U.S. Department of Housing and Urban Development

Research in Focus

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Mortgage Availability and Homeownership in Minority Communities

Americans attained homeownership in record numbers during the past decade. In 2004, homeownership rates peaked at a record 69 percent, and minority and low-income households actively contributed to the housing boom. Between 1994 and 2004, homeownership among African Americans and Hispanics climbed almost 17 percent to 49.7 percent and 48.1 percent respectively. And even as national rates fall, homeownership among Hispanics continues to increase.

This impressive increase in low-income and minority homeownership was fueled by the rise of subprime mortgage products and increased enforcement of the Community Reinvestment Act (CRA) and fair lending laws. Focus on CRA and fair lending caused lenders to increase access to mortgage lending in previously underserved minority and low-income communities. In addition, increased availability of subprime mortgages further opened opportunities for households previously unable to secure conventional home loans. Subprime mortgages—requiring low or no downpayments in exchange for higher interest rates and less favorable terms—enabled households with limited or bad credit histories to become homeowners.

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Effects of the Community Reinvestment Act on Distressed Communities and Mortgage Lending

The year 1989 marked a turning point in mortgage lending to underserved communities, noted Yan Lee, a 2005 Ph.D. recipient from the University of California, Los Angeles. Several events—including amendments to the Fair Housing Act, media scrutiny of racial discrimination in home lending, and increased bank merger activity in which the Community Reinvestment Act (CRA) was more closely invoked—resulted in increased enforcement of the CRA and fair lending laws.

In her dissertation, *Government Intervention in Mortgage Credit Markets: Increases in Lending to Minority and Low-Income Communities, Reductions in Neighborhood Crime from Homeownership, and Potential Efficiency Gains for Banks from Regulation*, Lee, now an economist with the Federal Deposit Insurance Corporation, shows a direct link between increased enforcement of the CRA in 1989 and increased home purchase lending after 1990 to low-income and minority communities by CRA-targeted banks. Building on her initial analysis, Lee's dissertation also probes CRA's real effects on targeted communities and lenders.

Personal Observations Lead to CRA Focus

As an Asian-American growing up in a predominantly African-American neighborhood in New York City, Lee observed differences in where African Americans lived and their ability to accumulate wealth; however, she did not understand its roots until studying redlining (the conscious denial of financial services to people in particular areas or neighborhoods) and early mortgage lending history in an undergraduate class. Subsequent employment as a compliance examiner for the Federal Reserve Bank of New York increased her understanding of

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As credit availability increased for disadvantaged households, the benefits of homeownership were touted as reasons to further increase low-income and minority homeownership. Wealth building, safer and more stable home environments for children, higher educational attainment by children living in owner-occupied housing, and increased community stability as a result of more active neighborhood involvement by homeowners were some of the benefits highlighted. But as more disadvantaged families bought homes, concerns grew over whether low-income and minority households and their communities gain when families are faced with burdensome housing costs. *The State of the Nation's Housing 2007* notes that the number of households (owners and renters) severely burdened by housing costs is escalating. Among homeowners, 41 percent of low-income households paid more than 50 percent of their income toward housing costs in 2005, an increase of almost 13 percent since 2001.

The tide has turned in the real estate market. Many minority and low-income households, some of which have only recently become homeowners, now face foreclosure. This has left many of those who live and work in disadvantaged communities asking how minority and low-income communities will be affected. In order to answer this question, researchers, legislators, and policymakers must understand how changes in the mortgage market have transformed the way mortgage lenders operate in inner-city neighborhoods. It is also important to examine the role homeownership plays in the lives of low-income and minority families and the communities in which they live. Several Office of University Partnerships Doctoral Dissertation Research Grant (DDRG) recipients shed some light on these questions.

- In *Government Intervention in Mortgage Credit Markets: Increases in Lending to Minority and Low-Income Communities, Reductions in Neighborhood Crime from Homeownership, and Potential Efficiency Gains for Banks from Regulation,* Yan Lee, Ph.D. recipient from the University of California, Los Angeles, examines whether the CRA has been effective in increasing mortgage credit to minority and low-income neighborhoods and whether these increases have had *real* effects in improving communities, specifically examining the correlation of crime to increased home lending.

- In *Advantage or Disadvantage? The Changing Institutional Landscape of Central City Mortgage Markets,* Philip S. Ashton, Ph.D. recipient from Rutgers University, examines the effects of the U.S. retail finance crisis of the 1980s and 1990s and the extent to which key lenders have increased access to credit and credit alternatives within underserved markets.

