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Federal Home Loan Bank Lending to Community Banks: Are Targeted Subsidies Desirable?

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Abstract

The Gramm-Leach-Bliley Act of 1999 amended the lending authority of the Federal Home Loan Banks to include advances secured by small enterprise loans of community financial institutions. Three reasons for the extension of this selective credit subsidy to community banks and thrifts are examined, including the possible need to: subsidize community depository institutions, stabilize the Federal Home Loan Banks, and address a market failure in rural markets for small enterprise loans. We empirically investigate whether funding constraints impact the small-business lending decision by rural community banks. We estimate static and dynamic models of small-business lending by community banks. The data

reject the hypothesis that access to increased funds will increase the amount of small-business loans made by community banks.

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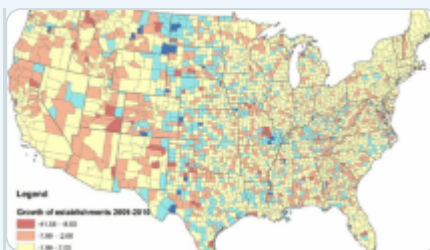
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