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## About the Researchers

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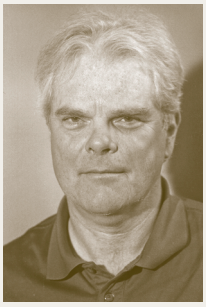

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# Emerging Markets and Financial Services in the Latino Community: Problems and Strategies

## Introduction

The economic potential of the Latino market offers a significant source of new business for financial institutions. Latinos are the fastest growing consumer market in the United States, with a purchasing power of $700 billion that is expected to grow to $1 trillion by 2010.[1] They are considered an 'under-banked' community because they typically use fewer banking services than most Americans.[2] Many financial institutions are seeking to initiate banking relationships with Latino immigrants that eventually lead to full-service customer accounts.[3] US government policies also encourage outreach activities to the Latino market.

Questions facing financial institutions seeking to develop business relationships in the emerging Latino market are: What services are needed? Are first-generation Latinos (born outside the United States) a different market tier from second- or third-generation Latinos? At what stage of contact with US society do Latinos graduate from savings accounts to a broader range of financial products such as credit cards, electronic deposit, mortgage loans, bonds, or stocks—or is that something that happens in the second and subsequent generations?

The purpose of this paper is to study the barriers to Latino use of financial services, generational differences, and market strategies and regulatory policies intended to help overcome those barriers. All tables in this report are based on the 1,512 Latino respondents to the Chicago Area Latino Survey.[4] Findings are estimates for the Latino adult population of the Chicago metro area.

## Latino Generations in the United States

The definition of Latino generations used here follows that used by the Pew Hispanic Center.[5] Table 1 (next page) shows that 41 percent of the Chicago-area Latino population are first-generation immigrants (born outside the United States; they may be naturalized US citizens, legal immigrants, or undocumented immigrants). Among the first generation about half have been in the United States a short period of time (0–11 years) and about half have been in the United States longer.

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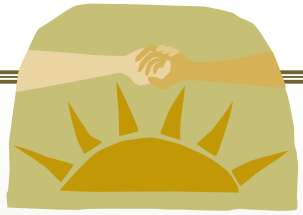

## Metropolitan Chicago Initiative

The Metropolitan Chicago Initiative (MCI) conducts applied research and policy analysis and promotes community capacity-building in the metropolitan Chicago area. Community projects focus on Berwyn-Cicero, where the MCI profiles the status of Latino families and neighborhoods and identifies ways to improve their health, education, and well-being. Regional projects focus on measuring the minority education achievement gap, monitoring education public policy developments, and conducting analysis of Census data for Chicago-area neighborhoods and municipalities. Current projects are funded by the Arthur Foundation, the Joyce Foundation, and the Chicago Community Trust.

For more information visit www.nd.edu/~latino/mci.htm.

## Latino Generations in the United States *continued*

The Pew Center reports that for a wide range of attitude measures the significant differences are between first- and second-generation Latinos, with only slight differences between second and higher generations.[6] The Chicago Area Latino Survey data on financial services show this pattern as well. There are few substantive differences between second- vs. higher-generation Latinos, so these groups are combined for the analysis. Table 1 shows that 50 percent are second generation (born in the United States with at least one foreign-born parent) or higher generation (born in the United States with both parents also born in the United States).

**Table 1: Latino Generations**

| | |
|---|---|
| First Generation (born outside US) | |
| In US 0–11 years | 19% |
| In US 12+ years | 22% |
| Second/Higher Generation (born in US/ parents born in US) | 50% |
| Missing data | 9% |
| | 100% |

## Generation and Use of Financial Services

The data show that in the Latino community graduation from bank accounts to a broader range of financial products generally takes place *within* the first generation.

Table 2 shows the percentage of Latino households that own their primary residence, motor vehicles, and other real estate. Among first-generation Latinos who have been in the United States for a short period of time the rate of home ownership is 37 percent; 3 percent say they own other real estate; 60 percent own a motor vehicle; and 23 percent own two or more motor vehicles.

The rate of home ownership among recent Latino arrivals, 37 percent, is below the Census report of 50 percent home ownership among all Latinos and well below the 67 percent rate of home ownership among all US-born

[1] Elisabeth Malkin, "Spanish Bank Courts Hispanic Customers in United States," *New York Times,* September 22, 2004.

