

FINANCIAL ACTIVITIES AMONG UNBANKED HISPANICS IN NEW YORK CITY AND  
LOS ANGELES

by

FARAH MIHOUBI

(Under the Direction of Joan Koonce Moss)

ABSTRACT

This research explores in detail unbanked Hispanic consumers, using the Office of the Comptroller of the Currency's Survey of Financial Activities and Attitudes dataset. Logistic regression was employed in an attempt to understand the differences between Hispanic and non-Hispanic consumers' behavior in the financial services marketplace. This study examined whether Hispanics were more or less likely to be unbanked or to use alternative financial services, both before and after controlling for other variables that could proxy for demographic characteristics, economic characteristics, language-related characteristics, and geographic characteristics. The findings indicated that Hispanics are indeed more likely to be unbanked than their non-Hispanic counterparts. After adjusting for other factors, Hispanics were less likely to be unbanked, suggesting that certain characteristics of the population may play a greater role in being unbanked than being Hispanic. However, the findings did not support the direction of the hypothesis when examining the use of AFS.

INDEX WORDS: Unbanked, Hispanics, Alternative Financial Services, Fringe Banking

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## DEDICATION

I dedicate this research to my silent fourth committee member, my strongest cheerleader, and my “dad,” Professor Robert Drazin of the Goizueta Business School at Emory University. Without his unwavering support and sound fatherly advice, given freely and in abundance, I would never be where I am today. There are simply no words in the English language to express my gratitude or my depth of emotion. Any and all of my future achievements from this moment on I attribute in large part to his having seen the kernel of possibility in me all those years ago, as he watched me grow and finally be free to leave the nest and soar.

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## CHAPTER 1

### INTRODUCTION

Consumer advocates and policymakers have debated the fate of the “unbanked” population in the United States for decades. Much research on understanding those who do not use the traditional financial services sector (but instead operate in the alternative financial fringe) has focused on ascertaining *who* are the unbanked and *why* they are unbanked. Broadly, this research has attempted to narrow down the population to those with certain likely demographic characteristics. There have also been attempts to elucidate the reasons for the unbanked choosing to remain unbanked. A variety of reasons have been borne out by the research. More specifically, however, it is of particular interest in this research to understand an important subset of this unbanked population. Hispanics make up a large segment of unbanked consumers in the United States today and will be the focus of this study.

#### Overview of the Hispanic Population

The U.S. Hispanic population is especially interesting to study, not only because of its booming growth and diverse makeup, but because it is possible that a number of types of barriers affect Hispanic consumers’ choice of financial services, or affect them differently than other consumers. Whether the term Hispanic refers to those who are illegal immigrants seeking a better life and economic opportunity, first-generation pioneers who may or may not decide to stay for good, or those who have been here since even before the first American settlers arrived (for example, Mexican-Americans who became U.S. citizens when Mexican land was annexed to the United States), some proportion of the entire continuum of Hispanic-Americans are likely

disadvantaged in the financial services marketplace. Their financial decisions are certain to have lasting effects on future generations of this growing ethnic population.

Understanding specifically the Hispanic unbanked population, as a subset of the larger unbanked population is of vital importance. Currently, the estimated U.S. Hispanic population is over 35 million or 13%, and is growing rapidly; by 2020, there should be over 55 million Hispanics in the U.S. (Russell, 2002). There are also an additional 3.8 million Hispanics in Puerto Rico, which are often uncouned in national statistics on the size of the Hispanic market. This market is not only large, but growing exponentially. Hispanics are the “fastest-growing population segment” (Radice, 1997, p. 109) in the United States today, and the purchasing power of this group is over \$452 billion annually (Kelderhouse, 2002). In the period from 1990-2000, the U.S. Hispanic population has grown over 57.9% (Jackson, 2002), and in the past four decades, this population has grown over 600% (Radice, 1997).

Hispanics are a complex demographic group to study and “defy easy classification” (Cafferty and Engstrom, 2000, p. xiv). Nearly 24 different nationalities make up this population (Radice, 1997)—a drastically heterogeneous group with different culturally-mediated values who may all react differently to the challenges of the marketplace. In an attempt to classify Hispanics, they are often lumped together into one ethnic group solely for their common language. An assumption of their ability to all speak Spanish then “becomes the visible proxy for culture” (Cafferty & Engstrom, 2000, p. xiii). Others choose to sub-categorize them by country of origin. The main categories of Hispanics are those of Mexican origin, which are the largest group (66%), followed by Central and South Americans together (14%), Puerto Ricans (9%), Cubans (4%) and “other Hispanics” (6%) (Russell, 2002). However, breaking down Hispanics by country of origin can also be “inadequate.” For example, in describing Mexican-Americans, who

can be further divided into “recent immigrants from Mexico, second- and third-generation U.S.-born people who still feel close to Mexico and people who might describe themselves as Chicanos or Mexican-Americans but who know little and care less about the ancestral homeland, there are many whose families were never in present-day Mexico” (Fox, 1996, p. 34). Finally, there is also the frustration in applying a single term “Hispanic” to a population that is classified very ambiguously by various methods of data-gathering, whether it be national-level (Census) data or smaller regional studies. Some definitions of Hispanic go by mere presence of a Spanish surname, others by Hispanic origin, and others use Spanish heritage or mother tongue to operationally measure the Hispanic-defined population. In addition, many self-report surveys involve self-categorization, and there is much variability in how respondents classify themselves (Fox, 1996).

The Hispanic population is also very different from other ethnic groups and this difference may contribute to a large proportion of unbanked Hispanics. In contrast to most other immigrant groups which have assimilated into the American landscape at least by the second or third generation, Hispanics are marked by their *lack* of complete assimilation. Many Hispanics retain a temporary attachment to their new homeland, and often do not plan to become citizens or permanent residents of the U.S. In fact, many Hispanics often retain strong ties to their homeland and culture, most especially because of their proximity to the United States. They often travel “freely to visit family and friends in Spanish-language society, and Spanish language use is constantly renewed by the migration stream” (Cafferty and Engstrom, 2000, p. xiii). Many Hispanics maintain constant “cultural refueling,” “constantly going back to their countries and recharging their culture and values” (Davila, 2001, p. 79). A large majority of Hispanics continue to function in at least some areas of their daily life in Spanish. This is especially true of the next

generation of Hispanics (Generation Ñ), which by 2005 is expected to comprise 17% of the under-18 market (Gardyn, 2001). Most of this generation embraces its heritage and wishes to preserve it; many prefer speaking Spanish, and most still watch Spanish-language TV and listen to Spanish-language radio. This lack of complete fluency with the English language would put many Hispanics at a disadvantage in their choice of financial services.

It is useful to compare Hispanics with their non-Hispanic counterparts. In general, it can be said that Hispanic-Americans are younger than the rest of the population, with more than one-third under the age of 18 and 50% under the age of 26 (Diaz, 2001). Most have high fertility rates and are comprised of larger families than non-Hispanic families. Most also have lower incomes than White households. According to the U.S. Census, Hispanic median household income in 1999 was about \$31,000, compared to about \$43,000 for White households. Poverty rates are also higher for Hispanic households; Russell (2002) cites that 43% of Hispanic households earn less than \$35,000, which compares with only 30% for White households. Finally, Hispanic families generally have lower net worth than White families. Between 1995 and 1998, the median net worth of Hispanic families sank by 24%, to \$9,200 per family, while the median net worth of White families rose to \$95,610 over that same period (“Hispanic Savings,” 2000).

#### Banking by Hispanic-Americans

Based on data from the 1998 Survey of Consumer Finances (SCF), 87% of all households had banking accounts, while only 70% of Hispanic households did (Diaz, 2001). Language barriers are higher for Hispanics, as are the inconvenient hours and locations of many banks. Hispanics’ attitudes toward banks can reflect “immigrants whose families experienced lost deposits in their home countries’ banks because the bank went out of business or because of

currency devaluations” (Diaz, 2001, p. 3). A certain number of Hispanics are also new immigrants, and carry their mistrust of the banking system with them from their mother countries (Greene, 1998). Many Hispanics face difficulties from not having enough or the right kind of documentation to open accounts; this obviously is a greater problem for those who are undocumented in the first place. Diaz (2001, p. 3) notes that the “practice of requiring documentation in excess of that required by law to open accounts is widespread and constitutes a major barrier.”

The literature on Hispanics and banking is limited, since the Hispanic population specifically has not been targeted as an area of study on the unbanked. The SCF data has been mined extensively, but only attempts to answer the question of the proportion of Hispanics that are banked versus unbanked. However, it quickly reaches the limit of its usefulness, as the dataset is not designed specifically to answer the questions posed in this research. Using a study designed by the Office of the Comptroller, which specifically gets at detailed information about Hispanic banking and non-bank activities is not really a replication, as prior research on the subject is limited and largely non-existent.

#### Purpose and Objectives of the Study

The goal of this research is to investigate the financial activities of Hispanics in New York and Los Angeles to more closely focus in on the particular needs of this important and growing population. Specifically, it will be important to observe whether Hispanics are more likely to be unbanked or to be users of the alternative financial sector than non-Hispanics. It has been established that being unbanked poses a disadvantage to consumers. The unbanked who often resort to the alternative financial sector to manage their financial lives often face higher costs than those who use mainstream financial institutions. Research has found that Hispanics

are more likely to be unbanked than non-Hispanics; this may mean that they also use the alternative financial sector more than non-Hispanics. It may be that the reasons that Hispanics are unbanked are quite similar to those for non-Hispanics, and bringing to light these factors is the purpose of this study.

This study will focus on two issues:

1. Whether Hispanics are more likely to be unbanked than non-Hispanics, and whether there is a difference between Hispanics and non-Hispanics in being banked or unbanked, when other factors are controlled.
2. Whether Hispanics are more likely to use alternative financial services than non-Hispanics, and whether there is a difference between Hispanics and non-Hispanics in using alternative financial services, when other factors are controlled.

To date, there has been little analysis of the growing Hispanic population in the United States with regard to their financial activities. Neither has this rich and thorough dataset, which answers numerous questions about its sample population's financial activities, been well mined. The addition of this data to the little that is already known about the unbanked, especially as it relates to activities of Hispanic populations in New York City and Los Angeles, two cities where Hispanic immigrants have traditionally flocked, is very necessary.

The Debt Collection Improvement Act of 1996 and the U.S. Treasury's Electronic Funds Transfer Program (EFT'99) were attempts on the part of the federal government to reduce government paperwork and expense for the issuing of government payments by using direct deposit methods instead. With this legislation has come a newfound appreciation for the growing unbanked population. As financial service providers turn increasingly toward technology to remain competitive and reduce costs, it is important to make certain that this

population does not become part of a “digital divide.” A better understanding of one ethnic population may help policymakers, consumer advocates, and others working in social service agencies to extrapolate their findings to other ethnic populations, especially those for which language barriers may put them at a greater disadvantage than other impoverished groups, such as African-Americans or Native Americans, for whom English language fluency is less of a hindrance.

## CHAPTER 2

### REVIEW OF LITERATURE

This section summarizes reasons for being unbanked, disadvantages of not being banked, and *who* exactly are the unbanked. Trends in the U.S. banking industry that have contributed to the increase in the unbanked over time are also explored and discussed. Alternatives to mainstream financial institutions, such as check-cashing and pawnshops (the alternative financial sector, or AFS) are detailed as well. Finally, this section ends with government interventions, such as the Debt Collection Improvement Act of 1996 and the Treasury's Electronic Funds Transfer Program.

