

How the Other Half Banks

Author : Daria Roithmayr

Date : October 2, 2015

Mehrsa Baradaran, [How the Other Half Banks](#) (2015).

Once upon a time there were banks that served the poor. Government structured banks for that purpose—government gave banks cheap money and protection against failure partly in exchange for their providing a place to deposit money, earn interest and get credit, along with economic stability, for everyone. Financial innovation, increased competition and deregulation changed all that: the period of dramatic transformation left the poor and working class without services, as banks came under competitive pressure.

Once upon a time, post offices provided banking functions, giving the ordinary customer a brick-and-mortar office to park their cash. Then competition from higher-interest rate banks changed all that; with shrinking demand, postal banking was dismantled in 1967.

[Mehrsa Baradaran](#)'s terrific book, *How the Other Half Banks*, argues that we could and should ask banks to serve the poor and working class once again. In particular, post office banks (with storefronts and websites both) could provide those missing banking services: a place to park cash, earn interest and take out small amount loans.

Baradaran has become the academic face for postal banking: in the wake of her article in the *Harvard Law Review Forum* on postal banking, she has consulted for the U.S. Postal Service Inspector General, has appeared together with Paul Krugman, and has published in the *New York Times*, *The Atlantic*, Bloomberg, NPR, *Slate*, and other major media outlets. Senator Elizabeth Warren has relied on Baradaran's historical expertise in sketching out the case for postal banking as a real policy option.

The book expands on the *Harvard Law Review Forum* essay significantly, but for a cross-over audience, academic and trade, leaning heavily on the trade (necessarily with less nuance and fewer footnotes). The book makes two central arguments. First, despite banking's origins as a public institution, banking no longer offers adequate services to the poor and working class in the wake of deregulation, because banks have come under competitive pressure to chase profits. Second, a public option for banking could restore these services to those who are now unbanked; in particular, postal banking is one potential public option whose time might have come again. Baradaran contributes a great deal by linking these two arguments together, to remind us of banking's public beginnings, and to show us how postal banking cures what ails us.

In the first part of the book, Baradaran narrates the story of how banks first adopted, and then abandoned, the mission to serve all sectors of the public. History shows that government structured banks as it did on the assumption that banks would serve not just the moneyed classes, but people from humbler circumstances as well. At the broadest level, banks were originally envisioned as public institutions through which the government wielded its hand on economic policy to shepherd the national economy towards productivity. At the narrower level, banks were expected to serve all members of the public regardless of economic circumstance. For those reasons, banks were given access to cheap credit, discount windows, federal backing via FDIC insurance, and, more recently, government bailout in time of great crisis. Far from being ordinary market players, banks were stewards of public economic

health, and government was entangled in every part of their operation.

Bank deregulation changed all that, together with the accompanying shift in thinking and policy, and the radical restructuring of the market. Now banks have become free to act more as private corporations with fewer restrictions, in order that banks can pursue profitability. At the same time, banks are still vested with responsibility for (and the ability to affect) the country's economic health. Smartly, Baradaran acknowledges that banks needed to restructure, given the shift in the economy, but she quarrels with the specifics of deregulation (and tends to oversimplify a bit along the way). Still, her aim is not to criticize deregulation per se: her main focus is to demonstrate the dramatic departure from public institution to pseudo-private actor, and that she does well.

Against the historical backdrop, she sketches the problem of the unbanked—the failure of banks to serve the poor and working class. Baradaran first focuses her lens on the alternative services to which the unbanked have now turned: payday lending, title and installment loans, check cashing, and other such services. She rehearses at length the research on the existence and effect of such services on the poor and working class: bankruptcy, sky-high debt and an economic downward spiral.

One of Baradaran's central contributions is to redescribe the problem of the unbanked in terms other than market failure. Given the level of government entanglement with banks, we can't think about banks as following ordinary market rules (think about the Fed setting rates, for example). Accordingly, says Baradaran, the problem of payday lending and other fringe services is not a problem of ordinary market failure involving mundane asymmetries of information, but rather a structural policy problem. In particular, in the wake of innovation and deregulation, institutions that had once served the poor and working class abandoned their public mission to now chase profits, by necessity.

