native language		10%
Bank offered me free checking		13%	Better customer service		9%

SURVEY QUESTION: Thinking of the [financial institution] you are currently using, what were your reasons for selecting this [financial institution]? Select all that apply.

SURVEY BASE: Total banked respondents, N=1,000, Total unbanked AFS respondents, N=386

majority (85%) of unbanked AFS users will patronize a provider because it is nearby; about two-thirds (64%) use a check-cashing service within walking distance. Likewise, most of the Banked (60%) use a particular branch because it is nearby. One-third (33%) patronize a bank or credit union within walking distance, and 82% within a 10-minute drive.

- **Members of the cross-over group favor financial services providers who speak their language.** Almost one-quarter of the cross-over segment (22%) say that whether bank representatives can transact in their native language is the primary factor in choosing a bank.
- **Hours of operation also affect choice of financial service provider for the cross-over segment.** Among the cross-over segment, 40% of respondents were “very likely” to switch to a financial institution that was open in the evenings or on Sundays. These preferences for immediate access nearly matched those achieved by account-based tactics for shifting bank relationships, such as lowering rates, fees or minimum balances.

- **Respondents who use a financial services provider—whether a bank or an AFS—tend to like and trust the type of provider they have.**

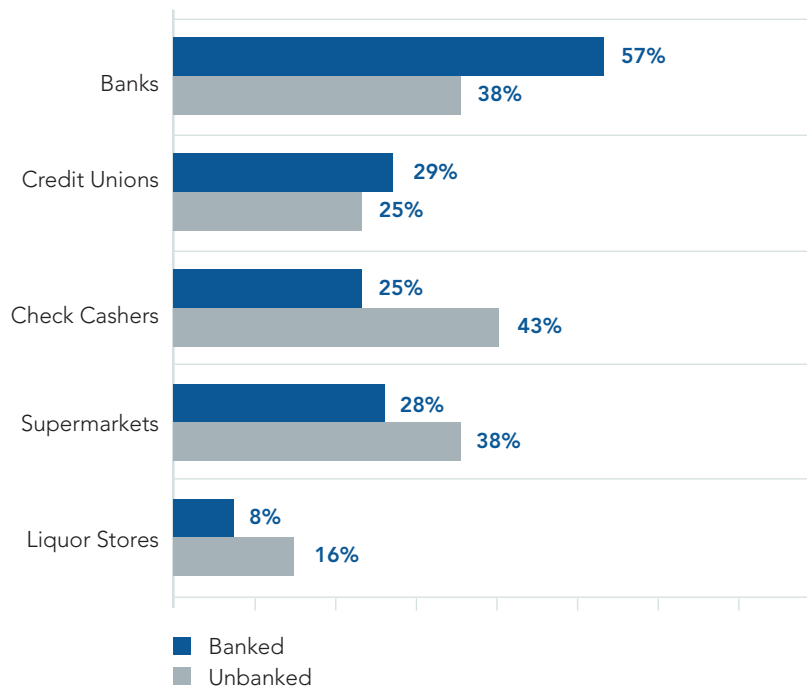
The Banked and the Unbanked express equally high satisfaction with their current financial service provider and distrust the type of provider they do not patronize (Figure 7). (Among Latinos, who comprise a majority of our survey population, neither the Banked nor the Unbanked have high trust in credit unions.) However, when it comes to courting the cash economy segment, banks have an advantage. While the AFS only sub-segment, which already patronizes AFS providers, trusts check cashers over banks, the cash economy sub-segment trusts banks more than check cashers. Although more than 90% of all respondents had no financial education, more than 55% were interested in attending a financial education workshop.

- **Hidden fees cause consumers to change financial service providers.** Banked respondents would be most likely to leave their present bank

FIGURE 7

TRUSTWORTHINESS OF FINANCIAL INSTITUTIONS

% Top 2 Box Scores
(7 pt. scale)



SURVEY QUESTION: On a scale of 1 to 7, where 1 is “not at all trustworthy” and 7 is “very trustworthy”, how much do you trust the following types of establishments when it comes to using them for financial services?

SURVEY BASE: Total banked respondents, N=1,000, Total unbanked respondents, N=1,021

A look at how low-income Los Angeles households manage the money they earn

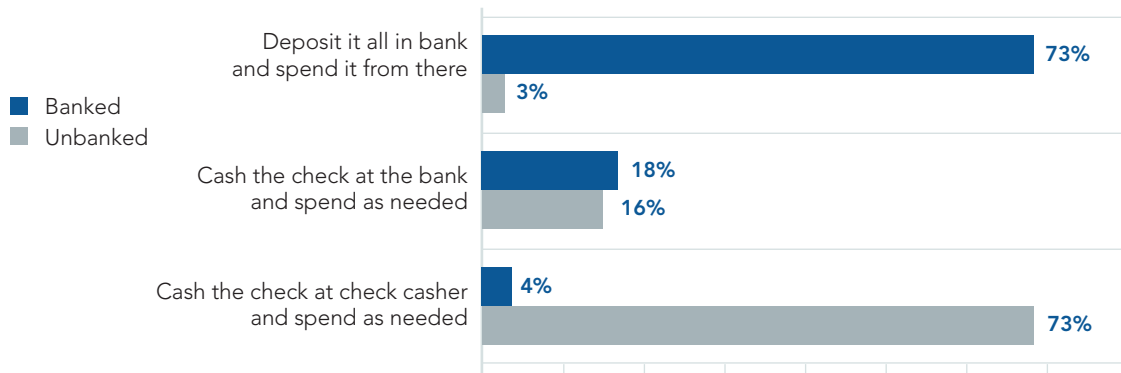
if it started “charging new fees without explanation” (72%). Another reason was “being treated rudely” (62%). Respondents were also likely to leave a bank for “stopping to support one’s culture or community” (56%). One-third (33%) of the Banked said they would leave a bank if its employees only spoke English.

