



THE FUTURE OF FAIR HOUSING and FAIR CREDIT

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NOW WHAT? KEY TRENDS FROM THE MORTGAGE CRISIS AND IMPLICATIONS FOR POLICY

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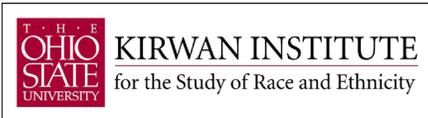
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Now What? Some Key Trends Coming out of the Mortgage Crisis and Implications for Policy Prepared for the Kirwan Institute for the Study of Race and Ethnicity

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From a fair housing and fair lending perspective, the U.S. mortgage crisis has had, and will continue to have, a wide variety of mid-to-long-term effects on housing finance and housing patterns more broadly. This brief memo touches on just a few of the likely impacts.

Homeownership Finance

Even after accounting for the demise of many high-risk subprime lenders, most lenders have tightened underwriting standards. According to the Federal Reserve's Senior Loan Officer Survey, prime lenders began tightening standards in 2007, as the subprime crisis worsened, and this continued through at least the spring of 2009, although the pace of ongoing tightening began to slow some in late 2008. However, even in early 2009, 49 percent of lenders continued to tighten standards, while no lenders reported easing standards. At the same time, FHA market share, which had dropped to around 5-7 percent of home purchase loans in 2005 and 2006 increased to an estimated 25 percent by early 2009. The FHA expansion, combined with the conservatorship of Fannie Mae and Freddie Mac meant that the federal government has become the critical driver of the mortgage market by late 2008. As had been the case earlier, FHA loans currently constitute a disproportionately large share of the market in lower-income and minority neighborhoods.¹ This may be due to differences in real or perceived risks across zip code types (including differences in credit scores and down-payments), to differences in lending practices of lenders or private mortgage insurers across neighborhoods, and/or to other factors. Regardless of the reasons behind these disparities, they are important to recognize. In part because FHA loans are generally more expensive, such disparities could have significant consequences for lower-income and minority communities and households.² More work is needed to understand what lies behind these disparities and their implications for lower-income and minority communities. Substantial attention to this issue by regulators and fair lending advocates is warranted.

Homeownership Rates and Related Segregation

After climbing from the mid 1990s through the early 2000s, the homeownership rate in the U.S. began dropping during the peak of the subprime boom in late 2004 and early 2005, driven by surging foreclosures. By early 2009, the national homeownership was down 1.9 percentage points to 67.3 percent (a decline of 2.8 percent in the homeownership rate), roughly equivalent to the rate in early 2000. While this decline itself is significant, national changes mask steeper declines in many local communities. From late 2005 to early 2009, for example, the homeownership rate had fallen by 10 percent in the Toledo metropolitan area and by 8 percent in the Riverside metro. As homeownership rates fall, there are likely to be implications for racial and economic segregation. Because rental housing in many low-poverty and low-minority communities is scarce, less access to homeownership may bring with it decreased access to such neighborhoods by lower-income and minority households.

Prospects for Rental Housing Markets

As foreclosures surged and credit markets tightened, the demand for rental housing did increase in many places. If the foreclosure crisis had not been followed by the deep economic crisis, however, these increases would have been far more substantial. As it is, the effects have been moderated by weaker net household formation due to higher unemployment and slowing immigration rates.³ Importantly, the overall demand for

¹ My analysis of data from LPS Analytics (not shown here) finds that the share of home purchase loans in high-poverty (>20%) zip codes in the last quarter of 2008 was 39 percent higher than the FHA share in low-poverty (<5%) zip codes.

² Unlike many "conventional" borrowers, FHA borrowers are essentially paying higher effective interest rates through insurance premiums while many conventional borrowers are not necessarily doing so, especially following conservatorship of the GSEs.

³ Peter Passel, *Recent Trends in Immigration: 1980s to 2009*. Presentation at University of California at Davis, May 21-22, 2009, at <http://migration.ucdavis.edu/cf/files/2009-may/passel.pdf>.

multifamily *apartments* has generally not increased, due to increasing sources of competing supply.⁴ Some condominium stock and foreclosed, single-family homes are being converted to rental housing. Despite the lack of substantial tightening in rental markets on an aggregate basis thus far, it is important to understand that rental markets are subject to high levels of affordability mismatch, where many units are provided at high rents but few are affordable to lower-income households. As unemployment increases, there is likely to be a paradox of higher overall vacancy rates as more people double up or live with relatives, while many families' incomes drop faster than any declines in rents. There are also geographic mismatches in the rental market. The foreclosure crisis has led to substantial concentrations of vacant homes in particular neighborhoods.⁵ Some of these homes are available for rent, but they are often clustered in areas that have been hit hard by the foreclosure crisis and, increasingly, by the broader recession. Moreover, for many renters, this new supply of rental units may not be located in places that are well suited for them, given job locations, schooling and child care issues, and other constraints. Meanwhile, in some communities offering superior access to jobs and good schools, conversion of owner-occupied units to rental may occur slowly, especially in places where condominium or homeownership associations resist such changes.