[2] Federal Reserve Board, "The Unbanked—Who Are They?" *Capital Connections* 3 (2, spring 2001); Ana Aizcorbe, Arthur Kennickell, and Kevin Moore, "Recent Changes in US Family Finances: Evidence from the 1998 and 2001 Survey of Consumer Finances," *Federal Reserve Bulletin* 89 (January 2003).

[3] Robin Newberger, Anna Paulson, and Shirley Chiu, *Financial Access for Immigrants: Highlights from the National Conference* (Chicago: Chicago Fed Letter, July 2004).

[4] The 2003 Chicago Area Survey was a randomized sample of 1,512 Latino, 411 non-Latino White, and 403 non-Latino Black households in metropolitan Chicago (Cook, DuPage, Kane, Lake, McHenry, and Will counties). The lines of inquiry and questionnaire were designed by a group of scholars working with the Institute for Latino Studies at the University of Notre Dame. Field work was conducted by NuStats Corporation of Austin, Texas. Approximately 21,750 households were eligible for interviewing. A total of 2,326 interviews were completed among Latinos, Whites, and Blacks in the Chicago region. Respondents were 18 years and older; interviews were conducted in both English and Spanish. For more detailed information about the survey visit the website: http://www.nd.edu/~latino/CAS. Survey data in this report are from the 1,512 surveys completed among Latino respondents.

[5] Robert Suro and Jeffrey S. Passel, *The Rise of the Second Generation: Changing Patterns in Hispanic Population Growth* (Washington DC: Pew Hispanic Center, October, 2003), 2.

[6] The Pew Hispanic Center, *Survey Brief: Generational Differences* (March 2004), 1.

[7] Rob Paral and Michael Norkewicz, *The Metro Chicago Immigration Fact Book* (Roosevelt University Institute for Metropolitan Affairs, 2003), Appendix 9.

| Table 2: Assets Owned by Chicago-Area Latinos | Primary Residence | Other Real Estate | Vehicle | 2+ Vehicles |
|---|---|---|---|---|
| First Generation | | | | |
| In US 0–11 years | 37% | 3% | 60% | 23% |
| In US 12+ years | 60% | 4% | 65% | 37% |
| Second/Higher Generation | 58% | 14% | 61% | 45% |
| Total | 53% | 9% | 63% | 38% |

| Table 3: Use of Financial Services | First Generation | | Second/ Higher Generation | Total |
|---|---|---|---|---|
| | In US 0–11 yrs. | In US 12+ yrs. | | |
| Checking Account Payroll or benefits checks are usually cashed/deposited at a bank or S&L. | 37% | 74% | 61% | 60% |
| Electronic Payment Monthly bills are paid by check or electronically. | 27% | 57% | 62% | 52% |
| Credit/Debit Card Some family member living in the household has either credit or debit card(s). | 17% | 43% | 49% | 39% |

natives in the Chicago region.[7] On the other hand, 37 percent home ownership and 60 percent vehicle ownership show that knowing how to accumulate assets is already established among the most recent immigrant Latinos, suggesting that steps to provide additional services targeted to the Latino population would achieve even higher rates of use.

For home ownership and multiple vehicle ownership the big jump is within the first generation. Among first-generation Latinos who have been in the United States 12 or more years the home ownership rate is 60 percent—about the same as for second- or higher-generation Latinos; 37 percent say they own two or more vehicles—well on the way to the 45 percent rate among second- and higher-generation Latinos. The graduation to the ability to pay for and, presumably, use financial products to help purchase these assets is completely within the first generation. The only exception is ownership of real estate other than a primary residence, where the jump in asset ownership occurs between the first and second generations.

The data show that graduation from bank accounts to a wider range of financial products also takes place within the first generation, and the finding applies to other financial services as well.

Table 3 shows Chicago-area Latino household use of a checking account and other financial services. Among first-generation Latinos who have been in the United States a short period of time the percentage who report using these US financial services is quite low: 37 percent have a bank/S&L account for depositing checks; 27 percent pay bills by check or electronically; 17 percent use credit/debit cards for purchases.

Among first-generation Latinos who have been in the United States 12 years or longer the use of financial services is considerably higher and in the same general range as among second- or higher-generation Latinos. Once again, the data show that graduation to the use of financial products takes place *within* the first US generation of Latinos.