- **Low-income customers are severely affected by overdraft fees and often do not understand them.**

Nearly half (44%) of the Banked had been charged an overdraft fee in the past year. This figure is more than double the rate (21%) documented in our statewide 2008 California survey, which included a wider range of income levels.¹³ Fully 18% of the Banked in the Los Angeles neighborhoods surveyed incurred insufficient funds or overdraft fees three or more times in the past year. Of those who have overdrafted their account, nearly three-quarters (72%) “did not know they were out of money” at the time.

FIGURE 8

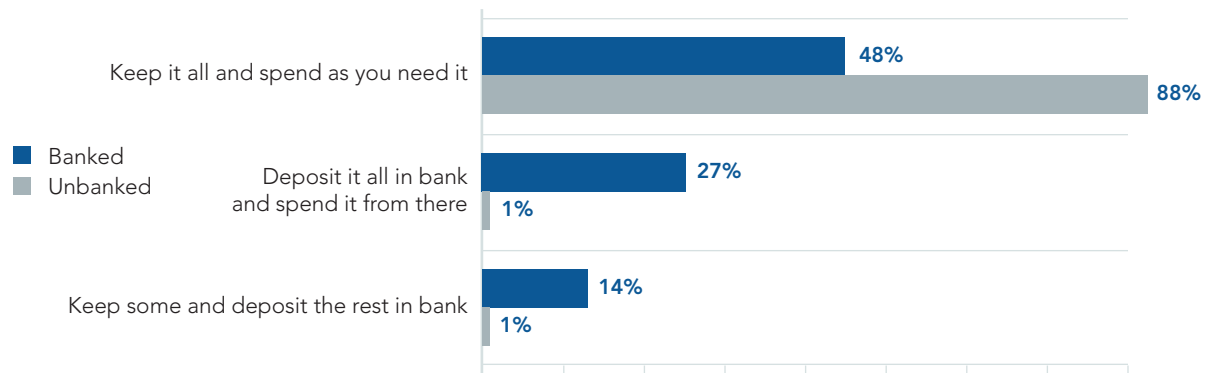
SAVINGS BEHAVIOR IF FORM OF HOUSEHOLD INCOME IS CHECK



SURVEY QUESTION: When you get paid by check, what do you do with it?
SURVEY BASE: Total banked respondents, N=350, Total unbanked respondents, N=215

FIGURE 9

SAVINGS BEHAVIOR IF FORM OF HOUSEHOLD INCOME IS CASH



SURVEY QUESTION: When you get paid in cash, what do you do with it?
SURVEY BASE: Total banked respondents, N=50, Total unbanked respondents, N=135

BANK ACCOUNTS CORRELATE WITH HIGHER SAVINGS IN LOW-INCOME COMMUNITIES

- **Payment by direct deposit strongly correlates with savings.** Among the Banked, payment by direct deposit has a strong correlation to savings behavior. Even in the current recession, respondents who are paid via direct deposit save at higher rates (36%) than their counterparts who are paid by check (25%) or cash (16%).

- **Banked persons paid by check are more likely to save than unbanked persons paid by check.**

Banked individuals are likely (73%) to deposit their checks in a bank. Many save a portion of their checks, but 18% simply cash the check at a bank and spend the money. A few (4%) take it to a check casher. On the other hand, payment by check does not encourage savings by the Unbanked. If paid by check, most Unbanked (73%) will patronize an AFS provider to cash the check and spend with no intent to save (Figure 8).

DISCUSSION

The Opportunity for Banks and Credit Unions

The size and density of the underserved Los Angeles community revealed by this study offers financial institutions an opportunity to secure relatively substantial cash deposits in addition to greater fees for transactional services. At least in Los Angeles, the data suggest there are thousands more unbanked households than prior surveys indicate. The FDIC's 2009 national survey of the nation's unbanked population estimated that they represented 7.7% of the nation's population and 9.2% of the Los Angeles MSA. These numbers are much higher in low-income neighborhoods like those surveyed by PHG, where estimates of the Unbanked range between 17% and 28%, and perhaps higher among less-educated individuals and non-English-speaking households.¹⁴ Among Los Angeles County's population of nearly 10 million persons, we conservatively estimate there are 1–1.25 million unbanked individuals.¹⁵

The Unbanked represent an emerging, untapped market for bank services. Some 85% are unbanked by choice and 63% have never had an account. In Los Angeles, high-density, low-income neighborhoods such as those surveyed contain high concentrations of Unbanked, making them attractive targets for bank efforts to attract market share. In a number of the City's urban communities the "income density" (a metric that quantifies income relative to area, measuring local purchasing power) aggregates between \$300,000 and \$400,000 per acre, which is three to four times the regional average.¹⁶ Used by retailers and developers to identify underserved markets for investment, income density is a metric of growing popularity. Simply put, when it comes to market demand

for basic, affordable, quality retail goods, including bank products, any lack of per capita income in low-income urban neighborhoods is more than compensated by the exceptional density of the region.

Our research indicates that Los Angeles' low-income communities present a loyal, solid customer profile that would utilize between four and six revenue-generating financial services. Geographic proximity and a fair and transparent fee structure appear to be the key components of customer loyalty. Trust of financial service providers (whether a mainstream bank or an alternative provider) appears to come with experience and working relationships. The Banked trust banks, but not AFS providers.

