U.S. Department of Housing and Urban Development

UNEQUAL BURDEN: INCOME & RACIAL DISPARITIES IN SUBPRIME LENDING IN AMERICA

This study presents a preliminary analysis of almost one million mortgages reported nationwide in calendar year 1998 under the Home Mortgage Disclosure Act (HMDA). The data clearly demonstrate the rapid growth of subprime lending during the 1990's and, further, the disproportionate concentration of such lending in the nation's minority and low-income neighborhoods. These findings are significant for the nation's policy-makers, in light of the growing evidence of widespread predatory practices in the subprime market.

AN OVERVIEW

Over the past several years, the nation has seen a veritable explosion in the subprime mortgage lending market, raising serious questions for the nation's policy makers.

In 1993, the subprime share of the overall mortgage market represented $20 billion. In five years, this volume multiplied more than seven times to $150 billion. By providing loans to borrowers who do not meet the credit standards for borrowers in the prime market, subprime lending can and does serve a critical role in the Nation's economy. These borrowers may have blemishes in their credit record, insufficient credit history or non-traditional credit sources. Through the subprime loan market, they can buy a new home, improve their existing home, or refinance their mortgage to increase their cash on hand.

But there are two sides to this story. Since subprime lending often operates outside of the federal regulatory structure, it is a fertile ground for predatory lending activities, such as excessive fees, the imposition of single premium credit life insurance and prepayment penalties. The recent acceleration in predatory lending activity has accompanied the growth in subprime lending over the past decade. And predatory lending can have disastrous consequences for the unknowing borrower. At the very least, equity is stripped from the home. In more egregious cases, homeowners may lose their home altogether.

Prime lenders have made significant efforts and, indeed, significant progress in reaching historically-underserved markets and communities. However, based on disproportionate concentration, there is still much work to be done in both the primary and secondary markets.

Our analysis has led us to four fundamental conclusions:

First, there has been a monumental growth in subprime lending since 1993, suggesting that a significant number of Americans need greater access to the prime lending market.

Second, based on the disproportionate percentage of subprime loans in low and very-low income neighborhoods, there are significant potential benefits to increasing access to prime lending for these communities and families.

Third, based on the disproportionate percentage of subprime loans in African-American neighborhoods, there needs to be much greater attention focused on how to continue to increase access to prime lending markets for these communities and families.

Fourth, based on the disproportionate percentage of subprime loans held by homeowners in high income black neighborhoods, these borrowers need greater access to the prime lending market.

The first step to ensuring that subprime lending acts to enhance, and not destroy, the economic health of the families involved, is to learn more about how and where it operates in America. This analysis is the first look at the most recent nationwide data on subprime lending broken down by the income and racial characteristics of neighborhoods nationwide.

THE FINDINGS

HUD'S detailed analysis of almost 1 million mortgages reported in 1998 under HMDA reaches four critical conclusions about the state and consequences of subprime lending in America:

1. **From 1993 to 1998, the Number of Subprime Refinance Loans Increased Ten-Fold** - In 1993, there were just 80,000 subprime loans reported to HMDA. By 1998, there were more than 790,000. Over the same period, there was a seven-fold increase in the dollar volume of subprime loans, from $20 billion to $150 billion.

2. **Subprime Loans are Three Times More Likely in Low-Income Neighborhoods than in High-Income Neighborhoods** - In low-income neighborhoods, subprime loans accounted for 26 percent of total loans in 1998 - compared with only 11 percent in moderate-income neighborhoods and just 7 percent in upper-income neighborhoods. Comparable 1993 figures were 3 percent in low-income neighborhoods and 1 percent each in moderate-income and upper-income neighborhoods.

3. **Subprime Loans are Five Times More Likely in Black Neighborhoods than in White Neighborhoods** - In predominantly black neighborhoods, the high-cost subprime lending accounted for 51 percent of home loans in 1998 - compared with only 9 percent in predominately white areas. Comparable 1993 figures were 8 percent in black neighborhoods and 1 percent in white neighborhoods.

4. **Homeowners in High-Income Black Neighborhoods Are Twice as Likely as Homeowners in Low-Income White Neighborhoods to have Subprime Loans** - Only 6 percent of homeowners in upper-income white neighborhoods have subprime loans while 39 percent of homeowners in upper-income black neighborhoods have subprime loans, more than twice the rate for homeowners in low-income white neighborhoods, 18 percent.

THE ANALYSIS

HUD's detailed study of the almost 1 million mortgages reported to HMDA in 1998 focused primarily on home refinancing loans, which account for 80 percent of costly subprime loans. Subprime lending involves providing credit to borrowers with past credit problems, often at a higher cost or less favorable terms than loans available in the conventional prime market. In some cases, subprime lenders engage in abusive lending practices known as "predatory lending", which hits homebuyers with excessive mortgage fees, interest rates, penalties and insurance charges that raise the cost of homebuying by thousands of dollars for individual families.

HUD's study found that:

1. From 1993 to 1998, the number of subprime refinance loans increased ten-fold.

In 1993, there were 80,000 subprime refinance loans reported under HMDA. By 1998, this number had increased by over 900% to 790,000. (See Figure 1.) Because refinancing represents 80% of the subprime market, this analysis looks most closely at the 790,000 refinancing loans. But in the total subprime market, the number of loans increased at the same pace from 104,000 to nearly one million (997,000) in 1998.