## Overcoming Barriers to Access

To build financial relationships in the Latino community institutions need products, procedures, and strategies that overcome barriers to Latino access.

The three wavy lines shown throughout this publication are a symbol from ancient times representing the human intellect in action. From *The Book of Signs,* collected, drawn, and explained by Rudolf Koch (London: The First Edition Club, 1930, page 8).

Studies of immigrant communities find that among first-generation Latinos immigration status is strongly related to the type and number of relationships with financial institutions.[8] Consistent with this finding, table 4 shows that among first-generation Latinos those who are naturalized US citizens are nearly twice as likely as those who are not to use checking accounts, electronic payments, and credit/debit cards.[9]

At the core of financial access for noncitizens is the ability to document one's identity, income, and creditworthiness in a way that is acceptable to the rules and procedures of the US banking system.

Table 5 shows that one of the most important documents a first-generation noncitizen can obtain in order to have access to financial services is a US driver's license. Among first-generation noncitizens with a driver's license the percentage who use financial services is about the same as among naturalized citizens or second- and higher-generation Latinos. Having a Social Security Number is also related to use of financial services among first-generation noncitizens, but the percentages are not as high as among those who have a US driver's license.

To overcome barriers of Latino access to financial services, particularly among the more recently arrived first generation, banking institutions are exploring new procedures for documenting identity and income, new products that are of high interest to this market, and new services to increase awareness and use of those products.

**Table 4: Citizenship and Financial Services, First Generation**

| | Naturalized US Citizen | Non-US Citizen |
|---|---|---|
| Checking Account<br>Payroll or benefits checks are usually cashed/deposited at a bank or S&L. | 85% | 49% |
| Electronic Payment<br>Monthly bills are paid by check or electronically. | 68% | 33% |
| Credit/Debit Card<br>Some family member living in the household has either credit or debit card(s). | 44% | 25% |

**Table 5: Documentation and Financial Services, First Generation, Noncitizens**

| | US Driver's License | | Social Security # | |
|---|---|---|---|---|
| | Yes | No | Yes | No |
| Checking Account<br>Payroll or benefits checks are usually cashed/deposited at a bank or S&L. | 73% | 41% | 55% | 30% |
| Electronic Payment<br>Monthly bills are paid by check or electronically. | 57% | 24% | 43% | 20% |
| Credit/Debit Card<br>Some family member living in the household has either credit or debit card(s). | 41% | 25% | 30% | 24% |

## New Procedures: Matrícula and ITINs

To help navigate banking rules and expand the delivery of financial services to Latinos who do not have a US driver's license or a Social Security Number, US bank regulators and oversight agencies are increasingly allowing the use of 'nontraditional' documents such as the Matrícula Consular issued by the Mexican government to Mexican

[8] Roberto Suro, Sergio Bendixen, B. Lowell, and D. Benavides, *Billions in Motion: Latino Immigrants, Remittances and Banking* (Pew Hispanic Center and Multilateral Investment Fund, 2002, based on a study of Miami and Los Angeles), 14.

[9] Sherrie Rhine, Maude Toussaint-Comeau, Jeanne M. Hogarth, and William H. Greene, *The Role of Alternative Financial Service Providers in Serving LMI Neighborhoods* (Chicago: Federal Reserve Bank of Chicago). Rhine et al. report that immigrants from Mexico who are US citizens are more likely to have a savings or a checking account than noncitizens. See also Newberger, Paulson, and Chiu, *Financial Access for Immigrants,* op. cit. n. 3.

[10] Suro et al., *Billions in Motion,* op. cit. n. 8, 15.

citizens living abroad or Individual Tax Identification Numbers (ITIN) issued by the US Internal Revenue Service to people who are not eligible for a Social Security number (because, for instance, of undocumented immigration status) but who need to report income for tax purposes. Under Section 326 of the USA Patriot Act foreign-government issued identification and the ITIN are acceptable forms of identification.