#### Reasons for Not Banking

There are numerous reasons for being unbanked that have been identified. Some of the unbanked population simply cannot afford to maintain an account. They cannot scrape up the minimum balance it takes to open an account or they do not have a stable enough income to maintain the minimum balance necessary to avoid various service charges. In other cases, they do not have enough reserves for the float that is necessary from the time they deposit their checks until the bank considers them "cleared," or for the reserves necessary to cover an employer's possible bounced paycheck. The most expensive deterrent of all is not having enough money to avoid the domino effect of a bounced check, in terms of bank penalties and vendor penalties. Prescott and Tatar (1999) suggested that account-holders with low-balance accounts, when confronted with the inevitable overdraft, more often close their accounts, while a high-balance account holder would be more likely to pay the overdraft fees, and presumably be more careful

the next time. Thus, many of the unbanked drop out of the system, rather than never having been in it. Belew (1989), in the Virginia Citizens Consumer Council's survey found that over half of the unbanked had previous accounts that were now closed. Kennickell, Starr-McCluer and Surette (2000) also found that nearly half (47.9%) of their unbanked respondents had accounts in the past.

Many of the unbanked cannot handle the increasing number of fees associated with maintaining a regular checking account, which include minimum balance requirements, a minimum amount to open an account, fees for check-return with monthly statements (as opposed to free check safekeeping), fees for non-bank ATM use, fees to make deposits at a teller instead of using direct deposit or ATM depositories, yearly ATM card fees, and dormant ATM card fees. Stavins' (1999) survey of 250 financial institutions in the 25 largest U.S. metropolitan areas reported average bank charges for a variety of services. For non-interest-bearing accounts, the minimum (average) required to open an account was \$81, and the minimum balance to avoid monthly service charges was \$348, with the average monthly penalty for not adhering to minimum balance requirements being \$5.50. For customers who could not accumulate a minimum-balance, Stavins (1999) found that the average non-interest-bearing account without a minimum balance requirement costs \$12.30 per month to maintain. Fees on interest-bearing accounts were higher.

For the unbanked who do not currently pay to cash their paychecks or government checks, it may be that bank fees are more costly than the way they function now, so that maintaining a bank account does not make sense. For example, Dunham (2001) found that only 17% of the unbanked had "banking" costs (check-cashing and money order creation) of \$100 or more per year, and these tended to be higher-income households who could better afford it; thus

being unbanked may not have entailed high alternative costs. Prescott and Tatar (1999) found that many of the unbanked use grocery stores, banks, and other retailers to cash checks for free.

Maintaining eligibility for welfare benefits is also an important reason for remaining unbanked. Marlowe, Godwin, and Maddux (1995) found that welfare recipients thought that welfare programs were more “stringent” than they really are, in terms of promoting earning and savings. Swagler, Lewis, and Burton (1996) suggested that it is possible to assume that households in a certain income range (the range that qualifies them for welfare assistance) who use alternative financial services disproportionately more than other poor groups may well be wishing to keep their transactions private. The alternative financial sector allows such anonymity. Privacy issues may also extend to keeping money private from other members in the household as well. In addition, privacy may be an important issue for some of the unbanked, particularly if they are illegal aliens or parents who owe child support and do not wish to have their wages attached. Those who are undocumented may not have social security numbers or other adequate identification it takes to open a bank account. Keeping assets away from creditors may also come under the privacy issues reason.

Some of the unbanked may have had bank accounts before, but perhaps lost a job or were unable to maintain their balance for a time, and are now on the banking industry’s blacklist: ChexSystems, where they will remain for 5-7 years. ChexSystems (2003), which provides information to financial institutions about potential customers, helps banks “identify applicants who may have a history of account mishandling” to help financial institutions screen potential customers. Approximately 7 million Americans are currently on this list (“Check 101.com Announces,” 2001). Some may have a poor credit history, or not even a credit history at all.

Finally, a medley of other possible issues may also be at work. Education may be a problem. Those without knowledge of how banking works may not have the tools to function in a system where balances must be maintained, and high fees are imposed for bounced checks and bounced ATM transactions. Some, especially those who come from countries where the banking system is not trustworthy, may carry those feelings of mistrust when they come here. They may prefer the human aspect of still being able to speak with a person at an alternative service provider. Having everything automated may be scary to some immigrants, the elderly, and those who do not have a trust of computer technology or mechanization. Further, perhaps the plethora of alternative financial service providers versus the scarcity of bank branches, particularly in low-income areas, contributes to the unbanked staying out of the mainstream.

Hogarth and Anguelov (2002) examined the Federal Reserve's SCF for the years 1989-1998 and found that three major categories for reasons for being unbanked emerged. They identified the three categories as "product design factors" (features of bank accounts themselves that often discourage their use by the unbanked), "practical factors" (inability to afford an account, need for an account, or ability to oversee an account), and "institutional factors" (which include larger factors like location/convenience of banks/hours, perceived friendliness of bank personnel, problems with past credit history, etc.). They found that 48% of those in their sample cited reasons related to "product design" for being unbanked. Practical reasons accounted for 29%, with 19% referring to institutional factors instead. By income levels, they found that institutional factors correlated with higher incomes and practical factors more often correlated with low incomes. Also, practical factors were more often associated with ethnic/minority groups. Older households were found to be more likely to state product design factors, as were households with more education. Households with less education identified more practical factors instead.

Looking at the literature shows some similarities among studies on understanding motivations of the unbanked. Kim (2001a) cited three main reasons for the unbanked remaining unbanked. She believed they fall under the categories of attitudes, “attractiveness of services” and costs. Attitudes include “dislike of banks,” “do not like dealing with banks,” “distrust of banks” (Kim, 2001a, p. 3) and needs for privacy of financial records. Scott’s (1988) survey found that two important reasons were the cost of maintaining a checking account and the inconvenience of banks (both geographically and in terms of hours of operation).

Based on studies conducted using the SCF, three reasons are consistently offered for being unbanked: unbanked consumers feel they don’t have enough money, do not write enough checks to necessitate a bank account, and do not feel comfortable dealing with banks (Good, 1999). Not writing enough checks (to make it worthwhile) was the main reason given in the 1989, 1992, 1995, and 1998 SCF (at 34.4%, 30.4%, 25.3% and 28.4%, respectively). Not having enough money was the second most common reason given in the 1989, 1992 and 1995 SCF. The next most frequent reason cited was “do not like dealing with banks,” which actually surpassed the former reason in the 1998 SCF, and was the third most common reason given in the 1995 SCF.

Caskey and Peterson (1994), in looking at the reason for the decline in bank account ownership between 1977 and 1989, found that “changes in the socioeconomic conditions” (p. 69) of the respondents were the main reason for the increase in the unbanked during that period. This included reasons such as “not writing enough checks” or “not having enough money to maintain a minimum balance.” The authors predicted that only measures that stabilized/increased the low-income consumer’s wealth were likely to decrease the population of the unbanked.

Lewis, Swagler, and Burton (1996) found that, among their 120 respondents, the reasons for being unbanked were maintaining welfare eligibility, not enough money to cover deposits while they clear the system, and concern over bounced checks. Rhine, Toussaint-Comeau, Hogarth, and Greene (2001) found that the reasons most often cited in their study of the Chicago-area unbanked were minimum balance requirements, high account maintenance fees, or not enough money to open an account. The second major reason was dislike of banks, distrust of banks, or desire for privacy.

Hogarth and O'Donnell (1997) found that among the unbanked, three main reasons for being unbanked were "don't write enough checks," "don't like dealing with banks," and "don't have enough money" (p. 63). Leech, Scott and Fox (1990) in their study of the Virginia Citizens Consumer Council found that the main reasons for being unbanked were that the opening balance requirement was too high (46%) and that fees were too high (23%).

#### Disadvantages of Not Banking

Clearly, there are also many disadvantages to being unbanked. If nothing else, using alternative financial services is expensive. Using these services hardly allows the neediest of families, those without savings, to eventually get ahead in the marketplace. Because of the alternative financial services sector's target market of low-income consumers, higher fees for services generally are borne by "those least able to pay them." Swagler, Burton and Lewis (1995a) suggested that most of the transactions in the alternative financial sector are not single-term transactions. With many alternative financial sector options comprised of rollover-type transactions, the burdensome debt eventually becomes usurious in its APR, if it were calculated. Furthermore, the vicious-cycle effect of relying on services from this sector does not allow a low-income consumer an easy way out of the negative cycle of use. Also troubling is that those

who use the alternative financial services sector are not able to avail themselves of the consumer protection legislation that covers the traditional financial sector. According to Swagler, Burton and Lewis (1995b), there are no federal-level protections afforded to consumers of this market, while there is some limited (and varying in usefulness) state-level legislation affecting the alternative financial sector.

Caskey (1994) and others have observed that it is becoming more and more costly to live outside of the financial mainstream. In an age of increasing technology, it is quite an oddity to still be functioning in the financial services fringe. Society is becoming increasingly cashless, so consumers who carry around cash to conduct their daily activities are more and more in the minority. Furthermore, carrying cash around can be dangerous, especially in low-income neighborhoods. Aside from outright crime and theft of cash, there is no recourse available to consumers for lost cash, as there might be with liability protections of consumers who use credit cards or various types of bank cards.

Alwitt and Donley (1996) suggested that carrying around cash can result in a lower likelihood of keeping records of transactions, which limits households' ability to budget and save. Carrying around an entire paycheck's worth of cash certainly does little to encourage saving; indeed, the middle- and upper-classes do not typically function in this way. Instead, they take out only a little cash at ATMs at a time. Kim (2001a) noted that a survey undertaken by the Office of the Comptroller of the Currency in New York and Los Angeles found that individuals with bank accounts were twice as likely to have savings as those who are unbanked, and were more likely to add to such savings accounts on a regular basis than those who live a cash-only lifestyle.

It is more inconvenient and time-consuming to wait in line for check-cashing and money order processing than it is to have direct deposit and payment of bills by check. In addition,

many of the places that once cashed checks for free no longer do so, and there are fewer sites that take in-person cash payments for utility bills. Some have suggested that banks are becoming more patronizing to non-customers, who often have to wait in line behind bank customers to have checks cashed, or require extra steps like fingerprinting (to cut down on fraud and reduce the banks' risk) for non-account-holders cashing checks drawn on that bank (Veverka, 1999).

Finally, households that rely on the alternative financial sector also miss out on the “intangible” benefits of building credit and acquiring knowledge about financial services. Such consumers are unable to gain knowledge of basic financial facts, which may well impact their agility in their interactions with the rest of society's institutions. They cannot build good credit, which will enable them to avail themselves in the future of educational, mortgage, car and small business loans. They cannot use easy unsecured credit (like credit cards), as the rest of the population does, to bridge them during times of dissaving, and must resort to often usurious forms of credit like pawn shop credit. Swagler, et al., (1995a) pointed out the short-term nature of lending in this industry, which does not allow for the ultimate purchase of homes via mortgage loans. Since home ownership is usually a household's first form of asset accumulation and a large source of wealth generation greatly facilitated by generous tax advantages given to homeowners (mortgage interest deductions, property tax deductions, home equity loan deductions, and exemption for a certain amount of profit realized upon sale, for example), this is particularly significant.

Most of all, the unbanked often do not have an asset base to draw on. Hogarth and O'Donnell (1999) found that those with bank accounts were more likely than those without bank accounts to have credit cards, cars (loans), mortgages (and, thus, home equity), savings and insurance. It is known that a large percentage of American households have little or no savings

(reserves) for emergencies (Oliver and Shapiro, 1995), and this lack of a financial cushion is particularly disabling for those unbanked consumers who are subsidized by federal or state-level benefits, as it serves to keep them mired in their cycle of poverty. Stegman (1999) has suggested that as many as 75% of those on welfare may be unbanked. He further stated, “It is hard to imagine families successfully transitioning from welfare to work without having access to an affordable, secure bank account” (p. 9).

#### Who Are the Unbanked?

The unbanked population is assumed to be about 12-13% of the U.S. population. Various studies have found a variety of characteristics of the unbanked. According to Yip (2001), who cited a report by the Fannie Mae foundation, 25% of lower-income families are unbanked, with 33% of the unbanked being African-American, and almost 30% Hispanic.