The magnitude and speed of the increase in subprime lending alone - almost 1000% in just five years - creates a critical need for greater scrutiny and concern. While the rapid growth of subprime lending may, on the surface, appear to be good news for higher-risk borrowers, behind the numbers there is some evidence that some portion of subprime lending is occurring with borrowers whose credit would qualify them for conventional loans. Subprime lending may expose borrowers to higher up-front fees and interest rates than they would bear if they had obtained prime loans.

2. Subprime loans are three times more likely in low-income neighborhoods than in high-income neighborhoods.

HUD's analysis of almost 1 million loans reported under HMDA for 1998 also demonstrates that subprime lending is being provided increasingly to low- and very low-income families. Nationwide, 11% of refinance mortgages in 1998 were subprime, but in low-income neighborhoods, the percentage more than doubles to 26%. (See Figure 2) In upper income neighborhoods, only 7% of families have subprime refinancing debt. In 1993, only 3 percent of mortgages in low-income neighborhoods and 1 percent each in moderate- and upper-income neighborhoods were subprime.

But in the poorest communities, where families make only 50% of the median income, subprime refinances are an astounding 44%. Broken down by individuals instead of entire neighborhoods, the impact is similar. Low-income borrowers are almost 3 times as likely as upper income borrowers to rely upon subprime refinancing, (21% of low-income vs. 8% of upper-income borrowers.)

3. Subprime loans are five times more likely in black neighborhoods than in white neighborhoods.

In predominantly black neighborhoods, the high-cost subprime lending accounted for 51 percent of home loans in 1998 - compared with only 9 percent in predominately white areas. Comparable 1993 figures were 8 percent in black neighborhoods and 1 percent in white neighborhoods.

A close examination of the 1998 HMDA data broken down by neighborhood racial composition raises the need for closer scrutiny. While subprime refinance mortgages accounted for one-tenth of the refinance mortgages in predominantly white neighborhoods in 1998, in predominantly black neighborhoods, **half** of the refinance mortgages were subprime. (See Figure 3.) This means that only one in ten families in white neighborhoods pay higher fees and interest rates, but **five in ten families in African-American communities are saddled with higher rates and costs**.

Broken down by individual borrowers instead of neighborhoods, blacks are still carrying the greater proportion of subprime: 33% of all refinance mortgages in 1998, compared with only 8% for whites borrowers overall. In total, black borrowers support 13% of the subprime mortgage market, but only 5% of the mortgage market overall.

4. Homeowners in high-income black neighborhoods are twice as likely as homeowners in low-income white neighborhoods to have subprime loans.

The most dramatic view of this trend comes from comparing homeowners in upper income black and white neighborhoods. Among homeowners living in the upper income white neighborhoods, only 6% turn to subprime lenders. But 39% of homeowners living in upper-income black neighborhoods have subprime refinancing. (See Figure 4.) This is more than twice the rate - 18 percent - for homeowners living in low-income white neighborhoods.

In fact, as neighborhood income increases, the disparity between the African-American and white neighborhoods grows larger. Homeowners in low-income black communities are almost 3 times as likely as homeowners in low-income white communities to have subprime refinancing. For moderate income neighborhoods, black neighborhoods are 4 times as likely and in the upper income neighborhoods, blacks neighborhoods are six times as likely as white neighborhoods to have subprime financing.

METROPOLITAN DYNAMICS

This new analysis also presents the first recent look at subprime refinancing by metropolitan areas. A look at five cities gives a good sense that the trends identified above are consistent at the metropolitan level.

- In **Atlanta**, in about one-fifth of the 475 census tracts subprime refinancing accounts for at least 25% of all refinancing. In the vast majority of these census tracts, the population is at least 30%

black.

- In **Philadelphia**, black neighborhoods carried about 10% of the refinancing overall, but 36% of the subprime market.

- In **New York**, subprime refinancing represents one in four loans in **more than half** of all census tracts, and black neighborhoods alone carry almost 50% of all the subprime lending in the city.

- In **Chicago**, 41% of the subprime refinancing occurs in black neighborhoods, compared to only 10% of the overall refinancing.

- In **Baltimore**, almost one-third of the census tracts (27%) have at least 25% subprime refinancing, with the greatest burden falling upon the black neighborhoods (118 our of 156 tracts).

CONCLUSION

HUD's analysis of almost one million mortgages reported to HMDA in 1998 clearly demonstrates the exponential growth in subprime lending and its disproportionate impact on low-income and, particularly, minority homeowners and communities throughout the nation. This concentration of subprime activity leaves these homeowners with significant costs of subprime loans. These borrowers may also be vulnerable to predatory lending practices.