Our findings further show that those who use AFS—both the cross-over and the AFS-only segments—also offer banks an unclaimed market for the financial services these households now purchase from alternative providers. Our prior research has shown those who use AFS pay a median amount of \$700 a year just to cash checks, and an undetermined additional amount for other services.¹⁷ In the study area alone, representing a 2000 U.S. Census count of 578,705 persons, aggregate AFS fees could amount to tens of millions of dollars annually.

The cross-over population appears to provide a particularly strong potential market for banking services. While cross-over customers maintain a bank account for certain purposes, such as to receive direct deposit from an employer, they purchase other financial products based on perceived value from AFS providers. Regularly using both banks and AFS providers, this group has no significant negative perceptions associated with either industry player.

A look at how low-income Los Angeles households manage the money they earn

Similarly, the Los Angeles region's substantial cash economy segment may offer a promising market for banks. The study indicates that these are working, multi-earner households that spend and transact regularly in the local economy. They have lived in this country, on average, for well over a decade. Although they transact only in cash, their trust intuitively lies with the U.S. banking system over AFS providers. They are disciplined money managers: on a salary well below the poverty line in a median range of \$10,000 to \$14,999, they set aside almost \$3,000 per year to send to their families abroad. Viewed as a form of saving, the remittance behavior of these families is impressive.

To date, the banking industry has largely missed these market opportunities. Some banks are moving to offer fee-based transactional products that compete with AFS services.¹⁸ Conversely, some AFS providers plan to offer low-balance depository products for their loyal customers.¹⁹ However, the nation's largest banks have so far proved unwilling to meet the underserved population on its terms. Outside of the publicly led Bank On effort, few financial institutions have taken voluntary steps to encourage unbanked individuals to open accounts and build assets, even when legislation offers a path to do so. For example, the USA PATRIOT Act allows banks to accept alternative, foreign government-issued identification like the Mexican *Matricula Consular* to open bank accounts for unbanked immigrants regardless of their legal status.²⁰ In 2001, Wells Fargo Bank was a leader in accepting the alternative identification, opening more than 400,000 new accounts within 30 months. The Mexican government estimated that 4 million *Matricula Consular* were issued in the United States as of 2004, a number that has likely doubled or tripled since then.²¹ Despite having the legal authority to do so, few financial institutions accept foreign government-issued identification other than passports, nor do they make other efforts to reach out to unbanked immigrants.

Need for Appropriate Regulation and Consumer Protection Policy

Our study suggests that banking promotes saving in the United States. Banked families, whatever their mode of payment from employers, are more likely to save, and they save in their local bank.²² Further, as earlier Pew research demonstrates, parents who save significantly contribute to the upward economic mobility of their children.²³ In contrast, families who live in the cash economy send their disposable

income out of the country, and AFS-only families, who pay the highest fees for financial transactions, save and remit at relatively lower levels.

Although cash economy families in some respects demonstrate financially responsible behavior to a greater degree than users of AFS services, living in the cash economy carries significant individual risks of being the victim of theft, fraud or loss. Banking the cash economy segment would reduce these risks. Also, by increasing the chance that they would file tax returns, banking this segment could increase their income, since most of the individuals in this segment would likely be eligible for the tax credit targeted at low-income households were they to file. In addition, the size of this population and its seeming resistance to change has larger implications for municipalities like the City of Los Angeles and for the nation at large. Higher levels of crime against cash economy households add up to higher levels of crime in the City and in the nation. Inability to track the cash economy's earning and spending leads to loss of tax revenue. The failure of the earned income tax credit program to fully reach this group reduces their spending power in the local economy.

The study's findings suggest several policy directions for further investigation.

- **First, a worker's form of payment can prompt him or her to open a bank account.** This indicates that localities, states or nations interested in banking their unbanked populations should examine how they can increase the use of direct-deposit payment among employers, starting with the government as employer. The City of San Francisco, for example, is moving to have all its employees paid by direct deposit, as the logical next step in its Bank On campaign.²⁴ On the national scale, the U.S. military's move to direct-deposit paychecks dramatically increased the banked percentage of troops—and improved military readiness.²⁵ The federal government's encouragement of direct deposit for Social Security checks, estimated at 83% of all recipients, led to more recipients opening bank accounts.²⁶
- **Second, more financial education and asset-building strategies are required to responsibly capture the cash economy segment of the country and to ensure these individuals do not quickly join the ranks of the dissatisfied previously banked.** Similar programs are needed to help those who use

predatory AFS products shift to lower-cost and better-regulated services. In Los Angeles, for example, the City has rolled out its “Bank On Los Angeles” social marketing campaign in conjunction with citywide reforms that offer integrated financial education, tax preparation services and asset-building programs across its social safety net agencies, collectively referred to as the Family-Source Center system.

- **Third, the failure of the banking industry to reach out to the underserved of the population with products and services it needs calls for**

legislative or regulatory solutions that encourage safe, regulated check-cashing services, payment mechanisms, money-transfer systems, low-balance depository products and small-dollar loan programs that help these customers move toward the financial mainstream. In addition, the PHG survey’s confirmation of the traditional wisdom that all consumers overwhelmingly use financial service providers near their home re-emphasizes the importance of policies that encourage banks to maintain branch offices in low- and moderate-income communities.

NEXT STEPS

Over the next year, we will continue to assess the financial behavior of residents in the eight communities, the impact of such choices on their well-being and the effect of policy efforts to date.

