HOUSING & PREDATORY LENDING WORKING GROUP ON CLOSING THE RACIAL WEALTH GAP

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1. BACKGROUND:

Housing has been crucial to building wealth in our society. While many people think of wealth as synonymous with income, home equity is often the largest component of the average American family's wealth. In 2000, data collected by the U.S. Census Bureau found home equity to account for 75% of the assets held by the median household in the U.S. Historically, home equity has been critical in the growth of the middle class throughout the U.S. following WWII.

While home equity has been a significant resource to improve conditions for White families in the U.S., families of color have not been able to access the wealth potential of home equity. Several factors account for this problem, a legacy of historical discrimination in lending and access to homeownership, the cost of living in segregated communities and continued discrimination in the housing market. Minority communities are often targeted by sub-prime lenders as well. Recent challenges facing the U.S. housing market, such as exorbitant cost and wide spread foreclosures, amplify these existing conditions, threatening to expand existing wealth disparities in the U.S.

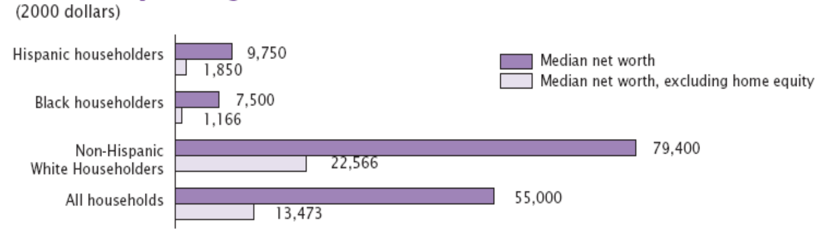
For whites in 2005 the homeownership rate was about 75%, compared to 46%-56% for persons of color.[1] Access to home buying opportunities remains highly segregated in many places, resulting in wide variations not only in ownership rates, but the value of home equity–with smaller relative shares of both for people of color. For the limited number of African American homeowners median home values are 35% lower than White home value. The home equity disparity gap between White and non-White households is compounded by the low homeownership rates of people of color, leading to wide spread asset gaps between African American and White households. For example, in 2000 the median net worth for African Americans was just $7,500, compared to $79,400 for Whites.[2]

The wealth gap disparity did not evolve naturally and is the result of a well-documented history of discriminatory policy, which has durable persistent impacts to asset development for communities of color. The following document reviews some of the historical and contemporary policies driving home equity disparities, reviews new challenges impacting home equity for communities of color and provides several policy recommendations to address the wealth gap in housing.

Home Ownership Rates by Race 2003	
White	75.40%
Black	48.10%
Hispanic	56.30%
Asian/Pacific Islander	54.30%
Native American	54.30%

U.S. Census Bureau, *Annual Statistics, 2003*

Figure 6.
Median Net Worth and Median Net Worth Excluding Home Equity of Households by Race and Hispanic Origin of Householder: 2000
(2000 dollars)



Source: U.S. Census Bureau, Survey of Income and Program Participation, 1996 panel.

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[1] U.S. Census Bureau, *Annual Statistics, 2003, Housing Vacancies and Homeownership,* Table 20. 75.4% Whites, 48.1% African American, 46.7% Latino, 56.3% Asian / Pacific Islander, 54.3% Native American.
[2] "Net Worth and Asset Ownership 1998-2000". Household Economic Studies. U.S. Census Bureau (2003)

2. Historical and Contemporary Factors/Policy Driving the Wealth Gap

At the end of World War II, the Serviceman's Readjustment Act of 1944 (the G.I. Bill) amounted to systematic isolation of African American servicemen from the rights and privileges of white servicemen, such as education and housing subsidy. In the suburb-shaping years (1930-1960), less than one-percent of all African Americans were able to obtain a mortgage. Public disinvestment and redlining in neighborhoods of color, explicitly racially restrictive zoning and covenants, combined with FHA preferences for homogenous suburbs created equity loss for many people of color. Blockbusting and other discriminatory realtor behavior helped devalue White neighborhoods in racial transition. Subsequently, the 'invisible hand' was left to do the rest, distributing capital where it earned the most return for investors (outside of areas with populations of color).