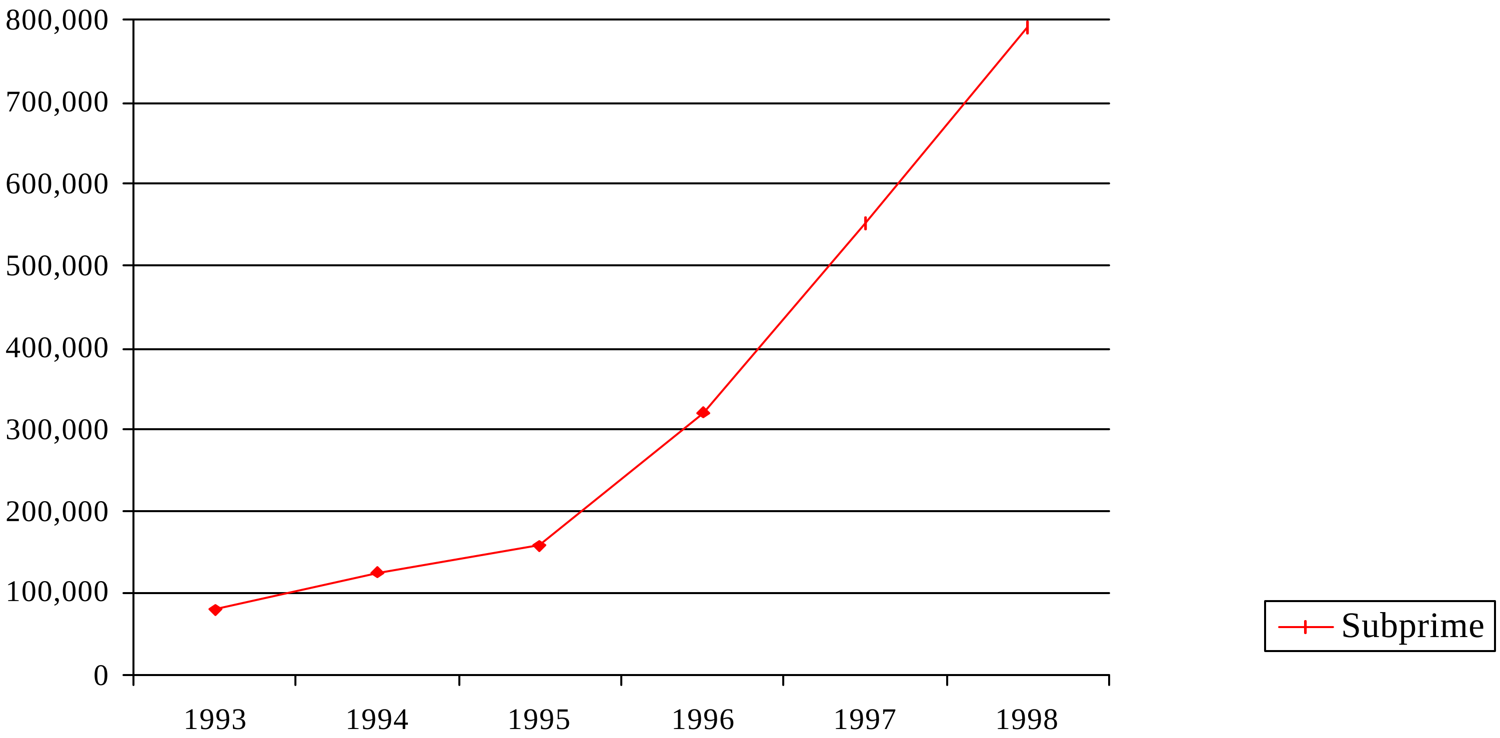
Despite the progress made by prime lenders in reaching these markets, the growing concentration of subprime loans in both low-income and minority communities, strongly suggest that much more can be done by both primary and secondary market participants to expand access to the prime lending market.

HUD's analysis clearly demonstrates the need for timely and concerted Federal action in this area - both to expand access to prime lending in these communities and to protect subprime borrowers from the dangers of predatory lending.