Good (1999) found that the unbanked are more often in the low- to moderate-income bracket (incomes less than \$25,000), are uneducated, and are more often younger. Kim (2001a) cited that 40% of the unbanked earn less than \$10,000 per year. Scott (1988) divided the unbanked into segments with differing needs: students, the elderly, persons on welfare, the “marginally employed,” and those in the military.

Serres (2001) cited a North Carolina study undertaken by the Center for Community Capitalism at UNC-Chapel Hill, which found that nearly 17% of all low-income households in North Carolina do not have a bank account, with low-income African-Americans and Hispanics twice as likely not to have a bank account. Even more troubling, nearly half of the state’s recipients of Work First (a welfare program) were without a bank account. Higginbotham (1996) quoted a study by the General Accounting Office that found that three-quarters of those

on welfare do not have accounts, in addition to half of those on supplemental security income (SSI).

Caskey and Peterson (1994), in comparing households with bank accounts in 1977 and 1989 found that the unbanked tended to have certain characteristics: they had lower incomes, more children, were more often headed by an unmarried minority, unemployed, and had a less educated (female) parent. Rhine and Toussaint-Comeau (1999) also found, in their survey of Black Chicago consumers, that the unbanked were primarily less well-off, more often unemployed, younger, with less education, and more often female.

Hogarth and O'Donnell (1997), in their analysis of the 1995 SCF, found that 37% of African-American households and 29% of Hispanic households were unbanked, in comparison with 7% of White households. They found the unbanked were more likely to be female, younger, with a mean of 11 years of education, and with a lower mean income (\$14,077). They more often encompassed the unmarried and the unemployed. Rhine et al., (2001) also found that being unbanked is significantly correlated with the use of check-cashing outlets, with a greater likelihood of being unbanked by race (Black or Hispanic over White).

According to the 1995 SCF, nearly 40% of households with less than \$10,000 in annual income belonged to the unbanked (Doyle, Lopez and Saidenberg, 1998). By the 1998 SCF, 82.6% of families without checking accounts had incomes of less than \$25,000, 44.7% had incomes of less than \$10,000, 57.1% were Hispanic or non-White, and most were younger than 35 (Kennickell, et al., 2000).

Hogarth and Anguelov (2002) found that of those without checking accounts, more than half were below or at the poverty level, 58% were minorities, 46% were undereducated (less than 12 years of schooling) and 29% were unemployed. Sherraden (1991) quoted a Los Angeles

survey of the unbanked, done for the Center for the Study of Urban Poverty at UCLA, which found 20% of Los Angeles residents to be unbanked. This study also found that the unbanked had a large percentage of the working poor and 56% of welfare recipients. They were undoubtedly largely minority, with 37% of Hispanics being unbanked.

#### Banking System Trends That Contributed to the Increase in the Unbanked

According to Brobeck (1991) and Caskey (1994), the deregulation of the banking industry profoundly and negatively impacted low-income households. It was hoped that banking deregulation (which was in effect by 1985) would create greater efficiencies which would lower prices and provide incentives for technological and product improvements. However, the reality was that costs were redistributed from the private sector to the individual level, with the poor absorbing a disproportionate amount of these increased costs. Before deregulation, banks could only sell certain types of products. Also regulated were prices, ceilings on consumer loan products, and where products could be sold. At this time, bank accounts paid little or no interest and charged no or low fees. In the 1970s, banks faced intense competition from other types of institutions which were able to pay higher interest rates or charge less for loans.

During a time of high inflation and high interest rates, in 1980 a law was passed to protect the banking industry by, among other things, allowing interest to be paid on checking accounts. As a result, banks had to generate added revenue from new fees (notably, new minimum balance requirements) and had to look for other cost-cutting measures. From the late 70s to the early 80s, bank service charges doubled, and banks closed less profitable branches. Unfortunately, low-income households had little to gain from interest payments on their meager checking accounts, but much to lose from new service charges on services that were previously free. Brobeck (1991) found that in the early days after deregulation, many low-income

households dropped out of the banking system. These consumers, after all, were the least able to avoid higher service fees by keeping higher bank balances, and were more prone to be hit with high overdraft fees as their accounts were frequently drained by the end of the month. Caskey and Peterson (1994) also looked at data from the 1977 Consumer Credit Survey and the 1989 SCF to look at trends toward low-income banking both before and after deregulation. They found a great decrease in possession of savings accounts during that time frame, as well as a drop in the percentage of households with deposit accounts, with a large part of that drop being found in households with less than \$11,970 in annual income, as well as in minority households.

In the 80s, there was even more competition for financial services previously the domain of banks, which included better-paying mutual funds, national credit cards with better terms, national mortgage companies with better rates, and large automakers with their more competitive financing options. Banks increasingly looked toward newer and greater fees to remain competitive. According to *Consumer Reports* ("How Good," 1996), some 15% of all bank customers, "transaction hogs," create 60% of all teller-mediated transactions that are costly to the bank. Banks have found that charging for these expensive services helps to discourage their use.

Another outgrowth of this process has been a reduction in the number of bank branches, especially in poorer neighborhoods. Stegman (1999) noted that the number of banks in 1980 was 14,434, but by 1997 had dropped to 9,143, leaving perhaps 7,000 or less branches by 2000.

#### Banking Alternatives: The Alternative Financial Sector

The banking system in the U.S. is becoming more consolidated, with the net effect that larger national banks dominate the industry. These large banks more often have higher service fees, and the diminishing of competition in the industry will likely contribute to increasing trends in bank fees ("How Good," 1996). Shields (1996) noted that banks are "(1) increasing existing fees,

(2) inventing new fees, and (3) making it more difficult for accountholders to avoid fees” (p. 275). She found that while in 1991 there were 96 or so separate fees for services by banks, by 1996 there were over 250 individual fees. The banking industry maintains that a large percentage of banks today already offer low-cost banking options, but consumer advocates maintain that these are not marketed in any way to effectively reach those who need to know that they exist.

The alternative financial services sector is defined by Swagler, et al. (1996) as including rent-to-own stores, pawnshops, car title pawnshops, refund anticipation loans, check-cashing outlets, payday loans using post-dated checks, and money orders. Yip (2001) suggested that the alternative service provider industry can boast of around 280 million transactions per year, which earns it \$78 billion in annual revenue. It has been shown that many of the patrons of the alternative financial services sector do indeed have a relationship with a bank, in the form of a savings or checking account. Rhine and Toussaint-Comeau (1999) found this to be the case for 54% of the households in their study who had bank accounts and also used check-cashing outlets. Most alternative financial sector transactions involve immediate, small amounts of cash (Swagler, et al., 1995b), and use of this sector is generally an extremely expensive option.

According to Caskey (1994), high fees charged by this sector can in part be explained by other factors than mere usury. He explained that transactions are usually very small, and the costs of handling these multiple small transactions is higher than, say, for a credit card company that offers multiple computerized low-cost loans to more stable customers. For example, the labor costs that go into a transaction at a pawnshop are nothing like that of a large bank providing a small loan via mail. He suggested that volume for each outlet is small, given that the low-income clientele are not able to shop around and monopolize the services of the lowest-cost provider in the area. Providers must then open multiple outlets in convenient locations, rather

than one superstore. This also works the other way, since any fringe providers in an area have a quasi-monopoly on the customers in the area. There are also the added costs of working in a more dangerous industry (where large amounts of cash must be maintained in the outlets), in more dangerous locales, and with higher operating costs, costs of insurance, and other such expenses.

Those who use these types of services may not exactly be able to calculate APRs for the yearly use of the money (especially since it is not usually provided), but may understand the dollar amount of what they are paying to use the money for a short time. This may well be an acceptable tradeoff, given the absence of other, cheaper, immediately-available alternatives. Lewis, et al.'s (1996) respondents were aware of the extra expense involved with using the alternative financial sector. It is not certain, as Burton, Swagler and Lewis (1996) questioned, whether the alternative financial sector is an understandable market result of unmet needs of the unbanked or whether it is merely an unfortunate institution that "facilitates consumers' worst tendencies" (p. 280).

### *Check-Cashing Outlets*

Check-cashing outlets are nothing if not convenient—they are open long hours and weekends, and many are located on main-access roads and near public transportation. Check-cashers over time have shed some of their marginal image, and can now be found in suburbia and in less downtrodden areas. Check-cashers cash primarily paychecks and government benefit checks. Today, there are almost 10,000 check-cashing outlets in the U.S. (McCabe, 2000), having nearly doubled in the past decade, and the industry is dominated by two large companies, Ace Cash Express and Dollar Financial Group. Kim (2001b) cited that the industry cashes \$55 billion in checks each year, and revenues for the entire industry are over \$1.6 billion per year.

As check-cashing necessitates the liquidity of a large amount of cash in one transaction, many consumers opt to avail themselves of other services that check-cashing outlets so conveniently offer. Many check-cashing outlets offer money orders, wire transfers, tax refunds, utility bill payment, vehicle registration, notary services, transportation passes, and other impulse-type purchases such as phone cards, postage stamps, lottery tickets, copying and fax services, pagers, cellphones, and car insurance.

Check-cashers have been reviled by consumer advocates, but the reality is that they provide certain services that the unbanked appreciate. For one thing, check-cashing outlets are open for more than banker's hours; many are open Saturdays and evenings, at times when the working poor are more likely able to handle their financial needs. They also offer a variety of services in a one-stop shopping environment, which many of the unbanked find convenient to have in one place, such as money orders, wire transfers, lottery tickets, and bill paying. Squires and O'Connor (1998) found that one-fifth of those who use check-cashers explain that the convenient hours were the primary reason. Location was cited by about 15% as the most important reason. Thus, 25% used the words "convenience" or "ease"—it is easy to assume that convenient hours and location make up a good portion of the meaning behind these terms. And, most importantly, checks are immediately liquid—there are no lengthy bank holds, and no end-of-the-month surprise bank charges.

The industry is not well-regulated; merely 25 states regulate check-cashing (Stegman, 1999). Some states put a cap on check-cashing charges; many do not. Thus, check-cashing fees can range from 1.5-15% of the value of the check. Stegman (1999, p. 153) lamented the lack of regulation in the check-cashing industry, stating that "this lack of regulation [is] particularly striking given the amount of state and federal oversight over mainstream financial institutions,

which serve customers who are far more sophisticated and able to protect themselves than many check-casher patrons.” Regulating the industry harshly, according to Caskey (1994) and Swagler, et al., (1995b), however, can pose problems for the end consumer, since, for example, if ceilings on fees are too low, it can cause all but the largest urban outlets to close, leaving the consumer with few options and higher prices in general.

Critics of the industry cite that use of check-cashing services tends to drain the wealth of low-income consumers. According to Treasury estimates, such check-cashing fees would amount to \$15,000 over a lifetime (Moser, 2001). They also cite that it is often a disproportionate amount of minority consumers who often frequent check-cashers. According to Squires and O’Connor (1998), African-Americans make up half of check-cashing customers, with Latinos making up another 33%. Often this is because, as Jean-Paul and Nathan (1999) explained, most check-cashing customers avail of the “cash and carry” means of financial management. These customers tend to have little or no savings and value highly (such that they are willing to pay a premium for this) immediate liquidity with regard to their money. It may also be because check-cashers tend to be more prevalent in low-income areas. Squires and O’Connor (1998) found, in their study of the check-cashing industry in Milwaukee, Wisconsin, that check-cashing outlets in the city are often in low-income and non-White areas. They found that 32% of check-cashing businesses are found in such areas, but only 9% of banks are found in those same areas.