Wave Two: A Second Data Point

This study has been designed as a multi-wave, longitudinal survey that tracks the financial behaviors of low-income households over time. Wave One was conducted from July to September 2009. Wave Two fielded in May 2010 and is set to finish in July 2010. By collecting data at two points in time for the same set of households, a richer analysis can be conducted. The resulting data and analyses may help us answer questions raised by the first wave or confirm patterns discerned in the initial study. Behavioral correlations can be established using multivariate regression analysis. Also, we hope to establish a measure of predictive capacity among our banked and unbanked households. The data also will enable study analysts to measure the financial evolution of the 2,000 tracked households across the current economic recession. After Wave Two, Pew will issue a report with refined sets of findings and recommendations, expected later this year.

Evaluation of the Bank On Los Angeles Campaign

In March 2009, Los Angeles Mayor Antonio Villaraigosa announced the launch of the Bank On Los Angeles campaign to encourage unbanked and underbanked residents to move their savings and financial relationships into mainstream banks. The campaign, supported

by PHG research, was piloted in four low-income neighborhoods that were shown to have empirically high percentages of unbanked households.²⁷ These four neighborhoods, as well as four other similarly situated low-income neighborhoods outside of the Bank On program, were selected as part of the PHG study area. The social marketing campaign associated with Bank On Los Angeles did not begin in earnest until the fall of 2009, after the completion of Wave One of the survey. Wave Two fieldwork will be completed after the initial ramp-up of the Bank On pilot, including the pilot’s first tax-preparation season. Although assessing efficacy of the Bank On program is not the primary inquiry of the PHG study, this longitudinal research comparing Bank On neighborhoods against a control group of neighborhoods will evaluate the early behavioral impacts of the public sector–led campaign. Any findings can inform other municipalities engaging in this growing movement to bank the Unbanked.

Addition of a Health Module

Given the scale and rigor of the financial-behavior data to be accumulated in this banking study, PHG has chosen to add an additional set of questions to the Second Wave survey that examine the social factors that affect health in this population, particularly the extent to which participation in the financial mainstream affects health. PHG aims to conduct two additional waves of health surveying with the same participating Los Angeles households. The first wave of fieldwork began in December 2009. The health survey will measure health care consumption behaviors; insurance coverage in low-income households; the

MORE ON METHODOLOGY

In selecting the methodology for this survey, PHG's intent was to ensure a level of rigor above that typically underwritten by industry market research or policy advocates. For this reason, the primary data collection methodology was interviewer-administered, face-to-face interviews of residents in their homes using random location sampling. Because this research approach is relatively high cost and labor intensive, it has largely been replaced by easier and less costly telephone and online surveys. However, PHG recognized that an online survey or purely telephone-based data collection would have been inadequate for a study such as this, which seeks to reach respondents who are unbanked or who are cash players in low-income urban areas. This is because many unbanked individuals lack regular access to computers and have no listed telephone number – and our demographic data confirm this to be true for our survey population. An online or telephone data collection approach would eliminate a large percentage of the intended target population. Additionally, our research experience shows that telephone-only surveys typically have extremely high drop-off rates at the 10-minute mark, as well as extremely high attrition in subsequent waves. Both our face-to-face approach and our cash incentives (discussed below) help mitigate these problems and enable us to conduct a survey with a longer instrument and multiple waves.

health impacts of financial stress; the economic impacts of poor health decisions; the scale of the cash market for health care services; and social determinants within communities that impact health. We think these data will provide context to the findings from our financial-behavior study and point to additional policy issues to consider.

The longitudinal study centers on a panel of 2,000 respondents drawn from a select group of eight low-income neighborhoods located throughout the City of Los Angeles, who were the subject of a two-phase survey conducted over the course of a year, with six to nine months between waves.²⁸ Respondents recruited for the panel were targeted to represent two specific sub-groups: (a) 1,000 unbanked households, defined as those with no current bank account; and (b) 1,000 banked households, defined as those who have at least one bank account. Approximately 3,600 households were contacted over the duration of Wave One to reach the above quotas.

For Wave One, respondents were screened and recruited via a door-to-door, interviewer-administered approach determined by random location sampling. Proportional quotas were determined for each of the eight target neighborhood geographies based on the broader sample quota of 1,000 banked

households and 1,000 unbanked households. Each of the neighborhoods was further subdivided according to census block group quotas using weighted census data. Individual quotas per block group were assigned via a Geographic Information Systems system based on the percentage each block group represents in terms of the total population of the census tracts represented in the neighborhood.

Three households per block group were randomly selected as possible starting points. If qualified respondents were not available at the first household, the second household was approached, followed by the third, if necessary. Up to four subsequent attempts were made to re-contact these starting households at different times of day. Upon the successful screening and recruitment of a household, interviewers approached other households per block, skipping a specific number of homes based on each block group's population size and target quota. The City of Los Angeles assisted field researchers to obtain safe access to large public housing projects and arranged a safe interview location in the building.

All interviewers were instructed to request the participation of the head of household or the individuals who share responsibility for household

financial decisions. If these individuals were not available, the interviewers returned to the household at a different time. Once deemed eligible, respondents were recruited into the panel and immediately administered the questionnaire. Interviews were attempted at different times of day, including both peak and off-peak employment hours, to ensure comprehensive representation of the target areas. Interviewers reflected the ethnic and racial backgrounds of the target areas' demographics. Because the population of these neighborhoods is heavily Latino, most interviewers were fluent in both Spanish and English. All interviews were conducted in the respondents' language of choice.²⁹ A total incentive amount of \$75 was offered to each participating panel member and dispersed through two stages: \$30 immediately following Wave One interviews and \$45 upon the successful completion of Wave Two interviews.