Figure 1

Growth in Subprime Refinance Lending

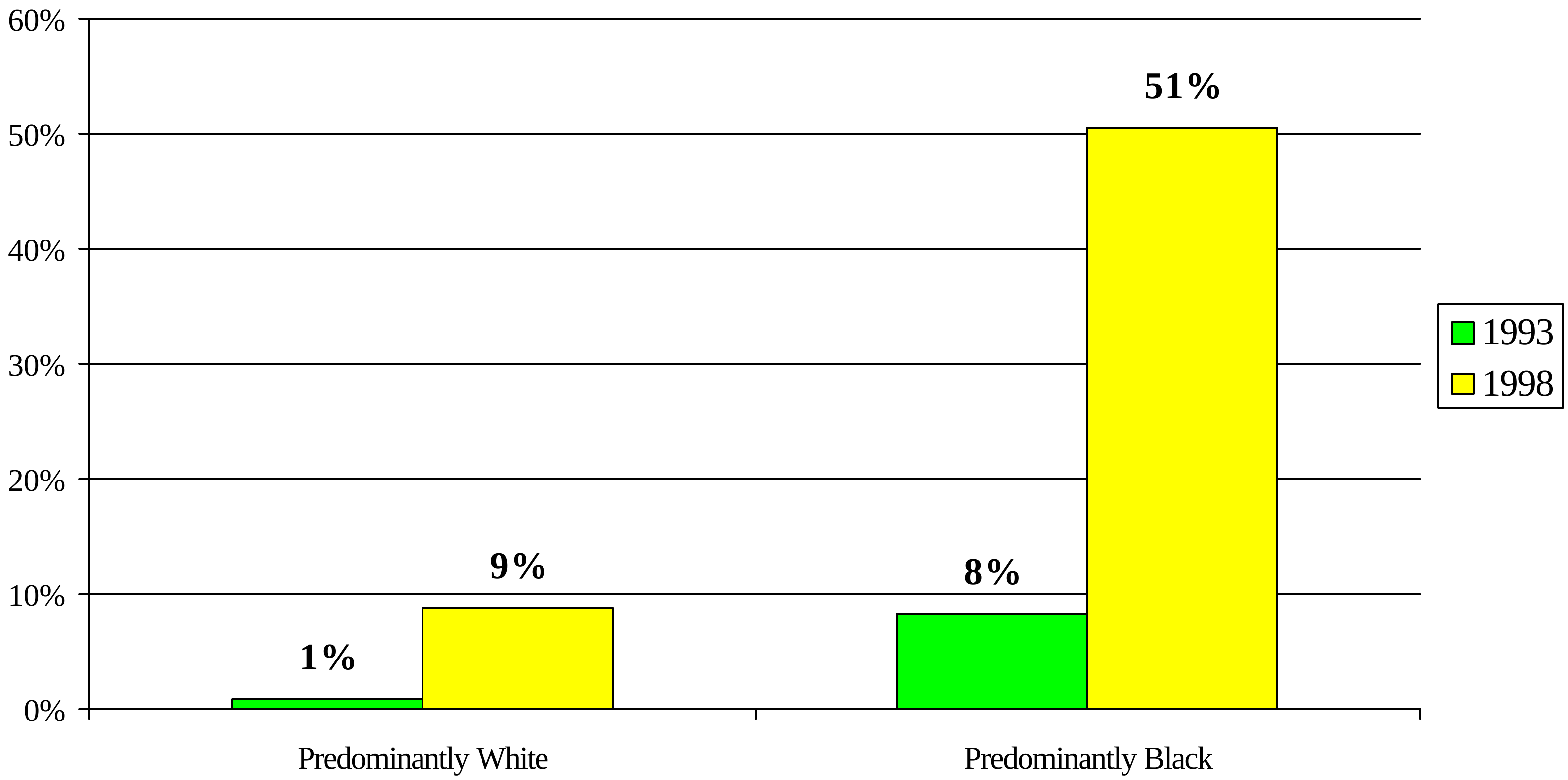
	1993	1994	1995	1996	1997	1998
Subprime	79,693	126,776	158,395	320,239	551,396	789,696



Source: 1993-1998 HMDA Data

Figure 2

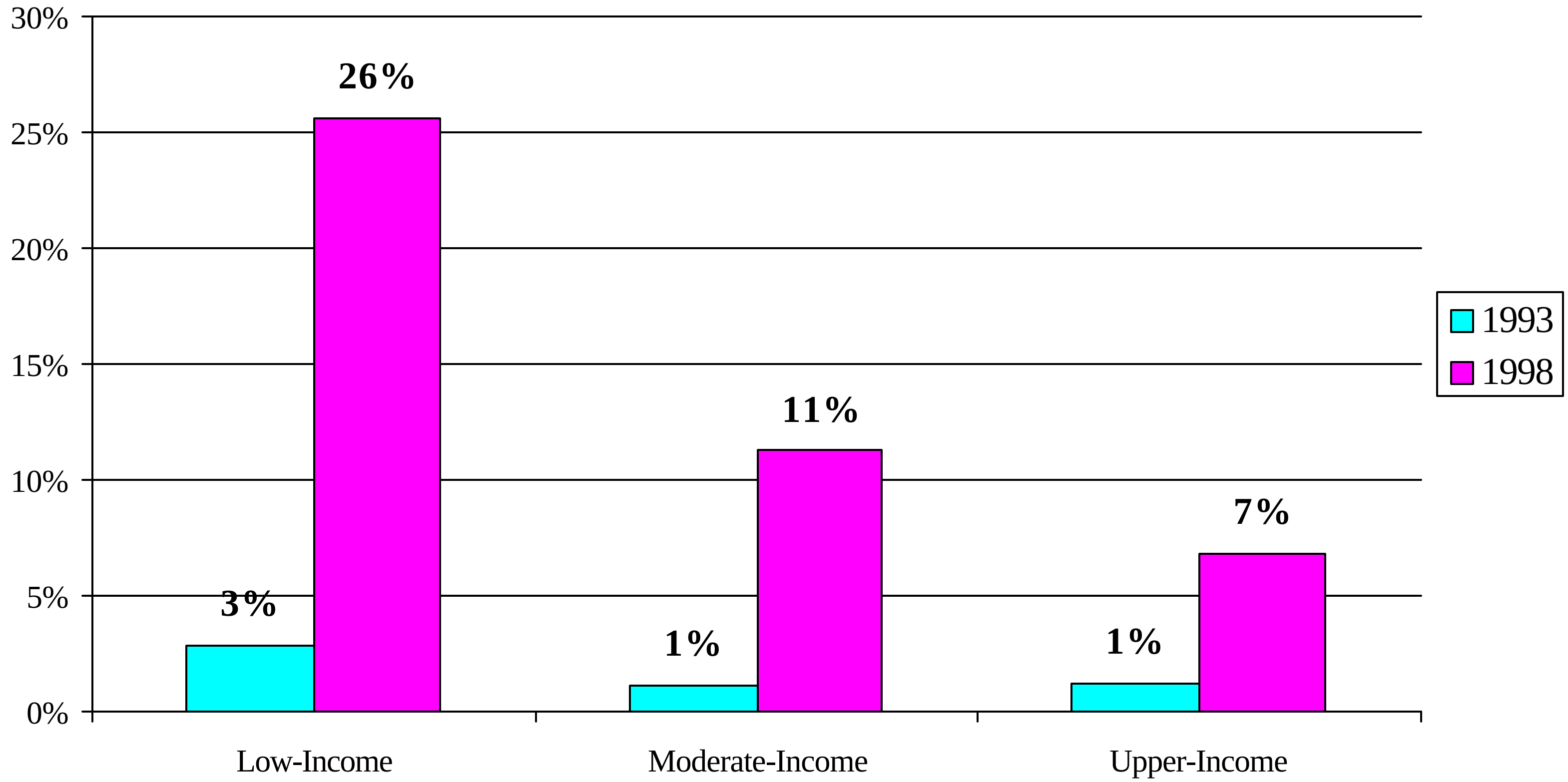
Subprime Share of Refinance Mortgages by Neighborhood Race