- In *A Study of the Impact of Homeownership on Opportunity for Low- and Moderate-Income Households,* Shannon Van Zandt, Ph.D. recipient from the University of North Carolina at Chapel Hill, examines whether homeownership does, in fact, increase wealth and stability in inner-city neighborhoods. She tests the theory that the promotion of homeownership is an effective tool for strengthening and revitalizing distressed areas.

These dissertations offer insight on how increased access to mortgage lending affects families living in minority and low-income neighborhoods. Such research lays the groundwork for further investigation of both the benefits of increased homeownership and the cost of widespread foreclosures on these areas.

Is "The American Dream" for Everyone?

Shannon Van Zandt, Ph.D.

The list of benefits that accompany homeownership is almost as long as any homeowner's list of house projects. Owning a home has been shown to lead to wealth accumulation. By building home equity, homeowners gain access to financial resources that can be used to start a small business, pay for college, or finance other self-improvement activities. Because homeowners tend to relocate less, homeownership leads to increased community stability with owners becoming more involved in the politics and civic life of their community. Homeownership is also believed to have a positive effect on children. Studies have shown that, compared with similar children of renters, children of homeowners are 5 percent more likely to be in school after age 17. Children of homeowners have also been shown to perform better on cognitive tests and to exhibit lower levels of behavioral problems.

These benefits (along with the fact that homeowners are free to paint their kitchen "Caribbean blue" or any other color they choose) have prompted the expansion of homeownership to segments of the population where homeownership rates are below average, based on the assumption that homeownership may form a foundation from which low-income and minority households can realize other opportunities. But does achieving "The American Dream" increase one's opportunities regardless of socioeconomic status?

This is what University of North Carolina at Chapel Hill doctoral student Shannon Smith Van Zandt hoped to discover while conducting research toward the completion of her dissertation *Achieving the American Dream: The Impact of Homeownership on Opportunity for Low- and Moderate-Income Households.* With the support of an Office of University Partnerships (OUP) Doctoral Dissertation Research Grant (DDRG), Van Zandt was able to complete her research in a timely manner, provide data that will help guide policymakers, and earn her doctoral degree.

Accelerating the Inevitable?

Van Zandt's research focused on three aspects of opportunity that homeownership might be expected to affect: perceived opportunity, social resources, and neighborhood quality. For her research, Van Zandt conducted a longitudinal study that collected data on the same group of adults from before they became homeowners to 2 years after they purchased a home, as well as on a control group of continuing renters.

Van Zandt's results indicate that homeownership is associated with differences among dimensions of opportunity. People who bought homes have better perceptions of opportunity, larger social networks, and live in better neighborhoods, but becoming a homeowner is not the cause of these perceptions. The data show that even before a respondent becomes a homeowner, the levels of the dependent variables were more favorable than for respondents who did not buy homes. Homeownership appears to be more of a benchmark in a person's life course, suggesting that homeownership education and affordable mortgage products may simply accelerate the purchase rather than generate new homeowners. Researchers and policymakers may be overestimating the breadth of homeownership's impacts and the power of homeownership to change an individual's life opportunities. Van Zandt's research suggests a closer look at the social benefits of homeownership is in order.

"Even though this study followed the same group of people for 24 months, it may take longer for the positive effects of homeownership to be realized by the homeowners themselves," said Van Zandt. "I suspect that many of the positive impacts of homeownership will be experienced by the homeowners' children. I also began to wonder if we are pushing homeownership too hard. Many nontraditional mortgage products out there make purchasing a home easier. Individuals who use these methods, but who are not quite financially ready to take on the debt of a new home, may be at risk of losing their home. I also noticed that many of the participants in our study were not always relocating in better neighborhoods than those in which they had been renting. I questioned if their new neighborhoods would provide greater opportunities. It is important for new homebuyers to evaluate the neighborhoods in which they are looking to buy and to be more selective, even if that means they have to prolong buying a home until they can save more money for a downpayment."

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lending discrimination and the regulations put in place to prevent it. These experiences led to her dissertation topic in which she questions whether changes in the CRA resulted in improved mortgage access for low-income households. "It wasn't clear to me whether banks were responding to the CRA, which encourages banks to reinvest dollars into neighborhoods from which they receive deposits, or to fair lending laws, which explicitly prohibit discrimination by race," said Lee.

Yan Lee, Ph.D.

Using Home Mortgage Disclosure Act (HMDA) data for 1980–2000, Lee analyzed changes in the lending patterns of California banks in minority and low- to moderate-income (LMI) communities. She found that mortgage lending by targeted banks (large banks and banks with historically below-average lending in LMI and minority areas) increased after the 1989 enforcement change. Specifically, targeted banks were relatively more likely to lend to minority areas and somewhat more likely to lend in LMI areas in the 1990s. "This leads me to conclude that perhaps fair lending laws have had more of an impact or have worked in conjunction with CRA to increase lending to minority and lower-income neighborhoods," stated Lee.