### *Pawnbrokers*

Pawnshops are also increasingly becoming more upscale, having shed their once-seamy image, and offering one-stop financial services shopping in much the same way as do check-cashers. They often have similar product offerings, but in some cases, much higher interest rates

than other fringe providers. Many even offer car-title loans. Caskey (1994) found that the average pawnshop customer had a low income, less than or equal to a high school education, and was usually in the 18-30 age range. A large percentage belong to a minority group, and were often unemployed or had irregular employment or frequent job changes. Unfortunately, it is often the case that customers of pawnshops are more concerned with the amount of the loan they are able to obtain for their pawned item than the terms and conditions of the loan agreement they are entering into (Caskey, 1994). This is consistent with Andreasen (1978), who suggested that

“anyone familiar with the purchasing behavior of the poor would be quick to point out that in shopping for credit the critical decision variables for them are not the rates of interest at various outlets, but (1) which outlets will in fact give them *any* credit at all and (2) what the monthly payments will be (i.e., what is the total cost and how many months do they have to pay it all off)” (p. 24).

#### Government Interventions

Congress introduced the Debt Collection Improvement Act of 1996 and the U.S. Treasury’s Electronic Funds Transfer Program (EFT ’99), dictating that by 1999 all government payments would be electronically deposited in banks to recipients. This led to the creation of the ETA, an electronic transfer account (partially subsidized by the government), which with its completely electronic technology-based orientation, would be less expensive for banks to operate. However, this new method had the potential for causing undue hardship for the unbanked. And, financial institutions balked at the new government initiative, fearing it would create the potential to shift costs and risk from the government to the financial services sector. It was to be a means of reducing government paperwork and expense to the tune of \$500 million in its first five years, as well as a way to eliminate the cost, hassle and potential for fraud for the 800,000 checks each year that are currently lost/stolen or damaged (Quinn, 1997). The government hoped to save vast amounts of money, when the cost of a 43-cent paper check is

compared to a 2-cent electronic payment. Perhaps this new legislation would be a “stepping stone” to cajole the unbanked into opening accounts at banks, some for the first time.

As originally planned, the Treasury was to allow only a select few banks to participate; instead, it opened the playing field to all who wanted to offer the service, hoping to allow the “market” instead of government fiat to put the policy into place. It was assumed that banks would jump on the opportunity to target a new customer base, especially with a small subsidy from the government. Unfortunately, the net effect for banks (since they had no exclusivity because all banks could offer the ETAs) was that there was little incentive, since each bank could only have a small piece of the customer pie, and therefore no bank aggressively began marketing this new account. Given the tepid response by the banking industry, the deadline for EFT was moved back one year, to January 2, 2000 (Stegman, 1999).

The other problem was with the waiver option for consumers for whom this would present a “financial hardship,” or those with disabilities or geographic limitations. It was ultimately decided to make waivers “self-certifying,” since the manpower did not exist for agencies to decide who should qualify for a waiver or not. As a result, the program was effectively watered down to a voluntary process, and it became obvious that the program might not have many followers, partly defeating the purpose. The final straw was when it was decided that waivers would be automatic for those who do not sign up for the program, essentially watering down the program even further. At present, it is hoped that the younger populations will increasingly embrace the direct deposit format, with lesser hope for the older generations who may fear the technology (Stegman, 1999).

Another issue with ETAs was whether the playing field should be limited to FDIC-insured banking institutions, or whether other alternative fringe bankers could be allowed to play

as well. It was finally decided that ETA-type products could only be offered by FDIC-backed financial institutions and not by fringe bankers, although the concession was made that if banks wanted to partner with fringe bankers on the back end of the transaction (by the customer voluntarily choosing an arrangement that allowed him/her to purchase financial services through a check-casher debit card through a bank, for example), that would be allowable. This was done for practical reasons, so that those who prefer not to deal with the banking industry would be able to continue dealing with the providers they prefer, but it would be the customer's choice. However, the caveat the Treasury insisted on was that the banking institutions would be required to provide adequate information about the fees and costs involved (Stegman, 1999).

To ensure that participating in ETAs did not impose additional costs on consumers, it was decided that there would be guidelines that banks had to use in creating ETAs. There would be a maximum monthly account maintenance fee of \$3, at least 4 free withdrawals per month, use of an ATM card to be used at the bank's ATM networks and point-of-sale terminals, no check-writing privileges, no minimum balance requirement, a free monthly statement, and the same consumer protections afforded other customers of that bank (Stegman, 1999).

There was also the assumption that the new deposits of government payments into the banking system would add more depository income for banks. However, most banks scoffed at this idea, since typical low-income accounts have low balances, and the float on these balances hardly adds to the bottom line of banks, who still lose money on such accounts that create more transactional costs for the bank but do not add revenue. Banks felt they could not make money on these EFT accounts, and that offering them would be a financial loss. However, many banks did already have similar "lifeline-type" accounts in place, so this was not felt to be a significant

hardship; also, Community Reinvestment credits could be offered to banks instead. In response, the Treasury offered a one-time carrot of \$12.60 for each account opened (Stegman, 1999).

One concession that was given to banks was their ability to screen new account-holders on the basis of their prior banking history. If they were reported to ChexSystems or had a previous bankruptcy or history of fraud (only in relation to a previous ETA), banks would be able to make the judgment call as to whether or not to provide them an ETA (Stegman, 1999).

By 2001, about 600 institutions having 13,000 branch offices were offering ETAs, and 8,700 ETAs had been opened (Rhine, et al., 2001), but 1,100 ETAs had also been closed as well (Kim, 2001a). Overall, to date, the program has not been a great success, when looked at in terms of the overall unbanked population.

EFT has the potential to be combined with other programs, such as Individual Development Accounts (IDAs) to create a comprehensive way for the unbanked to enter the mainstream financial services system. According to Stegman (1999), both banks and the unbanked could benefit. The banks would have more access to deposits from ETAs and IDAs, and the unbanked would have incentives to save and maintain their place in the mainstream. As Stegman (1999, p. 13) asserts, “EFT’99 is not simply about the technology of electronic banking. It is, above all else, about financial inclusion, closing the opportunity gap, and building assets for the future.”

## CHAPTER 3

### METHODS

It may be possible to explain the difference in Hispanic and non-Hispanic consumers in their use of traditional and alternative service providers by a number of reasons based on previously-cited literature, which fall into the following five categories: demographic reasons, economic reasons, language-related reasons, geographic reasons, and cultural reasons. Age and education may be important since prior research has suggested that the unbanked tend to be younger and less-educated; Hispanic households often tend to be comprised of persons who are younger and less-educated than the general population. Gender is also an issue, if Hispanic women or men tend to be more likely to be unbanked. Household income is another important factor, since prior research on the unbanked has suggested that they are typically from households with low incomes, another oft-mentioned characteristic of Hispanic households. Size of household is also a factor, since the number of children to support in a household may affect income levels. English literacy may be another factor, as many Hispanics continue to function in Spanish for segments of their daily lives, regardless of their generational status. Even the younger generations embrace their heritage and consistently tune into Spanish-language radio and television, a characteristic that seems to be different than for other assimilated ethnic groups. Location may also play a role. Those Hispanics who have gravitated to the West Coast (Los Angeles) may function differently from those on the East Coast (New York City). Finally, cultural reasons may also play a part, if Hispanics have little knowledge or experience with traditional financial institutions. Alternatively, negative experiences with banks in their

homelands may have colored their perceptions toward mainstream financial institutions in a very unfavorable direction, adding to a general distrust of these organizations. Unfortunately, because of limitations of the scope of the dataset used, cultural differences cannot be explicitly explored in this study.

Thus, it is hypothesized that demographic factors (age, education, and gender), economic factors (household income and size of household), language-related factors (English literacy), and geographic factors (location) influence Hispanics' non-use of banks and use of alternative financial sector options. Controlling for these factors will bear this out.

To test the four hypotheses of this study, two separate hierarchical models were used, and logistic regression analysis was employed. In all four cases, the dependent variable was dichotomous, and thus logistic regression was the obvious choice for the statistical analyses.

H1a: Hispanics will be more likely to be unbanked than non-Hispanics.

H1b: There is no difference between Hispanics and non-Hispanics in being banked or unbanked, when other factors are controlled (age, educational level, gender, household income, household size, English literacy, and location).

H2a: Hispanics will be more likely to use alternative financial services than non-Hispanics.

H2b: There is no difference between Hispanics and non-Hispanics in using alternative financial services, when other factors are controlled (age, educational level, gender, household income, household size, English literacy, and location).

### Research Design

This study uses an *ex post facto* cross-sectional multivariate design. The Office of the Comptroller of the Currency's Survey of Financial Activities and Attitudes, conducted in 1998-

1999, has a usable sample size of 2,006 respondents, of whom 1,002 were from New York City and 1,004 were from Los Angeles (note that 1 response was unusable). The survey involved computer-aided interviews, of which approximately 1,000 were conducted in each location, one-half via telephone and one-half in the respondent's home. The complex, computer-aided interviews were composed of various branches (nesting) and allowed the 245-question instrument to be more flexible and more tailored to the specific choices of the respondent. In the entire dataset, 922 observations are for Hispanic subjects and 1,052 are for those who are not Hispanic. The remaining observations fall into the categories of "Don't Know" and "Refused to Answer," and for the purposes of this research, they have been incorporated into the category of non-Hispanic (which includes Black, White, Asian, American Indian, Native Hawaiian or "another race"). The researchers of this dataset used a multi-stage stratified random sample design. For the first step of their three-stage sampling plan, they purposively chose New York City and Los Angeles for their sample, instead of conducting a nationwide sample. They state,

"we selected New York and Los Angeles as survey sites based on information developed in the literature review and obtained from OCC compliance examiners...[which] showed that New York City and Los Angeles are among the top few areas in the U.S. with large clusters of innovative bank practices intended to reach the traditionally unbanked. In those two areas the Survey may provide useful baseline data, to which the results of future surveys may be compared. This comparison could reveal which bank efforts have been most effective in reaching and servicing the nonbanked" (Dunham, Scheuren and Willson, 1998, p. 613).

Indeed, the largest majority of Hispanics have settled in these two cities. This makes the survey representative of large, and often majority populations of Hispanics from Mexico, Puerto Rico, El Salvador, the Dominican Republic, Columbia, Guatemala, Ecuador, Peru, Honduras, and Panama (Winsberg, 1994).

In the second stage, they chose a total of 21 Census tracts in each city, which were selected with “probabilities proportional to an estimate of the size of the nonbanked population within each tract” (Dunham et al., 1998, p. 613). The 1990 Census tracts were “stratified by income (low or moderate) and race and ethnicity (predominantly White, predominantly Black, and predominantly Hispanic), plus an integrated low- and moderate-income stratum” (Dunham et al., 1998, p. 613), and they chose three tracts from each stratum. Thus, the second stage employed proportionate stratified random sampling.

By the third stage, they looked at specific addresses in the sampled Census tracts, via a single, area sampling frame. This necessitated creating thorough lists of addresses for each of the Census tracts they surveyed, which was followed up by a match with telephone numbers. The researchers employed a “dual-mode” method of sampling (in-person and telephone interviews) to achieve their hoped-for 75% response rate (the 73% they ultimately reached was near target). Other modes were also used if the first two failed, such as the provision of a toll-free number for the respondent to call back and repeated means of reaching the respondent at a more convenient phone or in-person time.