Another problem is that many very low-income households rely on federal housing choice vouchers, which many landlords may not accept, and resistance to vouchers might be expected to be stronger in communities (including condos) where rental housing have not been prevalent in the past. Housing voucher users also tend to end up disproportionately concentrated in poor and minority neighborhoods.⁶

All of these forces mean that, even in periods when market data suggest an aggregate oversupply of apartment units, there are likely to remain significant problems of affordability and geographic mismatches when comparing the supply of rental housing to the needs of the households requiring affordable rental housing. These mismatches are likely to worsen if some problems in multifamily housing finance are not addressed in the near future.

Some Implications for Fair Lending and Fair Housing Policy

The trends outlined here have a number of implications for fair lending and fair housing policy. First, the, FHA's larger share of the home purchase loan market in lower-income communities, suggests the need for strong fair lending and community reinvestment attention to the distribution of FHA versus other forms of loans. As conventional lenders and mortgage insurance firms change their underwriting policies, these policies, and the resulting lending patterns that result, should be examined for potential fair lending problems and impediments to sound community reinvestment. So called "declining market" policies by mortgage insurance firms, for example, should be justified based on hard data that can be examined for disparate impacts that may not be justified by business necessities.

Second, the shift to the rental market suggests the need for stronger fair housing enforcement. The increase in homeownership rates and the geography of housing markets meant that, for a time, minority households gained somewhat better access to a broader array of neighborhoods. With homeownership rates on the decline, minority households may see highly restricted residential choices. Households whose credit histories have been damaged may be particularly hard hit as many landlords use credit histories to screen tenants. Federal and state agencies responsible for enforcing fair housing law will need to play a strong role in the housing market to mitigate these effects. Moreover, states and localities could pursue "source of income protection" ordinances that prohibit landlords from rejecting voucher holders as tenants.

Finally, state and federal policymakers should promote policies that encourage the development of shared-equity housing. Examples include promoting appropriate property tax treatment and adequate financing sources.⁷ Moreover, regional planning organizations should expressly foster the adoption of comprehensive plans that call

⁴ Gleb Nechayev, "Where Have All the Renters Gone?" *About Real Estate* Volume 10, Number 10, Torto Wheaton Research. May 14, 2009.

⁵ Dan Immergluck, *Intrametropolitan Patterns of Foreclosed Homes: ZIP-Code-Level Distributions of Real-Estate-Owned (REO) Properties during the U.S. Mortgage Crisis*, Federal Reserve Bank of Atlanta Community Affairs Discussion Paper 01-09, April 21, 2009, at http://www.frbatlanta.org/filelegacydocs/dp_0109.pdf.

⁶ In 2005, only 25 percent of voucher holders were located in low-poverty (<10% poverty rate) census tracts, compared to 39 percent of all renting households. Kirk McClure, "The Low-Income Housing Tax Credit Program Goes Mainstream and Moves to the Suburbs," *Housing Policy Debate* 17: 419-446.

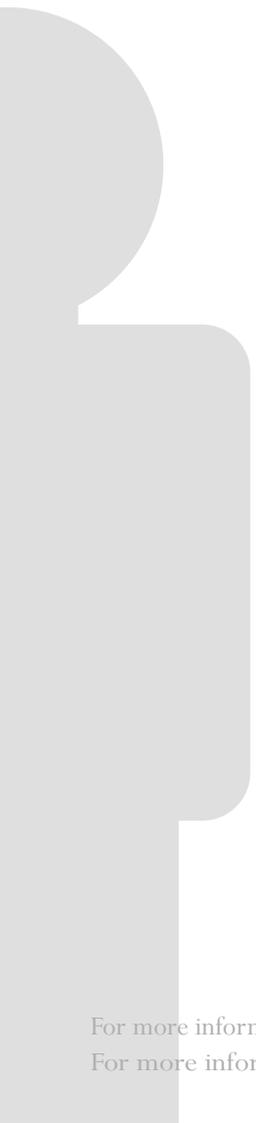
⁷ One important example is to make mortgage financing programs more easily useable for shared-equity ownership. For example the Community Land Trust Network has argued for modifying FHA rules to make the program more useable for CLT home purchase loans. Given the growing importance of FHA, such a policy could be very important. See <http://www.cltnetwork.org/index.php?fuseaction=Blog.dspBlogPost&postID=223>.

for diversifying tenure options as a way for providing for affordable and sustainable affordable housing across a wide variety of local jurisdictions.

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