Note: Predominantly White: At least 85% White; Predominantly Black: At least 75% Black.

Figure 3

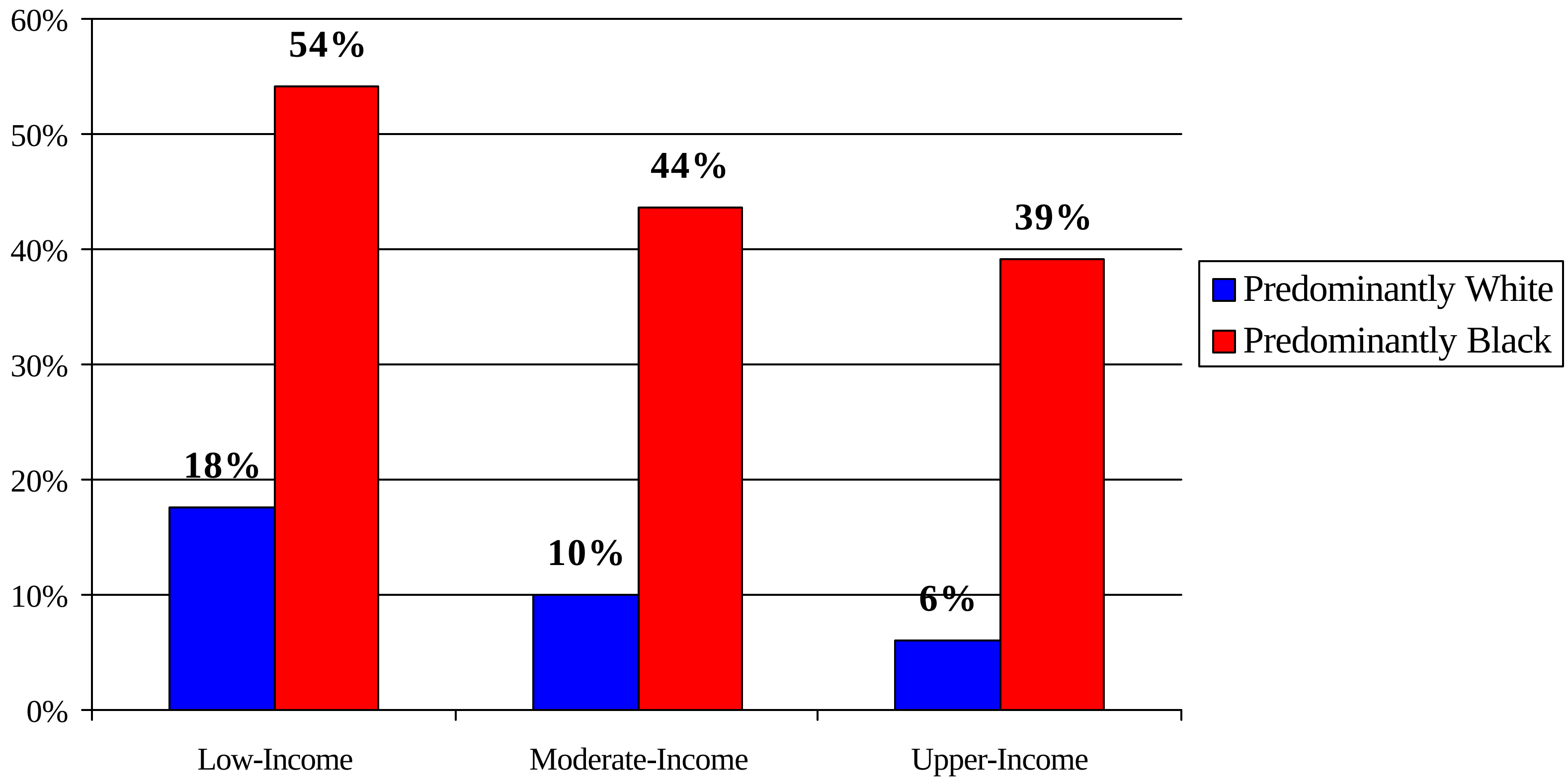
Subprime Share of Refinance Mortgages by Neighborhood Income