## Data Analysis Procedures

### *Variables*

A summary of all variables (two dependent and fifteen independent variables) used in this study are provided in Table 1. The first dependent variable (being unbanked versus being banked) is taken from the dataset, from a question that attempts to answer whether the respondent does or does not have a checking account. While other types of accounts are listed, the account of primary interest is whether or not the respondent uses a checking account. Other types of accounts at banks (savings accounts, for example) are less actively transactional, and

checking accounts are more sophisticated than other types of accounts to maintain successfully. UNBNKD was recoded to make it a dichotomous variable, and was recoded such that 1=unbanked (not having a checking account) and 0=banked (having a checking account). The second dependent variable, AFSUSE, looks at the variety of alternative financial sector services used by the respondents in the past three years. The dataset gives eleven options of alternative financial sector services (credit card cash advances, borrowing from a thrift plan or life insurance policy, buying on a layaway/installment plan, pawning at a pawn shop, obtaining a rapid tax refund/refund anticipation loan, obtaining a loan from a rotating credit society, renting from a rent-to-own store, leasing a car or truck, having someone co-sign or guarantee a loan, and obtaining a land contract for a house). Note that a respondent could indicate that they used none of these services in the past three years, which is option number eleven. In the actual dataset, there are five columns of recorded data. In the first column, it is recorded whether one such behavior was undertaken by the respondent in the last three years. If the respondent offered one such behavior, then the second column records whether another such behavior occurred, and so on, up to five total responses. Each column notes the behavior that took place (a “3,” for example, means that the respondent bought something on an installment or layaway plan in the past three years). As a consequence, there is enough information for recoding in a binary, 0/1 format each of the ten answers (in ten separate columns) for all of the members of the total sample, denoting whether they did or did not engage in that particular behavior. All ten items recoded in this way produced columns that were totaled. Thus, after recoding, it became possible to know how many respondents from the entire dataset actually “bought something on a layaway or installment plan,” for example. The variables have been recoded as AFS1-AFS10. Since a frequency analysis done on this variable showed that nearly 74% of the respondents did not partake in any one of

these behaviors, and about 19% and 5%, respectively, engaged in one and two behaviors (nearly two percent used more than two alternative financial services), it was necessary to collapse the categories to make this a dichotomous dependent variable. Thus, a new variable was created, AFS0\_1, where the data were recoded such that 1=using 1 or more alternative financial services and 0=using no alternative financial services.

The first and primary independent variable of interest is whether or not the respondent is Hispanic or non-Hispanic (HISPANIC). This is taken from a self-report item in the questionnaire, and was recoded such that 1=Hispanic and 0=non-Hispanic. Age of the respondent has five categories, where 1=18-29 years old, 2=30-39 years old, 3=40-49 years old, 4=50-64 years old, and 5=65 and older. CATAGE1 is the first category of age, which was the omitted category for reconfiguring this variable into dummy variables. This variable was recoded into four dummy variables, CATAGE2, CATAGE3, CATAGE4, and CATAGE 5. Educational level of the respondent exists in four categories in the dataset, where 1=less than 6<sup>th</sup> grade, or no formal schooling; 2=6<sup>th</sup> to 11<sup>th</sup> grade, no GED, or attended trade school or apprentice program (if no GED or 12<sup>th</sup> grade education); 3=12<sup>th</sup> grade, or passed GED, whether or not attended trade school or apprentice program; and 4=more than 12<sup>th</sup> grade. This was recoded into dummy variables, CATEDU2, CATEDU3, and CATEDU4, with CATEDU1 being the first and omitted category. Gender (GNDR) exists in the dataset as a dichotomous variable, and was recoded such that 1=female and 0=male. Household income of the respondent's household (HHINC) was recoded such that 0=less than or equal to \$30,000 per year and 1=more than \$30,000 per year. Household size describes the number of children under 18 (i.e., dependents) present in the household. Four categories exist in the dataset: 0 children, 1 child, 2 children, and more than two children. This was recoded into three dummy variables:

CATHHS1, CATHHS2, and CATHHS3, with CATHHS0 being the first and omitted category. English literacy level of the respondent (ENGLIT) corresponds to the LFLAG variable that exists in the dataset, which explains which language the interview was conducted in. The reasoning is that if the respondent “chose” to do the interview in Spanish, their day-to-day fluency, especially for complex financial matters, would be in Spanish, rather than in English. This was recoded, such that 1=Spanish and 0=English. Finally, the LOCATE variable is taken from a question in the dataset that states which city the respondent was from. This was recoded, such that 1=New York City and 0=Los Angeles.

### *Statistical Techniques*

For the first two hypotheses (1a and 1b), the log odds of being unbanked were examined, where the model was estimated via the maximum likelihood technique. Logistic regression was used in this analysis since the dependent variable was dichotomous. Recall that being banked or unbanked was recoded to make it a binary (0, 1) variable. Thus, logistic regression estimated the probability of being unbanked, after having transformed the dependent variable to a logit variable. The log odds of the dependent variable changing in the analysis was calculated using logistic regression and maximum likelihood estimation techniques.

In the baseline regression, the log odds of being unbanked was regressed only on the one independent variable of being Hispanic. In the next equation, the other variables were added, namely, age, educational level, gender, household income, household size, English literacy, and location (New York or Los Angeles). In both cases, the global test for logistic regression, the model chi-square test, was employed to test the appropriateness of the model. The Wald statistics were used to test the significance of individual independent variables, and a comparison of the two models was conducted using the well-known likelihood ratio test. Finally, the

Pseudo-R<sup>2</sup> measured the strength of association, and it is similar to the R<sup>2</sup> in its interpretation.

The two logistic regression equations were as follows:

$$\text{Log}(\text{UNBNKD}/1-\text{UNBNKD}) = a + B_1\text{HISPANIC} + e$$

$$\begin{aligned} \text{Log}(\text{UNBNKD}/1-\text{UNBNKD}) = & a + B_1\text{HISPANIC} + B_2\text{CATAGE2} + B_3\text{CATAGE3} + \\ & B_4\text{CATAGE4} + B_5\text{CATAGE5} + B_6\text{CATEDU2} + B_7\text{CATEDU3} + B_8\text{CATEDU4} + \\ & B_9\text{GNDR} + B_{10}\text{HHINC} + B_{11}\text{CATHHS1} + B_{12}\text{CATHHS2} + B_{13}\text{CATHHS3} + \\ & B_{14}\text{ENGLIT} + B_{15}\text{LOCATE} + e \end{aligned}$$

For the second set of hypotheses (2a and 2b), logistic regression was again used, in two separate regressions, with the dependent variable being the log odds of alternative financial sector (AFS) use. In the baseline regression, the log odds of AFS use was regressed only on the one independent variable of being Hispanic. In the next equation, the other variables used in the above logistic regression were added. In both cases, the global test for logistic regression, the model chi-square test, was employed to test the appropriateness of the model. The Wald statistics were used to test the significance of individual independent variables, and a comparison of the two models was conducted using the well-known likelihood ratio test. Finally, the Pseudo-R<sup>2</sup> measured the strength of association. The two logistic regression equations were as follows:

$$\text{Log}(\text{AFS0}_1/1-\text{AFS0}_1) = a + B_1\text{HISPANIC} + e$$

$$\begin{aligned}
\text{Log}(AFS0\_1/1-AFS0\_1) = & a + B_1\text{HISPANIC} + B_2\text{CATAGE2} + B_3\text{CATAGE3} + \\
& B_4\text{CATAGE4} + B_5\text{CATAGE5} + B_6\text{CATEDU2} + B_7\text{CATEDU3} + B_8\text{CATEDU4} + \\
& B_9\text{GNDR} + B_{10}\text{HHINC} + B_{11}\text{CATHHS1} + B_{12}\text{CATHHS2} + B_{13}\text{CATHHS3} + \\
& B_{14}\text{ENGLIT} + B_{15}\text{LOCATE} + e
\end{aligned}$$

Understanding the difference between Hispanic and non-Hispanic consumers in their use of traditional and alternative service providers will hopefully add to the literature, especially if the reasons for the differences can be seen as belonging to distinct categories, such as demographic or economic reasons, for example. In this chapter, the variables used in this research, the research design, and the statistical methods used were explained. The results of these data analyses will be explicated in the next chapter.

## CHAPTER 4

### RESULTS

In this chapter, results of the statistical analyses to test hypotheses 1a, 1b, 2a and 2b are presented. This section is divided into four parts. The first section describes the results of the correlation analyses for all the variables. Next, descriptive statistics are presented. Finally, the results of testing hypotheses 1a, 1b, 2a, and 2b via logistic regression are presented. The results are interpreted in light of the hypotheses.

For hypotheses 1a and 1b, Model One (the baseline model) used UNBNKD as the dependent variable, with Hispanic as the only independent variable. Recall that Hypothesis 1a predicts that Hispanics will be more likely to be unbanked than non-Hispanics. Thus, Model One tests the null hypothesis that being Hispanic does not predict being unbanked. Model Two (the full model) estimates the effect of being Hispanic, while adding all other variables to the model as well. This includes age, educational level, gender, household income, household size, English literacy, and location. Recall that Hypothesis 1b predicted that there is no difference between Hispanics and non-Hispanics in being banked or unbanked, when other factors are controlled. Thus, the full model tests the null hypothesis that the above independent variables, added to the Hispanic independent variable of the first model together do not predict being unbanked. The individual null hypotheses for each variable suggest that there is no relationship between that independent variable and being unbanked.

Similarly, for hypotheses 2a and 2b, Model One (the baseline model) included only Hispanic as the independent variable, since Hypothesis 2a predicts that Hispanics will be more

likely to use alternative financial services than non-Hispanics. Thus, Model One aimed to test the null hypothesis that being Hispanic does not predict greater use of alternative financial sector services. Model Two (the full model) estimated the effect of Hispanics, while adding in all the other variables, as described above for Hypothesis 1b. Recall that Hypothesis 2b predicted that there is no difference between Hispanics and non-Hispanics in using alternative financial sector services, when other factors are controlled. Thus, the second model aimed to test the null hypothesis that the above independent variables, added to the Hispanic independent variable of the first model together do not predict greater use of alternative financial sector services. The individual null hypotheses for each variable are that there is no relationship between that independent variable and greater use of alternative financial sector services.

#### Correlation Analysis

Table 2 presents the correlations between the dependent and independent variables. The correlation analysis provides useful information in determining if multicollinearity exists among the variables. While four of the Pearson correlation coefficients are between 0.43 and 0.58, none are greater than 0.70, suggesting that multicollinearity is not a problem in this analysis.

As can be seen from Table 2, only a few variables appear somewhat significantly correlated with being unbanked. These are English literacy, location, household income, 6<sup>th</sup>-11<sup>th</sup> grade education, and having greater than a 12<sup>th</sup>-grade education. Likewise, two variables appear to be somewhat correlated with AFS use: household income and education greater than 12<sup>th</sup> grade.

#### Descriptive Analyses

Table 3 presents the means on all variables, for all members of the sample, for the Hispanic subsample, as well as for the non-Hispanic subsample, for those who are banked and

those who are unbanked. As can be seen, in the total sample, there are 2,006 observations, of which 1,096 are banked and 910 are unbanked. In the Hispanic subsample, 386 are banked and 567 are unbanked. Finally, in the non-Hispanic subsample, 710 are banked and 343 are unbanked. Means in this table represent percentages of respondents in each category, and those that are statistically significant are interpreted as follows.

Looking first at gender, it can be seen that among Hispanics 48% of the banked were female while 58% of the unbanked were female. Similarly, 38% of the banked spoke Spanish, while 58% of the unbanked spoke Spanish. Looking at coastal locations, 36% of the banked lived in New York City and 58% of the unbanked lived in New York City. Fifty-one percent of the banked had a household income greater than \$30,000, while only about 15% of the unbanked had a household income greater than \$30,000. Looking at education levels, 4% of the banked had education levels of less than 6<sup>th</sup> grade, while 11% of the unbanked had education levels less than 6<sup>th</sup> grade. Further, 28% of the banked had a 6-11<sup>th</sup>-grade education, while 49% of the unbanked had a 6<sup>th</sup>-11<sup>th</sup>-grade education; and 39% of the banked had a 12<sup>th</sup>-grade education/GED, while 31% of the unbanked had this level of education. It can also be seen that 29% of the banked had more than a high-school education, while only 9% of the unbanked did so. Finally, 12% of the banked had more than two children in the household, while 21% of the unbanked had more than two children in the household.

