What drives banks' geographic expansion?
The role of locally non-diversifiable risk

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Abstract

Why do some banks react to deregulation by expanding geographically while others do not? This paper examines this question using exogenous variation in locally non-diversifiable risk arising from natural disasters that U.S. banks face in their business regions. Combining this data with data on the staggered branching deregulation in the United States in the 1990s, we find that banks facing relatively high locally non-diversifiable risks expand significantly more into other states after deregulation than banks that do not face such risks. These banks expand relatively more into out-of-state counties where locally non-diversifiable risks are positively correlated with the locally non-diversifiable risks in their home markets. This suggests that they rely on their expertise in local risks when they expand into other regions.