Profits and Community Gains

By examining the profitability of CRA-targeted banks, Lee attempted to determine whether increased lending in these areas caused banks to lose money, which may have resulted from charging off bad loans, or if banks changed their lending behavior to avoid complying with CRA. Her analysis found no significant losses in bank profitability and limited shifting of bank portfolios away from CRA-regulated loans. She surmises that this may indicate that CRA-targeted banks, while initially shouldering implementation costs, eventually found lending in low-income communities profitable.

To determine if any gains accrued to communities as a result of increased home lending, Lee paired HMDA data with Los Angeles Police Department crime statistics in low-income and minority communities. The analysis shows violent crimes fell in affected communities as home lending increased but had no effect to somewhat-of-an-increasing-effect on property crimes such as larcenies. Thus, increased home lending results in real benefits to targeted communities by decreasing violent crimes such as murder and robberies.

"Real changes in bank lending behavior and neighborhood outcomes suggest that fair lending laws, perhaps working with the CRA, were an effective *jump start* to force banks to extend credit in historically underserved areas," concluded Lee.

Disadvantaged Communities Drive Research

Lee continues to tackle questions directly affecting low-income and minority communities. Currently, she is co-authoring a paper probing the existence of statistical racial discrimination in small business lending. She also recently completed a study that considers gentrification's impact on crime levels in previously low-income neighborhoods.

For more information on her dissertation or current research, contact Yan Y. Lee, Ph.D., Senior Financial Economist, Federal Deposit Insurance Corporation, Washington, D.C., at ylee@FDIC.gov.

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An Emotional Boost

An assistant professor in the Department of Landscape Architecture and Urban Planning at Texas A&M University, Van Zandt is grateful for the OUP grant. "Receiving the grant from OUP not only allowed me to focus on completing and recording my research, it also provided a much-needed emotional boost," explained Van Zandt. "It told me someone was interested in my research and that it was worthwhile. The OUP grant is a highlight on my vitae and one of the accomplishments of which I am most proud."

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The Change in Home-Mortgage Lending for Underserved Markets

When Philip Ashton enrolled in doctoral studies at Rutgers University, he entered a program that had a track record of encouraging students to apply for HUD's Office of University Partnerships (OUP) Doctoral Dissertation Research Grants (DDRGs). His interest in the DDRG program grew by watching students ahead of him apply for and receive funding from OUP. Soon, Ashton was applying for a DDRG, but, disappointingly, his application was denied. But he did not give up. He reapplied the next year, using the reviewers' comments from his rejected application to help sharpen his focus. For him, the second time was the charm, and he received a grant.

Philip Ashton, Ph.D.

Initially, Ashton thought to focus his research on the important work that community development financial institutions (CDFIs) do. (It was while providing technical assistance to small community-based housing organizations that he first became interested in this area, and in how changes in the financial system—innovative new products and programs, greater flexibility in underwriting, and new kinds of institutions—might impact the ability of CDFIs to develop affordable rental housing and low-income homeownership opportunities.) However, as he studied these issues more closely, his interest shifted to the broader question of whether historically underserved markets were becoming more competitive in attracting mortgage capital than they had been in the past. He hypothesized that certain key categories of lenders promoted by the financial transformations of the late 1980s and early 1990s might have some competitive advantages that allowed them to better address the risks of lending in underserved markets. This hypothesis was the springboard for his dissertation, *Advantage or Disadvantage? The Changing Institutional Landscape of Central City Mortgage Markets,* summarized in the next column.

Research Summary

The resolution of the U.S. retail finance crisis in the post-1989 period altered the landscape of central city mortgage markets by spurring the growth of new financial players. While these developments are widely hailed as making mortgage markets more stable and efficient, there is now consensus that these changes have increased opportunities for *historically underserved markets*—low-income and minority households and the neighborhoods where they are concentrated.

In this research, Ashton examined the contemporary institutional landscape of mortgage lending in the United States, arguing that it was the product of a set of rules that arose out of the resolution to the U.S. banking crisis after 1989. These market reforms and the financial restructuring they spurred worked in complex and contradictory ways, but they served to promote the competitive advantages of a handful of key categories of lenders, including the large, geographically diversified financial conglomerates, lenders with community reinvestment agreements, and subprime lenders that are the focus of this research.

Secondly, he examined theoretical perspectives on credit risk, investigating whether the competitive advantages of these lenders are sufficient to overcome the legacy of urban decline that has produced a self-reinforcing profile of financial risk in historically underserved areas.