It is not illegal for undocumented immigrants to buy property in the United States, nor is it illegal for banks to provide mortgages for such transactions. The growing acceptance of the Matrícula Consular to establish identity for those who cannot obtain a driver's license has reduced the barriers to obtaining financial services.[10] Over the last few years an increasing number of traditional mortgage lenders have begun to document income history with ITIN records of those who do not have a Social Security number, which enables lenders to accept and process an increasing number of mortgage applications in the emerging Latino market. The acceptance of these documentation innovations by regulatory and oversight agencies is a green light to proceed with their use.[11]

### The Matrícula Consular

Since the 1870s Mexican consulates have issued an identity card, known as a Matrícula Consular or Consular Registration, for Mexican citizens living abroad to help them deal with American employers and police and to facilitate shipping belongings home or relatives back for burial. To obtain it an individual needs to present a Mexican birth certificate, another official identity document such as a Mexican voter's registration card or driver's license, and something that attests to his or her address in the United States such as a utility bill. The card bears the individual's photograph and his or her US address. After September 11, 2001, this photo ID was enhanced with 13 security features and is now called the High Security Consular Registration. It has become a prerequisite for entering many office buildings and hospitals, for buying train tickets, for wiring money, and as an alternative form of identification in states that began considering barring undocumented immigrants from obtaining driver's licenses. Many bankers, merchants, and politicians have also embraced the card. Today more than 100 cities (including Chicago), 900 police departments, 100 financial institutions, and 13 states accept it.

## New Financial Products: Free Checking, Remittances

The banking industry has tended to focus on 'free checking' as the way to develop banking relationships in the unbanked and Latino immigrant communities. But free checking does not seem to be a strong enough lure to pull the unbanked into the mainstream at the rate that banks and consumer advocates would like. The unbanked generally report that they encounter few problems with check cashing and bill paying: About two-thirds cash checks for free at grocery stores or other places of business,[12] and money orders are inexpensive and ubiquitous.[13] Moreover, free checking may not be seen as free: It requires money management and math skills; penalties may be assessed for mismanagement (overdraft fees); and mismanagement could trigger the beginning of a poor credit history—which is worse than no credit history. Under these conditions, signing up for a 'free' checking account might, in some cases, be an irrational act.[14]

The strategy to expand access to financial services to the unbanked through free accounts is difficult from the provider side as well. A bank requires revenues of about $100 per year to pay the cost of providing a free checking account, but studies find that only 17 percent of the unbanked population incur costs of $100 or more per year from cashing checks and purchasing money orders, indicating low market interest and low revenue potential.[15]

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11 Rachel L. Swarns, "Old ID Card Gives New Status to Mexicans in U.S.," *New York Times,* August 25, 2003; Nurith C. Aizenman, "Illegal Immigrants Buy into Homeowning Dream," *Washington Post*, August 18, 2003; Rhasheema A. Sweeting, "Trends: Mortgages for the Undocumented," *Chicago Tribune,* August 16, 2004.

12 Edward S. Prescott and Daniel D. Tatar, "Means of Payment, the Unbanked, and EFT '99," *Federal Reserve Bank of Richmond, Economic Quarterly* 85 (4, fall 1999): 49–70.

13 Under Illinois regulations, currency exchanges can sell money orders for up to a maximum fee of 1 percent of the money order's value plus $.75 per money order. Check-cashing fees are between 1 percent and 2 percent based on the face value of the check.

14 Suro et al., *Billions in Motion,* op. cit. n. 8, 3; Rhine et al., *Alternative Financial Service Providers,* op. cit. n. 9, 63; Constance R. Dunham, "The Role of Banks and Nonbanks in Serving Low- and Moderate-Income Communities," in J. L. Blanton, S. L. Rhine, and A. Williams, eds., *Changing Financial Markets and Community Development: A Federal Reserve System Research Conference (2001)* (Richmond VA: Federal Reserve Bank of Richmond), 46; http://www.chicagofed.org/cedric/changing_financial_markets_session1.cfm; John P. Caskey, "Reaching out to the Unbanked," in Lisa Morris and Michael Sherraden, eds., *Inclusion in Asset Building: Research and Policy* (forthcoming).