The survey consisted of between 70 and 150 questions, depending on the respondent's answers and financial behaviors. Nearly all questions were closed-ended, multiple-choice questions. Any open-ended questions were reviewed and categorized after fieldwork. The interviews lasted between 30 and 60 minutes, depending on the number of questions asked and the language of interview. In describing attributes of the banked and unbanked populations, each consisting of 1,000 randomly selected households, the margin for error is +/- 3.1% at a 95% confidence interval. The Wave One survey instrument is available upon request from the authors. The Wave Two survey instrument was finalized in May 2010. While most questions remain the same to preserve the longitudinal nature of the study, some revisions were made. Promising areas of inquiry received follow-up questions. Other questions with ambiguous results were refined.

A look at how low-income Los Angeles households manage the money they earn

APPENDIX A

FIGURE 10

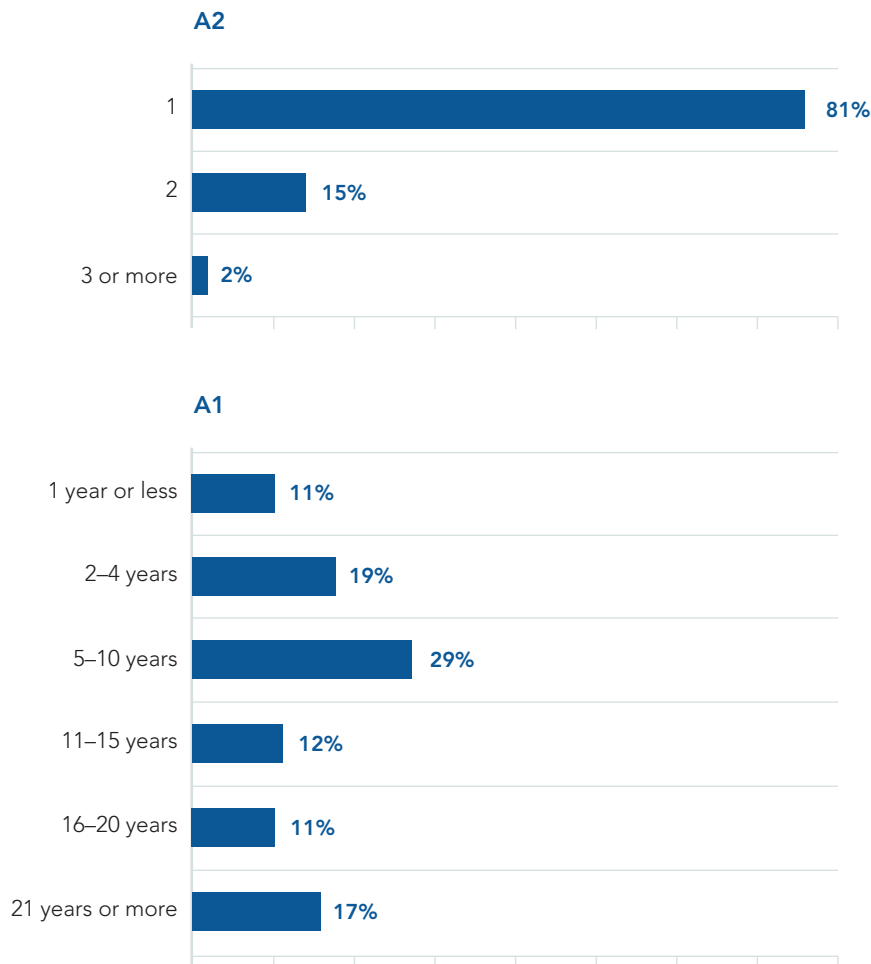
RESPONDENT DEMOGRAPHICS

Mean Score, 7 pt. scale		Banked	Unbanked
	Mean age	40.4 years	34.5 years
	Percent foreign born	65%	69%
	Average length of time in the U.S.	21.2 years	14.4 years
	Average household size	4.4 pp	4.7 pp
OCCUPATION	Non tech/non professional	31%	31%
	Homemaker	24%	34%
	Unemployed	12%	13%
	Technical	7%	4%
EDUCATION	Less than high school/some HS	39%	51%
	HS graduate	32%	33%
	Vocational/community college/some college	20%	13%
	College graduate and higher	9%	1%
	Median annual household income	\$15,000 to \$24,999	\$10,000 to \$14,999
	Use the Internet? Yes	43%	29%
	Voted in any U.S. election in the past? Yes	43%	20%

APPENDIX B

FIGURE 11

LONGEVITY OF BANKED STATUS



SURVEY QUESTION A2: How many banks or credit unions do you currently use?

SURVEY QUESTION A1: How many years has it been since you opened your very first bank account?

SURVEY BASE: Total banked respondents, N=1,000

APPENDIX C

FIGURE 12

HOUSEHOLD EXPENDITURES

Estimated Monthly HH Expenses	Banked	Unbanked
Rent/mortgage	\$989	\$731
Utilities	\$207	\$138
Phone	\$100	\$64
TV	\$63	\$52
Groceries	\$354	\$344
TOTAL	\$1,712	\$1,329

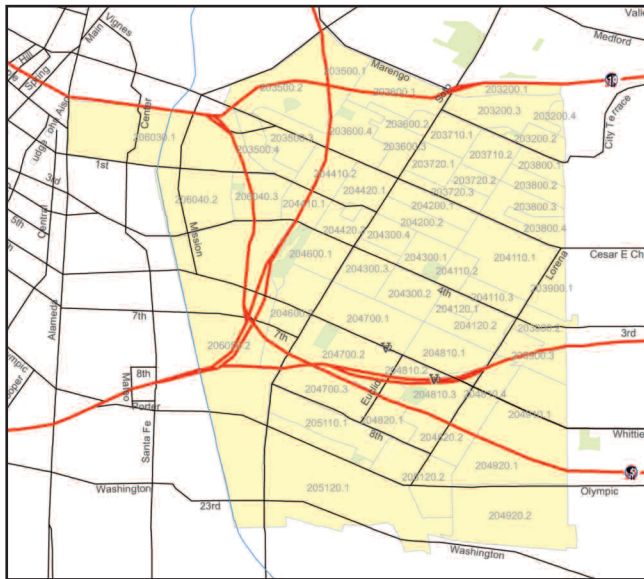
SURVEY QUESTION: Please estimate your monthly household expenses in the following categories.