For non-Hispanics, 42% of the banked lived in New York City, while 71% of the unbanked lived in New York City. Fifty-nine percent of the banked had a household income of more than \$30,000 per year, while only 24% of the unbanked had the same level of household income. By age, 15% of the banked were in the age 18-29 category, while for the unbanked 25% were in this category; and 27% of the banked were in the age 40-49 category, while only 18% of

the unbanked were in this age category. By education level, not even 1% of the banked had less than a 6<sup>th</sup>-grade education, but 4% of the unbanked were in this education category; 12% of the banked had an education level between 6<sup>th</sup> and 11<sup>th</sup>-grade, while 27% of the unbanked were in this education category. Further, 34% of the banked had a 12<sup>th</sup>-grade education/GED, while 48% of the unbanked were in this education category; and 53% of the banked had more than a 12<sup>th</sup>-grade education, while only 19% of the unbanked were in this education category. By household size, 61% of the banked had no children in the household, while 54% of the unbanked had no children in the household. Finally, 6% of the banked had more than two children in the household, while 10% of the unbanked were in this category.

Table 4 presents the means on all variables, for all members of the sample, for the Hispanic subsample, as well as for the non-Hispanic subsample, for those who used alternative financial services and those who did not. As can be seen, in the total sample, there are 2,006 observations, of which 526 used alternative financial services and 1,480 did not. In the Hispanic subsample, 215 used alternative financial services and 738 did not. Finally, in the non-Hispanic subsample, 311 used alternative financial services and 742 did not. As in Table 3, means in this table represent percentages of respondents in each category, and those that are statistically significant are interpreted as follows.

Looking first at location, it can be seen that among Hispanics, 40% of those using AFS lived in New York City, while 52% of those not using AFS lived in New York City. Forty-two percent of those using AFS had household incomes greater than \$30,000 per year, while for those not using AFS only 26% did. Looking at age, 2% of those using AFS were age 65 or older, while 7% of those not using AFS were in this age category. By education, 32% of those using AFS had between a 6-11<sup>th</sup>-grade education, while 43% of those who did not use AFS had

the same level of education. Finally, 26% of those using AFS had greater than a 12<sup>th</sup>-grade education, while only 14% of those who did not use AFS had the same level of education.

Similarly, looking at the non-Hispanic subsample, we can see that with gender, 48% of those using AFS were female, while 57% of those who did not use AFS were female. Forty-three percent of those using AFS lived in New York City, while 54% of those not using AFS did so. Looking at household income, 66% of those using AFS had a household income greater than \$30,000 per year, while 40% of those not using AFS fell in the same income category. By age, 9% of those using AFS were 65 years of age and over, while 16% of those not using AFS were in that age category. Finally, by education levels, 26% of those using AFS had a 12<sup>th</sup>-grade education or GED, while 44% of those not using AFS had the same level of education; and 60% of those using AFS had an education level of greater than 12<sup>th</sup>-grade, while 35% of those not using AFS had the same level of education.

These univariate comparisons using sample means are useful in speculating about the population means. They also suggest that further evidence for these relationships may be found in the multivariate analyses that were conducted next, and which are detailed below.

#### Logistic Regression Analysis for Hypotheses 1a and 1b

This section describes the results of the logistic regression analyses conducted to test hypotheses 1a and 1b, which predicted that Hispanics would be more likely to be unbanked than non-Hispanics, and then with other factors controlled, that there would be no difference between Hispanics being banked or unbanked. In order to test the first two nested hypotheses, two logistic regressions using maximum likelihood techniques, were conducted. As the dependent variable is dichotomous (being banked or unbanked), it was necessary to use logistic regression for testing these two hypotheses.

The results for Model One are shown in the second and third columns of Table 5. The Chi-Square for the overall model shows that Model One is significant. The last two columns of Table 5 report results for Hypothesis 1b (Model Two). Once again, the Chi-Square for the full model is significant. The baseline model (Model One) produced a log likelihood ratio of 1307.84 and a model chi-square of 147.95, versus the full model log likelihood ratio of 1053.58 and a model chi-square of 656.48. A likelihood ratio test comparing Model One and Model Two revealed that Model Two was an overall better fit to the data (chi-squared=508.53,  $p < .001$ ). The statistically significant model chi-squares for Model One and Model Two suggest that we may reject the null hypothesis and conclude that, globally, at least one of our independent variables has a significant amount of prediction ability.

Hypothesis 1a, that being Hispanic is associated with being unbanked, is supported by the data. Hypothesis 1b, that other factors are associated with determining who will or will not be unbanked than merely being Hispanic, is supported as well. It has been shown that being Hispanic is associated with a greater likelihood of being unbanked. Interpreting the odds ratios indicates that Hispanics are 3.041 times more likely than non-Hispanics to be unbanked. However, by the second model, the effect of being Hispanic declined from 3.041 to 1.383, remaining statistically significant. This indicates that being unbanked is in part associated with English literacy, location, household income, age, education, and number of children in the household.

The pseudo-R-squared value shows the efficacy of prediction of the set of independent variables for the dependent variable, compared with the null model hypothesis. The pseudo-R-squared of Model Two of 0.2375, compared to that of Model One (0.0535) shows that the model with the numerous independent variables improves the prediction of being unbanked by about

23% compared to chance or to the null model, versus the greatly reduced 5% of the baseline model (Model One). Additionally, the coefficients were tested for significance using the Wald Chi-Square statistic. The Wald Chi-Square for each independent variable shows that a number of independent variables were indeed significant.

The odds ratios for the variables in Model Two are shown in the last column of Table 5. Only the significant odds ratios are discussed below. It can be seen from the table that those who speak Spanish were 1.772 times more likely to be unbanked than those who speak English. Respondents who lived in New York City were 2.677 times more likely to be unbanked than those who live in Los Angeles. All else held constant, those in households with incomes greater than \$30,000 per year had a likelihood of being unbanked that is only .266 of those with household incomes of less than \$30,000 per year. By age distinctions, those in the 30-39 age category had a likelihood of being unbanked that is .618 of those in the 18-29 age group. Those in the 40-49 age group had a likelihood of being unbanked that is .527 times as large as those in the 18-29 age group, and respondents in the 50-64 age group had a likelihood of being unbanked that is .494 as large as those in the 18-29 age group. Finally, those in the 65 and over age group had a likelihood of being unbanked that is .369 as large as those in the 18-29 age group. Examining education, those with a 12<sup>th</sup>-grade education/GED had a likelihood of being unbanked that is .393 as large as those in the less than 6<sup>th</sup>-grade education group. Those with a greater than 12<sup>th</sup>-grade education had a likelihood of being unbanked that is .173 as large as those with a less than 6<sup>th</sup>-grade education. Finally, those with more than two children in the household had a likelihood of being unbanked that is 1.694 times as large as those with no children in the household.

## Logistic Regression Analysis for Hypotheses 2a and 2b

This section describes the results of the other logistic regression analyses conducted to test hypotheses 2a and 2b. In order to test the first two nested hypotheses, two logistic regressions using maximum likelihood techniques, were conducted. As the dependent variable was recoded to make it dichotomous (AFS use or non-use), it was necessary to use logistic regression for testing these two hypotheses as well.

The results for Model One are shown in the second and third columns of Table 6. The Hispanic coefficient is negative, as opposed to what was hypothesized, suggesting less AFS use by Hispanics overall. This contradicts Hypothesis 2a, and thus, Hypothesis 2a is not supported by the data. For Hypothesis 2b, which suggests no difference in AFS use between Hispanics and non-Hispanics, when other factors are added, the null hypothesis cannot be rejected. Of significance were the variables of location, household income, age 65 years or greater, and having greater than a 12<sup>th</sup>-grade education. Thus, as seen in the last column of Table 6, those who live in New York City have a likelihood of using AFS that is .751 times as large as those who live in Los Angeles. Those with a household income of greater than \$30,000 per year have a likelihood of using AFS that is 1.965 times those with household incomes of less than \$30,000 per year. Age greater than or equal to 65 produces a likelihood of using AFS that is .624 times those in the 18-29 age group, and finally, those with an education level of more than 12<sup>th</sup> grade have a likelihood of AFS use that is 2.092 times that of those in the less than 6<sup>th</sup>-grade level category.

## CHAPTER 5

### SUMMARY AND IMPLICATIONS

In summary, the results of the logistic regressions suggest many reasons why Hispanics are more likely to be unbanked. Of significance are speaking Spanish and living in New York City. Higher levels of household income are negatively associated with being unbanked, as are higher age categories, higher education levels, and fewer children in the household. Thus, it can be concluded that being unbanked is associated with demographic characteristics (age and education), economic characteristics (household income), language-related characteristics (English literacy), and geographic characteristics (location). In addition, the odds ratio drops significantly from Model One to Model Two, from 3.041 to 1.383. From the literature search, it does not seem that any other study has found such a significant drop, which would provide ample support for the necessity for understanding the other variables that contribute more to being unbanked than merely being Hispanic.

The results of the baseline model from the second group of logistic regressions having to do with AFS use showed that the coefficient of the Hispanic variable occurred in a direction opposite to what was hypothesized, namely that Hispanics use alternative financial services less than non-Hispanics, and found no difference in use for the full model. It may be suggested, however, that the specific alternative financial services on which data was collected for the original dataset *are not in fact the behaviors* that Hispanics would be likely to engage in. A different study using different data might uncover alternative findings.

The fact that H2a and H2b in this study are not wholly supported is of importance since it shows that Hispanics may not indeed be using alternative financial sector services at all. Perhaps Hispanics do not use these services, and use other services instead. Perhaps they are no more likely to use alternative financial sector services than non-Hispanics. Again, this is fodder for future research.

### Strengths and Limitations of Research Design

Using an *ex post facto* cross-sectional multivariate design with a large sample size helps to mitigate some of the threats inherent to such designs. However, the internal validity threat of ambiguity of causal direction is still present, and it is not possible to determine causality with complete certainty. It may be possible to say that there is a relationship between being Hispanic and being unbanked, but it is not possible to apply this to all Hispanics. Also, the variation among subjects in the dependent variable that is observed (being unbanked) could also be explained by other factors that have not been considered, even as we have tried to account for age, educational level, gender, household income, household size, English literacy and location. As far as external validity, this study creates findings that are not representative of all Hispanic-Americans, and are only generalizable to Hispanics in New York City and Los Angeles County. Such “urban” Hispanics (those who have chosen to settle in large metropolitan areas such as New York City and Los Angeles) have characteristics that are presumably different from those who have not chosen to live in two of the largest U.S. cities. Also, two different coasts are represented, one of which likely has more “early adopters” of innovative practices than the other, and all this makes generalization to Hispanics living in other parts of the country in smaller cities and towns less tenable.

The original researchers also agree that there were problems involved in designing such a complex and lengthy survey of such scope, which is not surprising, since very little data has previously been obtained on the unbanked, much less the Hispanic unbanked. Their first and most important problem was the highly sensitive nature of the study's aim—getting at complex and often personal information about how a household conducts its financial activities (it is also difficult to know if respondents answering in the comfort of their own homes can give answers that would mirror their actions in real-life stressful marketplace conditions, or those that are more “wishful thinking”). And, since prior information on the subject was scarce, it was necessary to design a pilot study, enlisting the knowledge of various experts in the field to hope to get at the constructs needed to carry out the final survey correctly. Thus, it was decided that interviews would be both in-person and by telephone, but both methods create difficulties, especially for Hispanic populations who may be more likely not to have telephones or be literate (or financially literate) enough to participate fully in the interview. The study designers hoped to achieve a 75% response rate, and the two-mode approach to reaching respondents allowed for either method to be used to finally reach difficult targets (Dunham et al., 1998).