15 Dunham, "The Role of Banks and Non-Banks," op. cit. n. 14, 44; http://www.chicagofed.org/cedric/files/cfmacd_dunham.pdf.

| Table 6: Remittances to Country of Origin | Send Monthly or More Often | Send Less Often | Do Not Send |
|---|---|---|---|
| First Generation | | | |
| In US 0–11 years | 30% | 38% | 30% |
| In US 12+ years | 24% | 20% | 52% |
| Second/Higher Generation | 6% | 14% | 75% |
| Total | 15% | 21% | 58% |

| Table 7: Percentage Who Say Someone in the Household Currently Needs Financial Counseling | |
|---|---|
| First Generation | |
| In US 0–11 years | 24% |
| In US 12+ years | 23% |
| Second/Higher Generation | 10% |
| Total | 16% |

To significantly increase the number of banking relationships in the unbanked Latino community there is a need to develop new products that appeal more directly to financial needs in the community. The most successful strategy for building new banking relationships may be to provide services for remittances (money sent from Latinos in the United States to relatives back home). The remittance market is large and expanding: The amount of money sent from the United States to Mexico has increased dramatically from $9.2 billion in 2001 to $13.2 billion in 2003, according to the Bank of Mexico.[16] In 2003 an estimated 40 million remittance transactions, averaging $400 each, carried money from the United States to Mexico.

Financial institutions can offer remittance services at competitive rates. At present about 85 percent of remittances are sent by wire transfer through agencies such as MoneyGram or Western Union, at an average cost of $52. By comparison, the average cost for a $400 transmittance from Chicago by bank or credit union is about $18.[17]

Sending remittances is concentrated among first-generation Latinos but persists in the second and higher generations.[18] As such, the first-generation unbanked Latino market will be well served by attractively priced remittance services, and the use of these services is likely to continue as the threshold is crossed to demand for a wider range of financial products.

Table 6 shows that among first-generation Chicago-area Latinos who have been in the United States a short period of time 68 percent send remittances during the year and 30 percent send remittances at least once a month.[19] Among first-generation Latinos who have been in the United States a longer period of time remittances are somewhat lower—44 percent during the year, 24 percent monthly. Among second- and higher-generation Latinos remittances drop off further but still constitute a substantial market—20 percent during the year, 6 percent monthly. In the Chicago region the remittance market predominantly involves transfers of cash to Mexico. Among first-generation Chicago-area Latinos who have been in the United States a short period of time about 77 percent are from Mexico; among those who have been in the United States 12 years or longer about 88 percent are from Mexico.

Expanding the use of new financial products is likely to require another new financial service: customer education.

**New Services: Financial Education**

A study of the remittance market in Miami and Los Angeles finds that about 75 percent of first-generation Latino immigrants say they lack knowledge of the available options for sending remittances and have done little to explore the market.[20] More generally, table 7 shows that about a quarter of first-generation Latino households in the Chicago area report a need for financial counseling.

The Chicago area is home to many community-based organizations (CBOs) that have developed productive alliances with banks to help them overcome barriers to access. They connect fringe consumers to institutions (increasing their customer base) and provide services such as financial literacy training and home ownership counseling (mitigating potential risks and losses). Evaluation studies show that those who participate in financial education come away with substantially greater knowledge and ability to handle financial services.[21] When they become aware of innovations, remittance senders are willing to entertain new money transfer products and new technologies such as the use of ATMs for international transactions.[22]

## Conclusion: Barriers, Response, Policy Supports

According to the results from several research projects, the principal barriers to Latino use of financial services include:[23]

• **Documentation barriers** that make it difficult to meet the rules of US mortgage banking—lack of identity documents; lack of documentation of income and/or credit history; lack of 'due diligence' documents and other verifications when resources are informally pooled among extended families and other 'non-arm's-length relationships' for home purchases.

• **Product barriers**—high fees; lack of sufficient funds to open an account; minimum balance and other requirements; inconvenient branch locations; ubiquitous access to 'fringe banking' alternatives.

• **Knowledge barriers**—distrust of financial institutions; lack of familiarity with financial products; cultural clashes between tellers and clientele more accustomed to a 'fringe service' environment.