SURVEY BASE: Total banked respondents, N=1,000, Total unbanked respondents, N=1,021

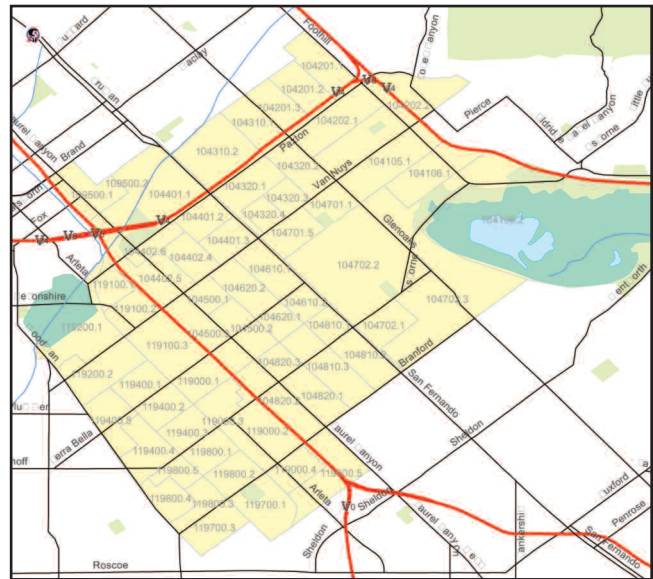
APPENDIX D

FIGURE 13

TARGET NEIGHBORHOODS: BANK ON



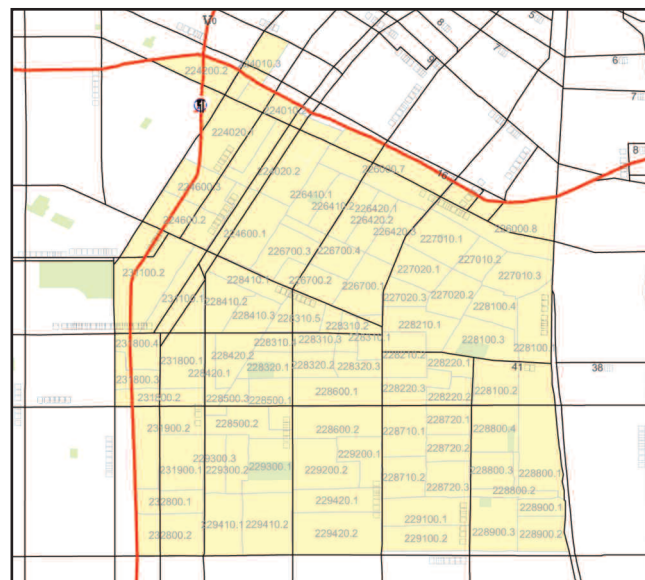
BOYLE HEIGHTS



PACOIMA



WESTLAKE/PICO UNION



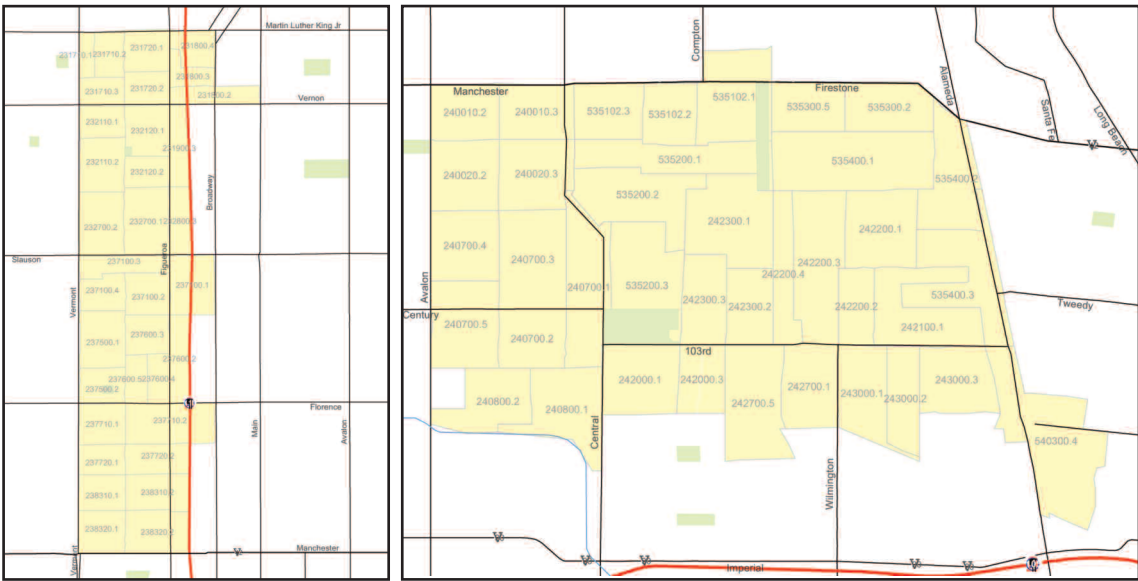
VERNON-CENTRAL

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APPENDIX D ...continued

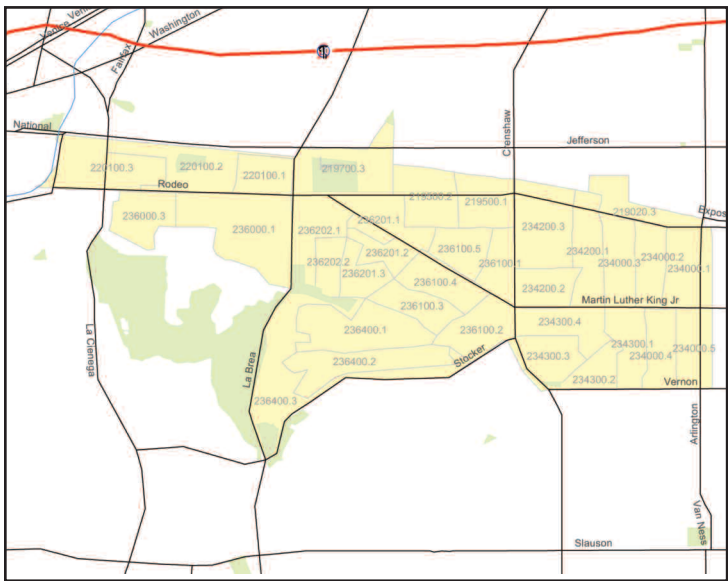
FIGURE 14

TARGET NEIGHBORHOODS: CONTROL GROUP

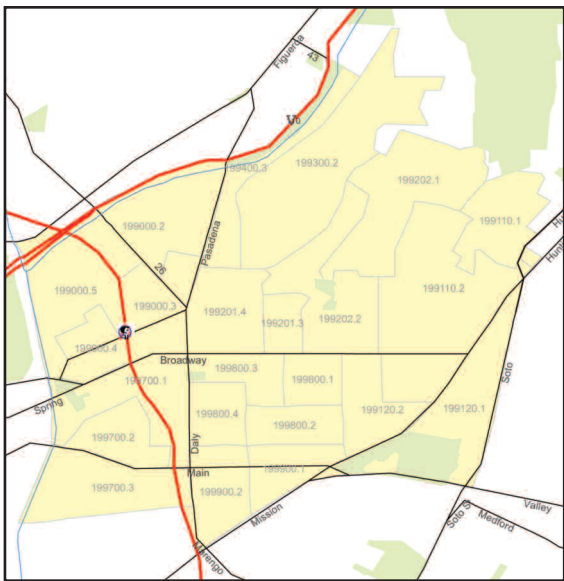


SOUTH FIGUEROA CORRIDOR

WATTS



BALDWIN VILLAGE/LEIMERT PARK



LINCOLN HEIGHTS

ENDNOTES

- ¹ Throughout this paper, except as specifically indicated, the word “bank” is used to refer to regulated depository institutions, including banks, credit unions and thrifts. In fact, our banked respondents overwhelmingly use banks.
- ² Matt Fellowes and Mia Mabanta, *Converting Basic Financial Service Fees into Prosperity: An Untapped Opportunity for Consumers and Banks*, (Washington: The Pew Charitable Trusts, 2008), www.pewtrusts.org/safebanking (accessed June 16, 2010).
- ³ Confidential industry interviews undertaken by Emerging Markets, Inc., on behalf of the Pew Health Group (2009).
- ⁴ The survey did not ask individuals why they presently cannot get an account.
- ⁵ Constance R. Dunham, *The Role of Banks and Nonbanks in Serving Low- and Moderate-Income Communities*, (Washington: Office of the Comptroller of the Currency, Government Printing Office, 2002), http://www.occ.treas.gov/SFAA/role_bks_nonbks.pdf (accessed June 15, 2010); Michael S. Barr and Jane K. Dokko, “Tax Filing Experiences and Withholding Preferences of Low- and Moderate-Income Households: Preliminary Evidence from a New Survey,” (paper presented at the IRS Research Conference, Washington, DC, 2006), <http://www-dtp.cc.utexas.edu/law/academics/centers/clbe/assets/BarrPaper.pdf> (accessed June 15, 2010); and Ellen Seidman, Moez Hababou and Jennifer Kramer, *Getting to Know Underbanked Consumers: A Financial Services Analysis*, (Chicago: The Center for Financial Services Innovation, 2005), http://www.cfsinnovation.com/system/files/imported/managed_documents/seg.pdf (accessed June 15, 2010).
- ⁶ Federal Deposit Insurance Corporation, *FDIC National Survey of Unbanked and Underbanked Households*, (Washington: FDIC, 2009), http://www.fdic.gov/householdsurvey/Full_Report.pdf (accessed June 15, 2010).
- ⁷ Jeffrey S. Passel and D’Vera Cohn, *A Portrait of Undocumented Immigrants Living in the United States*, (Washington: Pew Hispanic Center, 2009), <http://pewhispanic.org/files/reports/107.pdf> (accessed June 15, 2010).
