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Do We Really Need States to Be Bankers?

Populists are once again advocating the creation of state-owned banks to overcome private-sector lending market failures. But market innovations hold a lot of promise for accomplishing the same goal.

In 1919, the state of North Dakota established its own bank as a public institution. It's the only one of its kind in the nation, having operated successfully for a full century through the Great Depression and a dozen recessions. Nine other states tried to follow suit in the following decades, only to fail and close their banks' doors. Founded to provide capital in a farm-centric economy that was underserved by large regional financial institutions that charged double-digit interest rates for ag loans, the Bank of North Dakota has served as an inspiration and touchstone to political populists, anti-bank politicians and easy-money advocates.

Over the past decade lawmakers in more than half the states have rekindled legislation in support of public-owned banks, according to the Public Banking Institute, an advocacy organization. The arguments in favor of these bills are similar: The private-sector banking industry underserves low-income communities, minorities and women; banks only lend to people who don't need the money; bank profits are excessive, so states need to establish a competitive yardstick; public banks can promote economic development opportunities that the private sector ignores; and state banks could make money on their investments and deposits — a win-win for taxpayers. Never mind that today money is cheap and the banking system is flooded with excess reserves.

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December 7, 2021 • Girard Miller