Note: Low-Income: Not More than 80%; Moderate-Income: 80-120%; Upper-Income: More than 120%

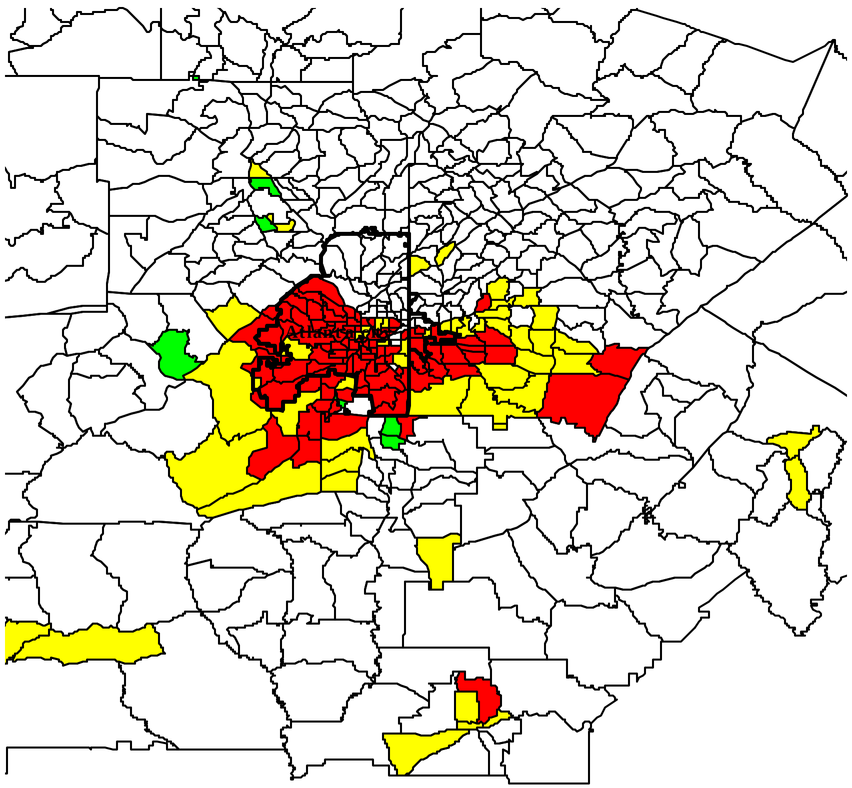
Figure 4

Subprime Share of 1998 Refinance Mortgages by Neighborhood Race and Income



Note: Predominantly White: At least 85% White; Predominantly Black: At least 75% Black.
Low-Income: Not More than 80%; Moderate-Income: 80-120%; Upper-Income: More than 120%

Atlanta Metropolitan Area
Refinance Market



Subprime mortgages accounted for at least 25 percent of all refinance mortgages in 101 (or 21 percent) of the 475 census tracts in the Atlanta, Georgia metropolitan area refinance market.

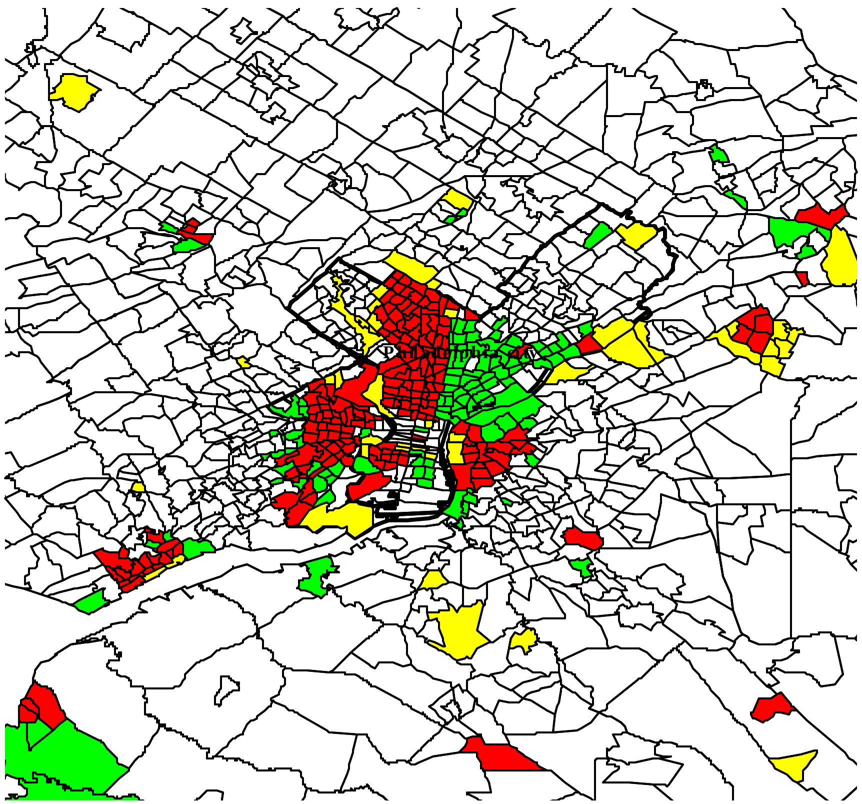
Census tracts where Blacks comprised at least 30 percent of the population (Black neighborhoods) accounted for 94 of these 101 subprime census tracts.