Today discriminatory policy continues but operates in much more subtle ways. Exclusionary zoning stifles affordable homeownership in high value communities. Realtor discrimination has declined but remains persistent and racial steering continues to support segregative housing patterns. Lending discrimination and predatory lending activities deny access to stable housing investments. These discriminatory policies and actions work together to continue to deny homeownership and home equity growth to many families of color.

Unfortunately, rapid changes in the housing market in the past decade threaten to exacerbate existing housing disparities and home equity appreciation for people of color. The nation experienced widespread rapid growth in home values in the past decade, especially in coastal housing markets and major metropolitan areas. The rapid appreciation in housing markets throughout the nation widened the existing affordability crisis facing the African American and Latino population. As housing grew more affordable, unconventional mortgage lending and predatory lending expanded. Teaser mortgages, sub prime loans and other adjustable rate mortgages have placed many homeowners on the edge of an economic precipice, with the slightest change in the market or their financial standing enough to push them into foreclosure.

The recent surge in foreclosures is the result of these activities. Between 2005 and 2006 the number of foreclosures rose by 42%, with industry analysts predicting another two million foreclosures in the following two years.[3] Spatially, foreclosures are accumulating in urban neighborhoods with high rates of subprime lending and threaten to spread when more adjustable rate mortgages (ARM) reset in the following year. Time Magazine recently reported that families with the average subprime loan can expect a $400 increase in monthly payments when ARM's reset, for those in teaser mortgages this increase could be $1,500. [4] If current trends continue a disproportionate share of these foreclosures will occur in urban communities of color. The foreclosure challenge impacts everyone, even those not immediately at risk for foreclosure, bringing additional hardship to all homeowners with lending institutions tightening lending guidelines, interest rates rising and homeowners in neighborhoods with many foreclosures experiencing a decline in their property values due to nearby vacant properties (home values decrease by 1% for every foreclosure within a 1/8 of a mile). [5]

3. Housing Equity: Is it Still Critical to Building Wealth?

As expectations across the broader housing market are lowering, the ability to access wealth through housing is decreasing. Some estimates suggest that given current and expected conditions it may take five years at minimum to break even on initial housing investments made today. How many families in the lower income brackets can sustain negative home equity? Related studies go even further; suggesting renters over the recent five-year period may actually have fared better than home owners, in terms of savings which could have been invested in other forms of wealth, such as enterprise formation and equity markets. The market realities facing all homeowners, but in particular persons of color, are complex. Rather than a clear urban-suburban wealth divide (such as that which boosted post-World War II

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[3] Stansbury, Robin (2007, March 31). Loan Woes Hit Home: Sharp Rise In Foreclosures In State Puts More Houses On A Bloated Market. *The Hartford Courant*

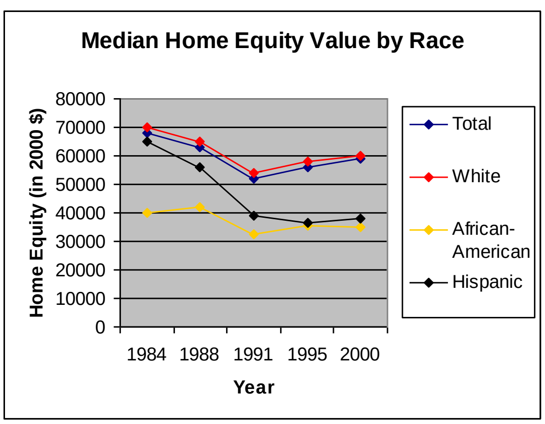
[4] Barbara Kiviat. (2007, August 16). Real Estate's Fault Line. *Time Magazine.*

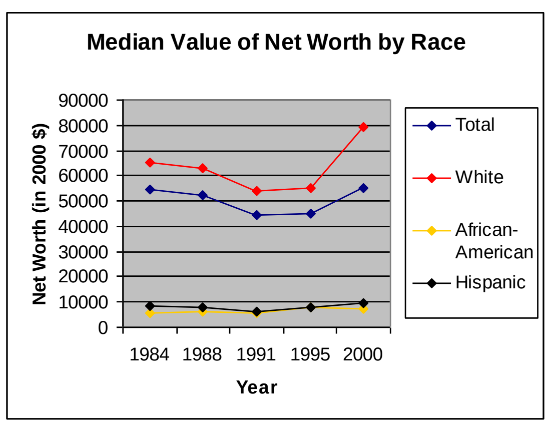
[5] Barbara Kiviat. (2007, August 16). Real Estate's Fault Line. *Time Magazine.*

suburban property values), declining inner suburbs are being flooded with capital by persons of color, while some urban centers are seeing waves of reinvestment or gentrification. The ‘sinking’ value in declining areas and the predatory lending debacle, coupled with the disproportionate share of wealth tied to homeownership, can severely limit the potential of increasing assets through homeownership.