Finally, other issues related to the design include length of the survey instrument, which might lead to fatigue on the part of the respondent, the fact that “random” in fact meant that whoever was in the household chosen at that time over the age of 18 was used as a respondent (elderly grandmothers and 19-year-olds may not have the sophistication to answer such detailed questions about the households' banking activities, for example), and privacy issues relating to the very sensitive topics discussed in the survey which may have precluded giving anything but socially-acceptable responses. Subjects may have been intimidated by the interviewer, and perhaps unconsciously coerced into giving answers they believed he/she wanted to hear. A self-

report questionnaire, which would not have involved as an intermediary the data-gatherer, might have elicited responses that may have been less censored by the respondent; this is difficult to ascertain.

### Future Research Directions

Future research may wish to explore Hispanic consumers in various geographic settings, which could include both urban and rural environments. Looking at cities where banking institutions are fairly distributed geographically, versus cities where financial institutions are scarce, may point to differing reasons for remaining unbanked. It may also be necessary to clearly define what constitutes being “banked.” Various studies have differing definitions of being banked (having a checking account only, having a savings account only, having mostly a non-transactional type of account, etc.). Specificity in describing what constitutes being banked would help in allowing differing studies to be compared more easily. The notion of who is “Hispanic” is also up for debate. This ethnic group defies “easy classification” because of the many routes that one can take to be considered Hispanic (Hispanic by birth to two Hispanic parents, Hispanic by surname alone, Hispanic by ancestry of one parent, Hispanic through marriage, etc.), especially in self-report data, and this ambiguity also significantly affects the comparability of results obtained. One nationally-representative dataset may consider Hispanics as embodying certain criteria, while another may have an entirely different set of criteria. What constitutes being Hispanic is thus terribly confusing, and in reality, not at all consistent in the literature. There may also be differences between first-generation Hispanics and those who have been in the U.S. for several generations, or between those hailing from differing Spanish-speaking countries. Finally, it may be that the alternative financial sector services used in this dataset are different from those that are actually used by Hispanic consumers. For example, Hispanics tend

to purchase wire transfers for remitting money home to families in their countries of origin (as many Hispanics do not have the intention of residing permanently in the U.S.); perhaps Hispanics' use of wire transfers as a means of payment could be further explored. It may be that using alternative financial sector services that are more relevant to Hispanic consumers might provide support for these hypotheses in future research. Thus, there is no shortage of ideas that may be suggested for future research, as the topic of Hispanic consumers' banking activities has hardly been scratched.

#### Implications for Banks, Public Policy Makers or Financial Practitioners

Despite the above limitations, there is much that can be gleaned from this research. This study has determined that Hispanics are more likely to be unbanked than non-Hispanics. Of significance in the study were the variables of English literacy (those who more often spoke Spanish), those residing in New York City, those with lower household incomes, younger respondents, and those who have less education. None of this is surprising, given prior research on the unbanked, which show the unbanked as more often with low to moderate incomes, uneducated and younger. However, as a growing and very large segment of the U.S. population, Hispanics are more disadvantaged in the marketplace if their language preferences create more of a hindrance to them than to other non-Spanish-speaking consumers. Given that they often engage in "cultural refueling" and maintain strong ties to their language and neighboring homelands (Mexican-Americans, most especially), their language handicaps in the financial services marketplace may be a cause for particular concern.

While it may be that being unbanked is a rational choice for some consumers, as explained earlier in the section on "Reasons for Not Banking," of which there are indeed many, there are almost equally as many disadvantages to being unbanked. These, mentioned earlier as

well, are particularly challenging; however, perhaps the most important long-term effect of remaining in the fringe of the financial services marketplace is a lack of access to asset-building and accumulation. Aside from the economic limitations of having no access to assets and financial reserves, there is a psychological burden as well. Being unbanked has been shown to have a negative effect on asset-building and accumulation. Sherraden (1991, p. 5) states that “Income only maintains consumption, but assets change the way people think and interact in the world. With assets, people begin to think in the long-term and pursue long-term goals. In other words, while incomes feed people’s stomachs, assets change their heads.” Obviously, being banked is related to establishing good credit, purchasing consumer durables (cars, homes, etc. on loan), and saving (savings accounts, CDs, IRAs, and other investment vehicles), all of which lead to asset-building and accumulation. Sherraden (1991) has argued that acquiring assets (such as a bank account) has a circular effect, bringing added benefits of knowledge about credit, investing and saving. The acquiring of one brings about knowledge of the others. Assets are also used in a positive cycle to create *more* income.

Furthermore, Sherraden (1991) has also maintained that certain consumers (the non-poor) are able to take advantage of systems of asset accumulation that are provided to them by government policy. He asserts that savings by the non-poor are not obtained by any “superior” ability of the non-poor to save. Instead, the non-poor are more often exposed to institutionalized processes that assist in asset accumulation. Beverly and Sherraden (1999) also found that incentives and institutionalized saving methods promote saving among households, but that low-income families typically do not have access to these methods of promoting financial discipline. As one example, home ownership is usually a household’s first form of asset accumulation and a large source of wealth generation. Homeowners have access to tax advantages that provide a

financial incentive to saving and asset accumulation. The same goes for retirement pensions that are tax-deferred. Both of these large forms of asset accumulation also tend to be handed down intergenerationally, further adding to the advantages of the next generation.

According to Sherraden (1991, p. 148), assets have nine benefits:

“they improve household stability, create an orientation toward the future, stimulate development of other assets, enable focus and specialization, provide a foundation for risk-taking, increase personal efficacy, increase social influence, increase political participation, and enhance the welfare of offspring.”

He further elaborates that assets improve household stability by providing a bridge during difficult times of financial stress for the household. Even a less-liquid asset such as home equity can be exchanged for credit during times of financial instability for the household. The long-termness inherent in collecting assets allows a family to turn from short-term survival to longer-term optimism and goal-setting. Assets also allow for the development of other assets, such as human capital. Or, alternatively, financial capital creates human capital, since those who have assets necessarily seek out more knowledge about additional asset accumulation. Asset accumulation allows for focus and specialization. Career advancement takes place through specialization and acquiring of specific skills via higher education or special training. Greater risk-taking allows for greater diversification of assets and possible higher rates of return, and a greater supply of assets can absorb shocks from losses from taking such risks. Increased personal efficacy comes about through greater personal control. Increases in social influence allow for a “superior position in social interactions,” thereby leading to the perception of higher social status and the perks in the marketplace that come about as a result. Participation in politics comes about as a result, since asset-holders have a “stake” in the political economy. Finally, as assets can be handed down to future generations, offspring may benefit as a result of the headstart in life that assets provide. Sherraden (1991, p. 295) sums it up, “simply put, when

people are accumulating assets, they think and behave differently and the world responds to them differently as well.”

It is hoped that this research can generate new knowledge on at least one rapidly-growing segment of the unbanked. Better niche marketing and solutions tailored to the Hispanic unbanked could follow from this research, perhaps from banking and other financial institutions. Critics have maintained that one of the greatest reasons for being unbanked is that banks fail to serve low-income consumers’ banking needs. Banks point to the high cost of maintaining branches in low-income areas, because of the greater number of small-sized transactions, which translate into high labor costs for banks. Low balances that are often found in accounts in these neighborhoods means less funds available for investment for banks who operate there. They also point out that dealing with this market carries greater risk, including a much higher security risk. Others may also fear, but not state explicitly, the downscale image they do not wish to be associated with. However, the economic reality is that suburban, more affluent markets are saturated, and industries are looking for untapped markets to focus on to create bottom-line growth. These customers could be “grown” into full-fledged customers in many ways.

Many have argued that better banking products tailored to meet the specific needs of the unbanked would benefit both the banking industry as well as the unbanked. For example, a wider acceptance of direct deposit among employers and state-level agencies through bank encouragement and financial incentives would allow consumers entrée into low-cost bank accounts and would eliminate the frustration that those on the financial edge face while waiting 3-7 days for a check to clear through the banking system. Direct deposit is also more economical for employers; it is estimated that paper paychecks cost \$1.71 per check to create and distribute versus the pennies it costs for electronic deposits (“US Warm,” 2002). A greater variety of low-

cost checking accounts, with lower barriers to opening an account, lower minimum balances and lower monthly fees could also be useful. Accounts that merely offer transactional services, without allowing check-writing or other ways to overdraft accounts, especially making use of newer electronic technologies could also help to “grow” the unbanked into future users of fee-based banking products, as well as credit products. Forms of low-risk credit, such as secured credit cards and low-risk short-term credit options to rival payday loans could also be useful. Scott’s (1988) survey resulted in ideas from the unbanked themselves. Scott’s respondents offered these suggestions: that financial management skills be taught at schools or banks; longer banking hours, especially for single working parents; and caps on monthly penalty charges, such as overdrafts.

In recent years, a number of new initiatives have been introduced to capture the unbanked market. A highly effective program in South Africa begun in 1994, just after the end of apartheid, found a way to deal with large populations of uneducated and poor consumers. It is certainly the case, however, that the backing of the South African government helped to spread the risk of catering to this higher-risk population, especially insofar as lending is concerned. South Africa’s Standard Bank, or AutoBank E, allows consumers to open accounts with a very small deposit, and issues them an ATM card with an embedded microchip. The cards are read by ATM machines that detect the customer’s fingerprint on the chip. No checkbooks or paper are involved, and technology serves to minimize bank costs. These accounts have “savings purses” that are available through the ATM machine, where savings can automatically be transferred and accumulated. Even literacy requirements of customers are minimal, in that ATM operations and button-pressing sequences can be “memorized.” (“Finance and Economics,” 2000).

In 1998, Directo, Inc. of Atlanta began offering “multifunctional bank cards” that function like ATM cards, for use in its “checkless checking accounts.” Using direct deposit for the workers’ paychecks, cards can then be used at various ATM terminals (Newkirk, 1999).

Western Union has secured card (prepaid card) products, where the risk to the issuer is small. Unfortunately, some of these cards have high start-up costs (activation fees), high annual fees for use, monthly maintenance fees and fees for use in PIN-based transactions. Western Union’s large reach (30,000 locations) allows for greater convenience, and its alliance with local banks gives it the bank backing for the program (Brittain, Mathis, Sills, Smith and Tumbarello, 2000). Also, a prepaid card created by MasterCard and MemphisFirst Community Bank and First Data Corp (parent to Western Union Financial Services, Inc.) is a special debit card that is fueled by direct deposit payments or cash infusions made at convenient Western Union branches. The card functions as a surrogate for a bank account, using the familiarity of a Western Union branch for those who eschew traditional banks, and by allowing usage as a credit card and at ATMs within its network (Brittain, et al., 2000).

Check101.com has gone one step further, offering both an ATM and online bill paying, which eliminates the need for money orders and uses direct deposit to save on check-cashing (“Check 101.com Announces,” 2001). Finally, FleetBoston Financial Corp. has created Internet kiosks in underbanked neighborhoods, which offer online banking and other technology-based banking services (Bills, 2002).

It is obvious that many of the strategies to help funnel the unbanked into the financial mainstream require greater financial literacy, as well as basic literacy in general. For many of the unbanked, one reason for not venturing into unknown territory as far as new financial services may be that they do not understand the potential benefits of services they do not now

use. Beyond that, there is the further challenge of keeping up with and understanding the benefits of new banking products, especially those that lower costs for both the consumer as well as the bank. It is obviously important to get the unbanked to become familiar with such new products, which they would have no opportunity to do in the “high-touch, low-tech” alternative financial services marketplace. As society, and especially the financial services system, continues to find new ways of using technology for mere day-to-day living, the unbanked stand to lose on all counts. This points to the need for simplified and standardized banking accounts, with fees clearly spelled out, and perhaps choices narrowed down to one or two types of accounts that would fit well with the unbanked population’s needs.