- ⁸ The FDIC nationwide study estimates that the nationwide cash economy segment is 25% of the unbanked population. Source: *FDIC National Survey of Unbanked and Underbanked Households*, (Washington: FDIC, 2009).
- ⁹ Los Angeles County counted 9,639,063 persons in the 2000 U.S. Census, over 12% living below the poverty line. The majority of these persons (56%) do not speak English at home. Within the county, the City of Los Angeles accounted for 3,658,397 persons. Family poverty rates exceed 15% in the city, and nearly 60% speak a foreign language at home.
- ¹⁰ Brian K. Bucks et al., “Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances,” *Federal Reserve Bulletin* 95 (2009): A45.
- ¹¹ *FDIC National Survey of Unbanked and Underbanked Households* (2009), citing “underbanked” estimates of the banked population at the national (19.4%), state (16.5%) and MSA (15.8%) levels.
- ¹² The totals may add up to over 100 percent since respondents can have more than one job or receive payment for a job in multiple forms.
- ¹³ Fellowes and Mabanta, *Converting Basic Financial Service Fees into Prosperity: An Untapped Opportunity for Consumers and Banks*.
- ¹⁴ The FDIC study estimates that in the Los Angeles MSA, the unbanked percentages vary as follows, with certain population characteristics matching our target neighborhoods: \$15,000-\$30,000 annual income, 26.50% unbanked; no high school diploma, 28.40% unbanked; African American, 17.80% unbanked; and Hispanic, 18.40% unbanked.
- ¹⁵ Los Angeles County’s population is currently estimated at 10,266,841 persons. Source: North Carolina Economic Development Intelligence System (EDIS), “County Profile: Los Angeles County,” (April 2010), <https://edis.commerce.state.nc.us/docs/countyProfile/CA/06037.pdf> (accessed June 16, 2010). Estimates of the unbanked percentage range from 9.20% in the 2009 FDIC National Survey of Unbanked and Underbanked Households to 30.05% in the 2002 U.S. Census Bureau Survey of Income and Program Participation. Other well-respected studies estimated the Unbanked at 19.31% (Center for Financial Services Innovation, 2007) and 10.87% (Federal Reserve Survey of Consumer Finances, 2004). This range conservatively supports an estimate of 1 to 1.25 million unbanked persons.
- ¹⁶ We compute a regional average density of \$97,139 as estimated in April 2010 using the following formula: $[(\$24,730/\text{person}) \times (10,266,841 \text{ people})] /$