Black neighborhoods accounted for 13 percent of all refinances in the Atlanta, Georgia metropolitan area but 33 percent of all subprime refinances.

- Subprime and Black Neighborhoods
- Other Subprime Neighborhoods
- Other Black Neighborhoods

Source: 1998 HMDA Data

Philadelphia Metropolitan Area
Refinance Market



Subprime mortgages accounted for at least 25 percent of all refinance mortgages in 319 (or 25 percent) of the 1,260 census tracts in the Philadelphia metropolitan area refinance market.

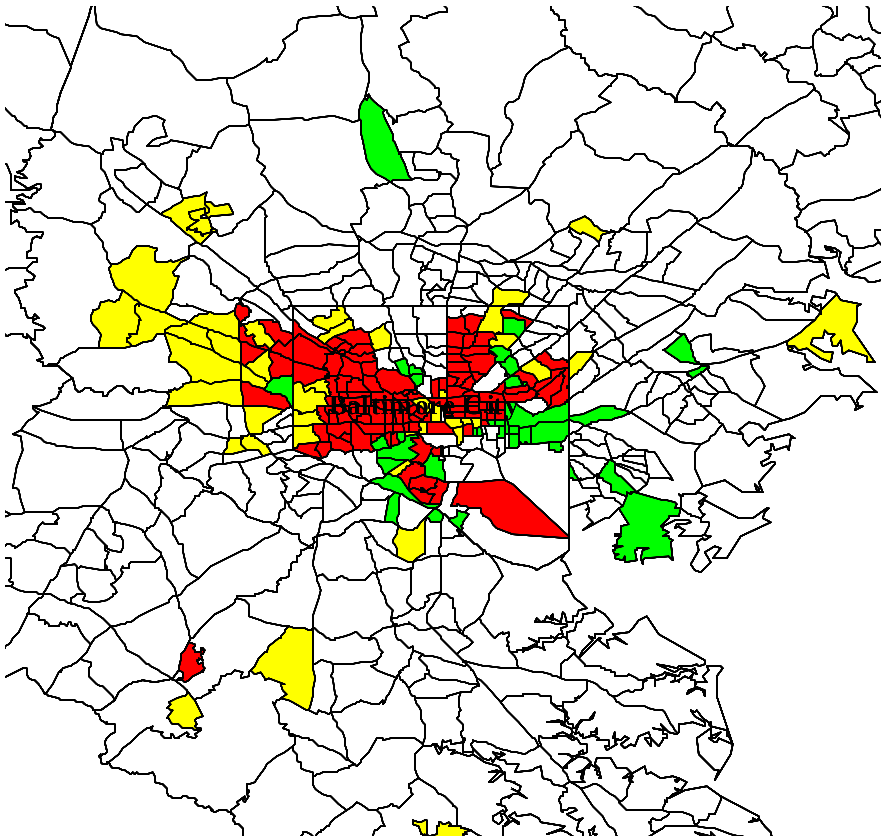
Census tracts where Blacks comprised at least 30 percent of the population (Black neighborhoods) accounted for 201 of these 319 subprime census tracts.

Black neighborhoods accounted for 10 percent of all refinances in the Philadelphia metropolitan area but 36 percent of all subprime refinances.

Subprime and Black Neighborhoods
Other Subprime Neighborhoods
Other Black Neighborhoods

Source: 1998 HMDA Data

Baltimore Metropolitan Area
Refinance Market



Subprime mortgages accounted for at least 25 percent of all refinance mortgages in 156 (or 27 percent) of the 574 census tracts in the Baltimore metropolitan area refinance market.