Table 1

*Description of Variables*

Variable	Definition and Categories
Unbanked	1=unbanked and 0=banked
AFS Use	1=used 1 or more alternative financial services in the past three years and 0=used no alternative financial services in the past three years.
Ethnicity	Hispanic or non-Hispanic was reported by the respondent, where Hispanic=1 and non-Hispanic=0.
Age	Age is a categorical variable, where 1=18-29 years old, 2=30-39 years old, 3=40-49 years old, 4=50-64 years old, and 5=65 and older. In the logistic regressions, 18-29 years old is the omitted category.
Educational Level	Education level is a categorical variable, where 1=less than 6 <sup>th</sup> grade or no formal schooling, 2=6 <sup>th</sup> to 11 <sup>th</sup> grade, no GED, or attended trade school or apprentice program (if no GED or 12 <sup>th</sup> grade education), 3=12 <sup>th</sup> grade, or passed GED, whether or not attended trade school or apprentice program, and 4=more than 12 <sup>th</sup> grade. In the logistic regressions, less than 6 <sup>th</sup> grade or no formal schooling is the omitted category.
Gender	1=female and 0=male.
Household Income	1=more than \$30,000 per year and 0=less than or equal to \$30,000 per year.
Household Size	This describes the number of children under 18 in the household (i.e., dependents), where 0=0 children, 1=1 child, 2=2 children, and 3=more than two children. In the logistic regressions, 0 children is the omitted category.
English Literacy	1=respondent chose to do the interview in Spanish and 0=respondent chose to do the interview in English.
Location	1=New York City and 0=Los Angeles.

Table 2: Pearson Correlation Coefficients for all Variables<sup>a</sup>

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20
1. Unbanked	1																			
2. AFS Use	-.21 ***	1																		
3. Hispanic	.27 ***	-.08 ***	1																	
4. Gender	.07 **	-.07 **	-.00	1																
5. English Literacy	.27 ***	-.07 **	.58 ***	.02	1															
6. Location	.23 ***	-.09 ***	-.02	.03	-.09 ***	1														
7. HHIncome	-.39 ***	.22 ***	-.09 ***	-.15 ***	-.20 ***	-.15 ***	1													
8. Age 18-29	.12 ***	-.01	.16 ***	.01	.05 *	-.03	.00	1												
9. Age 30-39	.01 ***	-.01	.09 ***	-.02	.06 *	.02	.02	-.35 ***	1											
10. Age 40-49	-.09 ***	.03 **	-.06 **	-.05 *	-.01 **	-.06 **	.13 ***	-.29 ***	-.32 ***	1										
11. Age 50-64	-.02 ***	.03	-.11 ***	.01	-.04 *	.05 *	-.03 ***	-.23 ***	-.26 ***	-.21 ***	1									
12. Age 65+	-.03 **	-.07 **	-.13 ***	.03	-.10 ***	.02	-.14 ***	-.19 ***	-.20 ***	-.17 ***	-.14 ***	1								
13. Education < 6 <sup>th</sup> grade	.15 ***	-.05 *	.16 ***	.03	.21 ***	-.01	-.15 ***	-.06 ***	-.03 ***	-.01 ***	.01 ***	.15 ***	1							
14. Education 6 <sup>th</sup> -11 <sup>th</sup> grade	.26 ***	-.08 ***	.26 ***	.02	.30 ***	.04	-.25	.01	.01	-.04	.03	.03	-.14 ***	1						
15. Education 12 <sup>th</sup> grade/GED	.01 ***	-.09 ***	-.05 *	.04	-.15 ***	.09 ***	-.04	.04	.03	-.03	-.01	-.03	-.17 ***	-.47 ***	1					
16. Education >12 <sup>th</sup> grade	-.35 ***	.21 ***	-.28 ***	-.08 ***	-.24 ***	-.15 ***	.37 ***	-.02 ***	-.01 ***	.09 ***	-.03 **	-.06 **	-.14 ***	-.41 ***	-.49 ***	1				
17. 0 children in HH	-.13 ***	.02 ***	-.26 ***	-.16 ***	-.21 ***	.05 *	.05 *	-.12 ***	-.11 ***	-.03 ***	.15 ***	.20 ***	-.04 ***	-.11 ***	-.02 ***	.14 ***	1			
18. 1 child in HH	.01 ***	-.01	.06 **	.07 **	-.01	-.03	.02	.05 *	-.03	.05 *	-.03	-.07 **	.00	-.01	.04	-.03	-.53 ***	1		
19. 2 children in HH	.04 ***	-.03	.13 ***	.07 **	.12 ***	.01	-.04	.04	.11 ***	-.00	-.08 ***	-.12 ***	-.03 **	.05 *	-.00	-.04	-.43 ***	-.26 ***	1	
20. >2 children in HH	.13 ***	.02	.16 ***	.08 ***	.19 ***	-.05 *	-.05 *	.07 ***	.09 ***	-.03	-.09 ***	-.08 ***	.09 ***	.11 ***	-.02	-.12	-.34 ***	-.21 ***	-.17 ***	1

<sup>a</sup> n=2,006.

\*p<.05. \*\*p<.01. \*\*\*p<.001.

Table 3

*Means on all Variables of Hispanics and Non-Hispanics by Banked and Unbanked*

Variable Name	Total Sample N=2,006			Hispanic Subsample N=953			Non-Hispanic Subsample N=1,053		
	Banked Mean N=1,096	Unbanked Mean N=910	t-value	Banked Mean N=386	Unbanked Mean N=567	t-value	Banked Mean N=710	Unbanked Mean N=343	t-value
Female	.512	.577	2.915**	.479	.582	3.137**	.530	.569	1.187
Spanish-speaking	.134	.363	12.414***	.381	.580	6.157***	0	.003	1.439
New York City	.397	.623	10.347***	.363	.575	6.573***	.415	.703	9.061***
HH Higher Income	.564	.181	18.984***	.510	.148	13.059***	.593	.236	11.519***
Age 18-29	.196	.297	5.269***	.290	.328	1.237	.145	.245	3.999***
Age 30-39	.273	.280	.374	.316	.319	.1	.249	.216	1.196
Age 40-49	.245	.170	4.117***	.207	.168	1.556	.266	.175	3.280**
Age 50-64	.153	.136	1.077	.111	.102	.447	.176	.192	.648
Age 65+	.107	.089	1.327	.052	.060	.529	.137	.137	0
Education<6th grade	.018	.080	6.641***	.044	.108	3.531***	.004	.035	3.974***
Education 6th-11th grade	.172	.410	12.272***	.275	.492	6.873***	.115	.274	6.589***
Education 12th grade/GED	.359	.369	.447	.391	.305	2.762**	.342	.475	4.184***
Education>12th grade	.444	.123	16.698***	.285	.085	8.455***	.531	.187	11.223***
0 children in HH	.526	.395	5.905***	.365	.309	1.825	.613	.536	2.360*
1 child in HH	.236	.246	.510	.277	.261	.557	.214	.222	.283
2 children in HH	.159	.191	1.910	.233	.220	.458	.118	.143	1.122
>2 children in HH	.079	.165	5.952***	.124	.206	3.300**	.055	.096	2.492*

\*p&lt;.05. \*\*p&lt;.01. \*\*\*p&lt;.001.

Table 4

*Means on all Variables of Hispanics and Non-Hispanics by AFS Use*

Variable Name	Total Sample			Hispanic Subsample			Non-Hispanic Subsample		
	N=2,006			N=953			N=1,053		
	AFS Use	Non-AFS	t-value	AFS Use	Non-AFS	t-value	AFS Use	Non-AFS	t-value
	Mean	Use		Mean	Use		Mean	Use	
	N=526	Mean		N=215	Mean		N=311	Mean	
		N=1,480			N=738			N=742	
Female	.492	.559	2.629**	.507	.550	1.118	.482	.567	2.534*
Spanish-speaking	.196	.253	2.636**	.474	.507	.837	.003	0	1.546
New York City	.416	.529	4.460***	.400	.515	2.377**	.428	.543	3.435**
HH Higher Income	.565	.328	9.760***	.423	.257	4.742***	.662	.399	8.037***
Age 18-29	.245	.241	.224	.353	.301	1.466	.170	.181	.4
Age 30-39	.266	.280	.6	.284	.328	1.225	.254	.232	.768
Age 40-49	.232	.204	1.345	.181	.184	.1	.267	.224	1.503
Age 50-64	.163	.139	1.356	.130	.099	1.311	.186	.179	.283
Age 65+	.063	.111	3.226**	.019	.068	2.751**	.093	.155	2.666**
Education<6th grade	.030	.052	2.025*	.070	.085	.735	.003	.019	1.957
Education 6th-11th grade	.213	.303	3.984***	.321	.428	2.828**	.138	.179	1.628
Education 12th grade/GED	.293	.389	3.961***	.340	.340	0	.260	.438	5.472***
Education>12th grade	.458	.242	9.513***	.260	.138	4.278***	.595	.345	7.698***
0 children in HH	.498	.455	1.712	.367	.321	1.269	.588	.588	0
1 child in HH	.219	.249	1.382	.251	.272	.616	.196	.225	1.039
2 children in HH	.158	.179	1.105	.191	.236	1.393	.135	.123	.557
>2 children in HH	.125	.116	.608	.191	.168	.775	.080	.063	1

\*p&lt;.05. \*\*p&lt;.01. \*\*\*p&lt;.001.

Table 5

*Results of Logistic Regressions on the Banked and the Unbanked*

Variable Name	Model One Hispanic Only (coefficients)	Model One Hispanic Only (odds ratio)	Model Two Hispanic and All Other Variables (coefficients)	Model Two Hispanic and All Other Variables (odds ratio)
Hispanic	1.1121***	3.041	.3242*	1.383
Gender			-.0118	.988
English literacy			.5720***	1.772
Location			.9847***	2.677
HH Income			-1.323***	.266
Age 30-39			-.4811**	.618
Age 40-49			-.6413***	.527
Age 50-64			-.7047***	.494
Age 65+			-.9975***	.369
Education 6 <sup>th</sup> -11 <sup>th</sup> grade			-.3992	.671
Education 12 <sup>th</sup> grade/GED			-.9342***	.393
Education > 12 <sup>th</sup> grade			-1.755***	.173
1 child in HH			.1392	1.149
2 children in HH			.0086	1.009
>2 children in HH			.5273**	1.694
Sample Size	2006	2006	2006	2006
Chi-Square for Model	147.95***		656.48***	
Chi-Square for Comparison	-		508.53***	

\*p&lt;.05. \*\*p&lt;.01. \*\*\*p&lt;.001.

Table 6

*Results of Logistic Regressions on AFS Use and Non-Use of AFS*

Variable Name	Model One Hispanic Only (coefficients)	Model One Hispanic Only (odds ratio)	Model Two Hispanic and All Other Variables (coefficients)	Model Two Hispanic and All Other Variables (odds ratio)
Hispanic	-.364***	.695	-.123	.884
Gender			-.108	.898
English literacy			.029	1.029
Location			-.286**	.751
HH Income			.676***	1.965
Age 30-39			-.127	.881
Age 40-49			-.103	.902
Age 50-64			.152	1.165
Age 65+			-.472*	.624
Education 6 <sup>th</sup> -11 <sup>th</sup> grade			.118	1.125
Education 12 <sup>th</sup> grade/GED			.062	1.064
Education > 12 <sup>th</sup> grade			.738*	2.092
1 child in HH			-.165	.848
2 children in HH			-.085	.919
>2 children in HH			.242	1.273
Sample Size	2006	2006	2006	2006
Chi-Square for Model	12.64***		147.55***	
Chi-Square for Comparison	-		134.91***	

\*p&lt;.05. \*\*p&lt;.01. \*\*\*p&lt;.001.

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