A look at how low-income Los Angeles households manage the money they earn

[(4084 sq mi) * (640 acres/sq mi)]. Sources: Population from North Carolina Economic Development Intelligence System (EDIS), "County Profile: Los Angeles County," (April 2010), <https://edis.commerce.state.nc.us/docs/countyProfile/CA/06037.pdf> (accessed June 16, 2010); Per Capita Income from Ibid.; Area from Los Angeles County Government, "About LA County," (April 2010), <http://portal.lacounty.gov/> (accessed June 16, 2010).

The most recently reported income density for the entire Los Angeles MSA is \$91,000 per acre as of 2008. Source: Social Compact, Inc., *Los Angeles Neighborhood Market DrillDown: Catalyzing Business Investment in Inner-City Neighborhoods* (Washington: Social Compact, Inc., 2008).

- ¹⁷ Fellowes and Mabanta, *Converting Basic Financial Service Fees into Prosperity: An Untapped Opportunity for Consumers and Banks*.
- ¹⁸ Union Bank's Cash & Save hybrid model is a good example of this innovation in Los Angeles. A full-service bank branch is co-located with a full-service check casher, allowing customers to select to the product or service most desired. Currently there are nine Cash & Saves located in traditional branches in the Los Angeles region.
- ¹⁹ Nix Check Cashing was recently purchased by nonprofit Kinecta Federal Credit Union, which intends to incorporate existing credit union products, as well as new products for the low- and moderate income customer, into Los Angeles' dominant check-cashing operation.
- ²⁰ In the PHG survey, 47% of all respondents were born in Mexico and could take advantage of the Mexican *Matrícula Consular* identification. Another 16% were born in Guatemala or El Salvador, nations that also issue consular identification to residents abroad. Only 33% of respondents in these eight neighborhoods included in this study reported being born in the United States.
- ²¹ Michael A. Frias, "Linking International Remittance Flows to Financial Services: Tapping the Latino Immigrant Market," Federal Deposit Insurance Corporation Bank Examination Supervisory Insights (2004), www.fdic.gov/regulations (accessed June 15, 2010).
- ²² Since banked families also earn more, it may be easier for them to save. However, it appears that the Unbanked are choosing to remit (as much as or more than the Banked), rather than to save.
- ²³ Reid Cramer et al., *A Penny Saved Is Mobility Earned: Advancing Economic Mobility Through Savings*, (Washington: The Pew Charitable Trusts, 2009).
- ²⁴ SafePay SF is a collaborative effort of the City of San Francisco's Office of the Treasurer, the San Francisco Chamber of Commerce and SF Works, a non-profit organization.
- ²⁵ Effective July 26, 1996, federal law required all federal payments to be made via electronic funds transfer (EFT) by January 1999. Since 1992, the prescribed method of payment within the Department of Defense has been EFT. This policy requires payments by EFT on all new active duty, reserve, retired and annuitant payments unless the recipient of the new payment certifies in writing that he/she does not have a financial institution or authorized payment agent. *Omnibus Consolidated Rescissions and Appropriations Act of 1996*, Public Law 104-134, 104th Cong., 2nd sess. (April 26, 1996).
- ²⁶ Ibid.
- ²⁷ The four communities were Boyle Heights, Vernon Central, Westlake/Pico Union and Pacoima. The first three were documented as highly unbanked in surveys published by Emerging Markets, Inc. (2008) and supported by market research released by Social Compact. Pacoima's underbanked profile was reviewed in a publication by the Center for Financial Services Innovation commissioned as part of a 2004 credit union feasibility study. See Appendix D for maps of these areas.
- ²⁸ As discussed above, the neighborhoods consist of four neighborhoods that had been the subject of the Bank On Los Angeles campaign and four similar neighborhoods that had not.
- ²⁹ The population of these neighborhoods has only a very small percentage of speakers of Asian languages, but interviewers fluent in Asian languages were available if interviewers encountered a monolingual Asian-language speaker.

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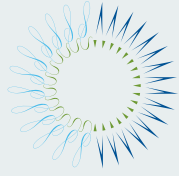
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