It is apparent that housing equity is now less a factor of total wealth than it has been in recent years. In 2000, median home equity value was still well below its 1984 value, and the proportion of total assets constituted by home equity has decreased for people of all races since peaking in 1984. In 2000, only 31% of whites’ wealth consisted of home equity, for African Americans this figure was 62% and 51% for Latinos. However, during this same time period, white median total net worth increased from $65,000 to $80,000, while both Black and Hispanic total net worth grew by less than $2,000.[6] As home equity has become a less powerful mechanism for building wealth, white wealth increased through large gains in both non home investments and in home equity.

Although home equity is in decline as a proportion of total assets, it still remains a crucial mechanism for growing wealth. The recent dynamics surrounding the housing market points to lessons that should inform initiatives to close the wealth gap through housing initiatives. First, location is still critical in respect to home appreciation, at both the metropolitan and national level. Home ownership initiatives should be targeted ownership to stable, high opportunity neighborhoods that show potential for significant appreciation. Non-geographically targeted programs create significant risk for new homeowners, potentially locking them into poor quality neighborhoods which may experience depreciation in the current unstable housing market. At the national level, attention must be focused on the national housing market; many metropolitan markets (especially those in the nation’s economically struggling rust belt) are experiencing depreciation and in recent years have not seen significant equity growth. Rates of asset accumulation and appreciation traditionally seen in the coastal housing markets cannot be expected for homeowners in many housing markets. Second, home equity should not be the only wealth accumulation strategy, but should be part of a multi-faceted approach to expanding wealth though over investment mechanisms. Finally, non-traditional mortgage products have proven especially sensitive to changes in the housing market, many first time homebuyers in recent years have used teaser mortgages, sub-prime mortgages and ARM’s to access homeownership. These are the owners most at risk to fall into foreclosure, any initiative to target the wealth gap in housing must explore alternative avenues to finance homeownership but be cautious of relying on these particular risky financing strategies.

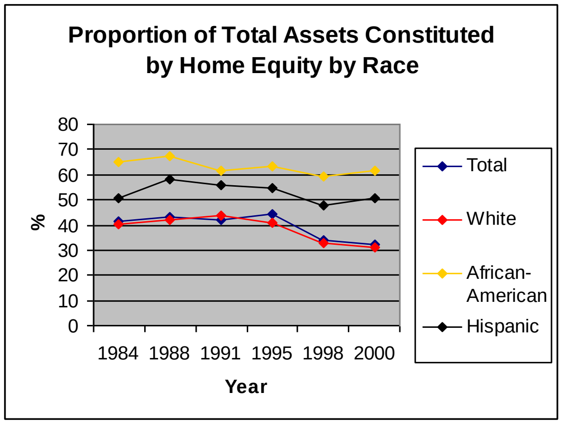




% of Assets in Home Equity				
	Total	White	African-American	Hispanic
1984	41.3	40.4	64.9	50.4
1988	43.1	42.2	67.6	58.2
1991	41.9	43.7	61.8	55.6
1995	44.4	41.1	63.3	54.9

[6] Source: U.S. Census Bureau

1998	**33.7**	**32.6**	**59.2**	**48**
2000	**32.3**	**31**	**61.8**	**50.8**



4. The Importance of Place: Housing as an Access Point to Economic Empowerment

Initiatives to close the housing wealth gap, must view housing as more than a financial investment but also as a mechanism and gateway to other opportunities. Housing location determines what schools children will attend, their safety, their access to employment and the potential for their home to gain appreciation. Housing value is more than just the value of the physical structure but reflects the price paid for access to schools, transportation, amenities, neighbors, perception, the actual attributes of the home, and expectations about today and the foreseeable future. In particular, many studies have pointed to school quality as one of the primary factors influencing home equity appreciation.[7]

Neighborhood quality also plays a significant role in shaping the life opportunities available to individuals. The long term ramifications of these factors can not only influence housing appreciation but influence the likelihood of future wealth development in other areas. For example, the quality of a child's school has a significant impact on the potential for them to meet academic success or failure, school quality influences if the child will become a high school drop out or a future physician, entrepreneur or leader in the area of politics, community or business.