This report finds that these barriers are primarily concentrated among first-generation, recent immigrants and that Latinos generally make the transition from unbanked to banked and graduate from savings/checking accounts to a wider range of financial products within the first generation of US residence. This supports the strategy of increasing banking relationships in the Latino community through 'tiered' product and marketing strategies targeted within the first generation.[24]

One way for banks to demonstrate compliance with the Community Reinvestment Act (CRA) is with programs that seek out the unbanked.[25] The four agencies that regulate banks issued a joint interagency letter dated June 3, 2004, stating that regulated financial institutions that offer international remittance services will receive favorable consideration during a CRA evaluation. In addition, the US Department of the Treasury Electronic Funds Transfer Program provides incentives to financial service organizations to offer accounts to the unbanked so that they can receive government payments electronically (which results in considerable savings to government).[26]

This report and the experience of the authors suggest that successful targeting strategies would include:

• **Documentation innovation**—use of ITINs and the Matrícula Consular to establish identity and income history.

• **Product innovation**—remittances; alternative versions of mainstream as well as non-mainstream and even non-banking products such as car insurance and health care screening.

• **Education services**—partnering with known and trusted local nonprofit service providers.

• **Infrastructure development**—senior-level commitment; hiring of managers to implement outreach programs; point-of-contact sales agents familiar with the language and culture; call-in centers with bilingual/bicultural staff; appropriate collateral and merchandising; automated bilingual systems; making the bank look and feel 'more Latino' in terms of its façade and design.

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16 Malkin, "Spanish Bank Courts Hispanic Customers," op. cit. n. 1.

17 Manuel Orozco, *The Remittance Marketplace: Prices, Policy and Financial Institutions* (Pew Hispanic Center, June 2004), 2, 8, 22.

18 Roberto Suro, *Remittance Senders and Receivers: Tracking the Transnational Channels* (Washington DC: Investment Fund and Pew Hispanic Center, November 2003), 5.

19 Rows add up to less than 100 percent because the percentage with "no answer" is not shown.

20 Suro et al., *Billions in Motion,* op. cit. n. 8, 3, 10.

21 Dory Rand, *Financial Education and Asset Building Programs for Welfare Recipients and Low-Income Workers: The Illinois Experience* (Brookings Institution Center on Urban and Metropolitan Policy, April 2004).

22 Suro et al., *Billions in Motion,* op. cit. n. 8, 3, 10.

23 Rhine et al., *Alternative Financial Service Providers,* op. cit. n. 9; Dunham, "The Role of Banks and Nonbanks," op. cit. n. 14; Suro et al., *Billions in Motion,* op. cit. n. 8, 3; Janis Bowdler, "Homeownership," in National Council of La Raza, *The State of Hispanic America 2004: Latino Perspectives on the American Agenda* (Washington DC, 2004), 43–47.

24 Newberger, Paulson, and Chiu, *Financial Access for Immigrants*, op. cit. n. 3, summarizing comments by Alice Perez.

25 The Community Reinvestment Act of 1977 requires every bank to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institutions. Banks come under periodic review by regulatory agencies and, based on their accomplishments, receive credits toward a compliance score. Banks that do not receive a high enough compliance score are unable to expand their operations. Rhine et al., *Alternative Financial Service Providers,* op. cit. n. 9, 63.

26 Federal Reserve Board, "The Unbanked—Who Are They?" op. cit. n. 2.

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**Francisco Menchaca** has more than twenty years experience in the financial services industry, focusing on capacity building and economic development initiatives and working with the emerging urban market business and consumer communities. He was the founder of a major corporation's Latino Employee Network and served as chairman for the City of Chicago's Latino Business Opportunity Conference for more than eight years. He actively participates in and volunteers with numerous organizations including the Spanish Coalition for Jobs, Inc., the Little Village Chamber of Commerce, the Advisory Board of Trustees at Macneal Hospital, Project LEAD, and the New Alliance Task Force. He has received various recognitions including, in 2004, the US Hispanic Chamber of Commerce's Corporate Small Business Advocate of the Year and the City of Chicago's Advisory Council on Latino Affairs Leadership Award. Menchaca migrated to the United States from Mexico as a child, grew up in the Pilsen/Little Village community, and received his BA from Northwestern University and MBA from the University of Illinois at Chicago.

**Robin Newberger** is a business economist in the Consumer Issues Research Unit of the Federal Reserve Bank of Chicago. She has a BA from Columbia University and a master's in public policy from the John F. Kennedy School of Government at Harvard University. Her areas of interest include the savings behavior of low-income individuals and welfare usage among immigrants. Newberger holds a Chartered Financial Analyst designation.

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