These institutions had little choice, she says. Owing to deregulation, credit unions, savings and loans, and other specialized and small community banks lost their once-protective geographic monopolies and now came under significant competitive pressure to improve profitability. Because community banks found it more costly to provide products and services for the poor and working class (e.g., small-amount loans, interest-based checking), banks abandoned those higher-cost services for lower-income patrons in favor of more profitable products and services.

Baradaran's exploration of this argument is thorough: she investigates failed government efforts to require, subsidize or otherwise entice banks to provide services for the unbanked. For example, she reviews at length the Community Reinvestment Act, a regulatory requirement/subsidy scheme that failed because it required too much of banks and failed to sufficiently subsidize the full cost of providing services for the other half.

In the last part of the book, Baradaran explores potential remedies for the problem of the unbanked, as part of a call to shift economic policy to provide for them. She investigates among other options the revival of community banks, micro-credit, pre-paid cards, and Walmart banking, noting their strengths and weaknesses. One could write a paper on each of these options, and I can't fault her completely for not spending more time on these potential remedies, though I'd have liked to see a more extended discussion, particularly of Walmart banking.

In the most refreshing and innovative contribution in the book, and perhaps the reason that I most adore it, Baradaran outlines at length the most ingenious "public option" solution: postal banking. The idea is not hers originally, but she seizes and expands on the idea brilliantly and at great length. In particular, she advances the case for postal banking by reviewing the country's earlier experience with postal banks, and by linking that experience to the modern problem of missing services for the poor and working class.

As this chapter opens, Benjamin Franklin's postal system comes into view and we learn about the bureaucratic and logistic wonder that is the U.S. post office. Like banking, the reach and scope of the postal system is essential to a growing economy; like banking, the system builds connections of trust between government and citizen.

Baradaran narrates the long history of the country's first postal banks, and the debate over their existence. Baradaran shows how postal banks provided for the needs of the working poor, and how in fact postal banks were adopted for that very reason. In a real moment of *déjà vu*, Baradaran recounts the financial crisis—the Panic of 1907—that paved the way for the country's full embrace of postal banking, as a way of providing for those toward the bottom of the economic ladder.

Baradaran then persuasively argues that postal banking might now be revived to provide both deposit and credit products and services for poor and working class customers. Although postal banks historically provided mostly the opportunity for savings, and less for extension of credit, the book suggests that small-amount loans could be offered via postal banks. For those who deal in cash, a brick-and-mortar postal bank could provide a way to convert cash to digital dollars; for those who prefer Internet banking, the postal bank could provide that too.

Baradaran smartly acknowledges that like Walmart banking, postal banking would face significant political opposition (though she notes that, compared to Walmart, postal banking would have the advantage of generating more trust as a public entity, without Walmart's profit-focused reputation of underpricing and then raising prices). Baradaran recounts not just the success of postal banks in the U.S. (which closed when community banks paying higher interest rates came onto the scene), but also their relative and variable success in other countries like Japan, Germany, the UK, France, and Brazil. One can appreciate why the policy world has come to Baradaran for her expertise, and this book will constitute a central contribution to the debate.

My one major quibble with this book is that it does not acknowledge the racial dimension of the problems of the unbanked. Though Baradaran discusses the history of the Freedman's Bank and talks about racial discrimination in banking, she does not acknowledge that payday lending and check cashing establishments are four times more likely to locate in minority neighborhoods, even controlling for income, and that a disproportionate share of borrowers are people of color. The structural problem of the unbanked involves the country's racial history more than she acknowledges.

Even so, I will recommend this book to all who are interested in structural racism. Without explicitly recognizing it, Baradaran demonstrates how the the post-deregulation restructuring of banking has disproportionately impacted communities of color, and how postal banking and other public options might bring them back into the fold once more. Baradaran's revival of postal banking, and her description of the disappearance of services in the wake of deregulation, is fresh and engaging, and I highly recommend both the law review forum essay and book for all who are interested in the structure of inequality.

Cite as: Daria Roithmayr, *How the Other Half Banks*, JOTWELL (October 2, 2015) (reviewing Mehrsa Baradaran, **How the Other Half Banks** (2015)), <https://juris.jotwell.com/how-the-other-half-banks/>.