When looking to expand homeownership for people of color, initiatives must target growth in homeownership in high opportunity communities, with good schools, sustainable employment and safe neighborhoods. By targeting more homeownership in high quality communities, we can help lift more than the property values for minority homeowners, but also influence the educational and economic success of future generations. This strategy can produce transformative changes in the economic future of many people of color, to help permanently close the nation's persistent wealth gap.

5. Recommendations

A. Enforcement, regulation, and designation of federal agencies to affirmatively close the gap through Title VIII.

1. **Purge discriminatory behavior under Fair Housing, Fair Lending, and Equal Credit Opportunity Acts.** All forms of discrimination in the housing market, acquisition, retention, growth and equity must be ended. The government had an obligation to affirmatively promote integration related to housing.
2. **Encourage proactive engagement in such areas as market mechanisms and credit scoring**.
3. **Encourage financial engineering that creates products and services that are reasonably designed to assist consumers who have historically been locked out of the credit market**.

[7] Brasington, David M., Which Measures of School Quality Does the Housing Market Value? *Journal of Real Eastate Research*, 1999, 18:3. Jud, Donald G. and Watts, James M., School and Housing Values, *Land Economics*, 1981, 57:3, 459-470. & Haurin, D. R. and D. M. Brasington, The Impact of School Quality on Real House Prices: Interjurisdictional Effects, *Journal of Housing Economics*, 1996, 5, 351–68. Espey, Molly, et al, Does Close Count? School Proximity, School Quality, and Residential Property Values, *Journal of Agricultural and Applied Economics*, 2007.

Such financial engineering should be coupled with efforts to enhance credit data and acquire more competent data.

B. Establish an Effective Sub-Prime Financial Regulatory System.

Prime markets are extraordinarily well managed, but the same degree of regulation and management does not currently extend to the sub-prime market. The kinds of loans that are commonly offered to lower income and minority consumers, in particular African Americans and Latinos, have been done using steering. With the use of steering practices, financially bad products for financially vulnerable consumers begin to unfold. Elements of the proposed financial regulatory system include:

1. **Underwrite consumers for loans at the full index price, and not just the teaser rate.** The 228 loans given to minorities or people of low income underwrite the consumer only at the teaser rate. These loans explode into larger rates, but the consumer is not able to afford this increase.
2. **Verify the consumer's ability to repay loans.** Prevent products deemed inappropriate for people of modest means from being offered to this sector of consumers. Brokers and other financial professionals will be held legally responsible for sharing and upholding this regulation.

C. Promote Access to Opportunity through Housing Location

1. **Increase Access to High Quality Education through Increased Affordable Housing Opportunities.** Establish racially targeted affordable housing initiatives in higher income communities to provide access to good school districts. The increase of accessibility to quality education will in turn positively impact the wealth earning potential and also place people amidst a community where asset generation is effectively exemplified in terms of property values.
    - **Consideration 1:** The LIHTC Program is an indirect Federal subsidy to finance the development of affordable rental housing for low-income households. Unfortunately, these housing units are generally located in economically depressed and racially segregated neighborhoods. The geographic concentration and the lack of access to suburban development and related job opportunities, provides little relief to low-income families trying to improve their financial well-being. States must modify their Qualified Allocation Plans to prioritize more family LIHTC development in communities with high-performing schools.
    - **Consideration 2:** Increase rental and mortgage opportunities to allow for access to high quality education.
2. **Leverage Public Investments to Assure the Implementation of Inclusionary Zoning.** To simultaneously create housing opportunities in neighborhoods of opportunity, standardize capital investment methods by not providing any new capital investment to growing areas unless there is inclusionary zoning. This applies to funds for infrastructure, new school development and transportation.
3. **Establish Affordable Housing Tax Credits Near Transportation Nodes.** Poor people tend to live further from their jobs and good transportation. Provide affordable housing tax credits near transportation nodes to create housing density around the area.
4. **Create Low-Cost Mortgage Opportunities near Job Centers, Quality School Districts, and Transit Nodes.** Generate low-cost mortgage opportunities for low-income people in areas near job centers, high quality education, and transit nodes.