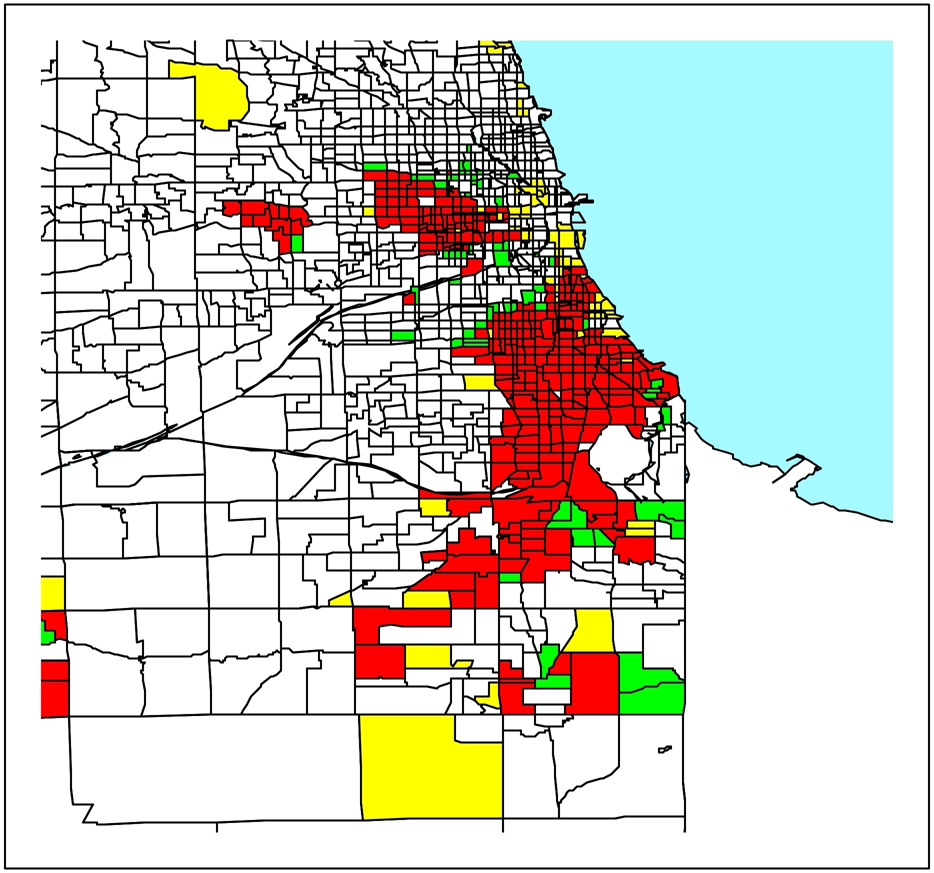
Census tracts where Blacks comprised at least 30 percent of the population (Black neighborhoods) accounted for 118 of these 156 subprime census tracts.

Black neighborhoods accounted for 13 percent of all refinances in the Baltimore metropolitan area but 36 percent of all subprime refinances.

- Subprime and Black Neighborhoods
- Other Subprime Neighborhoods
- Other Black Neighborhoods

Source: 1998 HMDA Data

Chicago Metropolitan Area
Refinance Market



Subprime mortgages accounted for at least 25 percent of all refinance mortgages in 438 (or 25 percent) of the 1,767 census tracts in the Chicago metropolitan area refinance market.

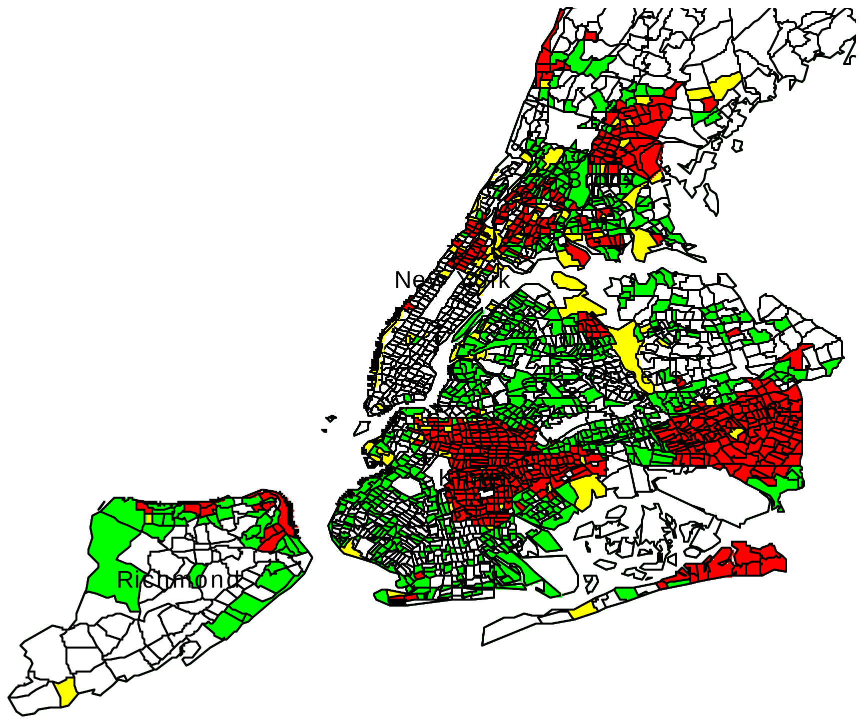
Census tracts where Blacks comprised at least 30 percent of the population (Black neighborhoods) accounted for 367 of these 438 subprime census tracts.

Black neighborhoods accounted for 10 percent of all refinances in the Chicago metropolitan area but 41 percent of all subprime refinances.

Subprime and Black Neighborhoods
Other Subprime Neighborhoods
Other Black Neighborhoods

Source: 1998 HMDA Data

New York Metropolitan Area
Refinance Market



Subprime mortgages accounted for at least 25 percent of all refinance mortgages in 1,265 (or 52 percent) of the 2,420 census tracts in the New York metropolitan area refinance market.

Census tracts where Blacks comprised at least 30 percent of the population (Black neighborhoods) accounted for 598 of these 1,265 subprime census tracts.

Black neighborhoods accounted for 23 percent of all refinances in the New York metropolitan area but 49 percent of all subprime refinances.

- Subprime and Black Neighborhoods
- Other Subprime Neighborhoods
- Other Black Neighborhoods

Source: 1998 HMDA Data