Third, he elaborated a methodology for assessing the role played by consolidating lenders and their counterparts in altering the geographic and social allocation of mortgage finance to benefit historically underserved markets. He applied this to an analysis of home mortgage lending in Chicago, Philadelphia-Camden, and San Francisco-Oakland from 1992 to 2000, specifically trying to assess and compare the role of key lenders in expanding mortgage market advantages to historically underserved borrowers and areas.

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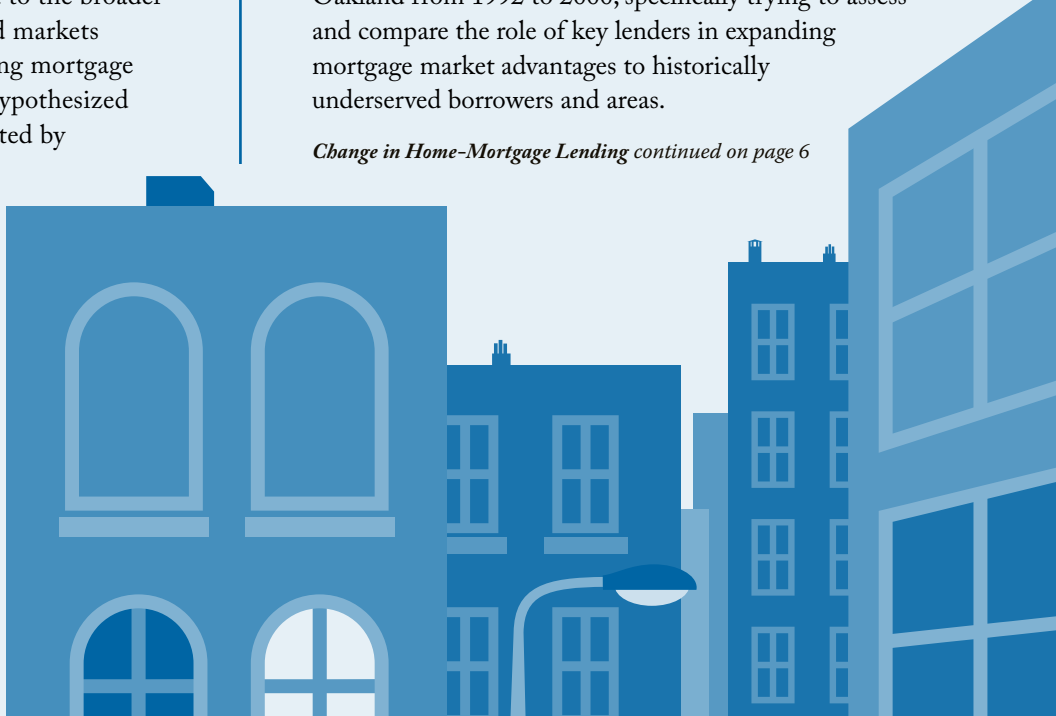

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Method of Analysis

Ashton employed a multivariate analysis of home purchase lending from 1992 to 2000 and found evidence that key lenders are leading the way in expanding opportunities for underserved markets relative to all other lenders. At the same time, he identified the selectiveness of those advantages for different groups of borrowers in different places. For consolidating lenders in particular, the advantages afforded to borrowers in underserved market segments seemed tied to signals from equity and capital markets—that is, they are more pronounced during periods of market expansion but recede or even reverse during periods of financial instability, such as the Asian financial crisis of 1997.

The leadership of key lenders also had a pronounced spatial component to it, since few advantages transferred to borrowers in those tracts with the lowest incomes or the highest minority populations. Indeed, within the most challenging markets, there is compelling evidence of a structural shift toward market dominance by subprime lenders as the decade progressed. He concludes his research by arguing that these competitive patterns increase the isolation of borrowers in those areas in a way that actually reproduces or even deepens their risk profile, posing fundamental challenges to advocates and policymakers working to expand housing and neighborhood opportunities in central cities.

Philip Ashton received a Ph.D. from Rutgers University in 2005. He is currently an assistant professor in the Urban Planning and Policy Program at the University of Illinois at Chicago.

HUD's Office of University Partnerships (OUP) provides grants to institutions of higher education to assist them and their partners with the implementation of a broad range of community development activities, including neighborhood revitalization, housing, and economic development. It also provides grants to doctoral candidates to develop and conduct applied research on policy-relevant housing and urban development issues. This newsletter, *Research in Focus,* highlights the accomplishments of grantees in OUP's Doctoral Dissertation Research Grant and Early Doctoral Student Research Grant programs. It includes a variety of articles on past and current grantee dissertations and research.