

*20th Annual Fair Lending Conference
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Racial Segregation and the American Foreclosure Crisis

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Outline

- ▶ The Effect of Segregation
- ▶ Residential Racial Segregation since 1980
- ▶ Segregation and the Foreclosure Crisis
 - ▶ Securitization and Subprime Lending
 - ▶ Consequences of Unequal Lending
- ▶ A Model of Differences in Foreclosures
- ▶ The Segregation-Subprime Link
 - ▶ The Link: Discrimination
- ▶ Conclusions for Fair Lending

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The Effect of Segregation

- ▶ Black Segregation Played a Major Role in Structuring the U.S. Foreclosure Crisis
 - ▶ Strongest Single Predictor of Rate and Number of Foreclosures Across Metro Areas
- ▶ Controlling for Host of Other Factors
 - ▶ Housing Price Inflation
 - ▶ Degree of Subprime Lending
 - ▶ Credit Worthiness of Borrowers
 - ▶ Land Use Regulation
 - ▶ CRA Coverage
 - ▶ Income, Education, Population Size, Region, Coastal Location

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Residential Racial Segregation since 1980

- ▶ Fair Housing Act 1968 and legislation of 1970s
- ▶ Uneven Decrease in Segregation of Blacks
 - ▶ Larger decrease in metros with small black populations
 - ▶ West, Southwest, and South
- ▶ Decreases *much smaller* in the Midwest, Northeast
 - ▶ Metros with larger black populations
 - ▶ Some places have seen very little change
 - ▶ Levels remain extremely high
- ▶ Hispanic, Asian segregation risen modestly
 - ▶ Overall levels low to moderate

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Segregation and the Foreclosure Crisis

- ▶ Crisis product of market forces and racial dimensions
- ▶ Context of rise in minority homeownership since 1990
 - ▶ Fueled by increase in subprime lending
 - ▶ Nearly half of rise in black homeownership in 1990s
 - ▶ In neighborhoods previously denied mortgage credit
- ▶ Collapse of housing market in 2006-2007
 - ▶ Price bust, overbuilding, leveraged borrowers, lax standards
 - ▶ Foreclosures concentrated in segregated areas
 - ▶ Context of segregation unappreciated

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Securitization and Subprime Lending

- ▶ Big shift in incentives for Wall Street during 1990s
 - ▶ Splitting of lending, servicing, securitizing
 - ▶ Segregated minorities no longer shunned
 - ▶ Risks and rewards forever changed
 - ▶ Rise of independent lenders and private label securities
- ▶ Old inequality made new inequality possible (Williams et al 2005)
 - ▶ Marketing of subprime lending made efficient
 - ▶ New type of dual mortgage market
 - ▶ No longer based on outright denial, but instead on abusive terms

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Consequences of Unequal Lending

- ▶ Homeownership rose (for a while), segregation remained
- ▶ Blacks and Hispanics with similar incomes, credit scores, down payments as whites more likely to receive:
 - ▶ Subprime rates, higher cost ratios, prepayment penalties
 - ▶ Racial and ethnic disparities may increase with rising incomes
- ▶ Unexplained racial gap in homeowner stability opens up
- ▶ Among lenders who went out of business in 2007
 - ▶ Blacks three times more likely to get subprime loans (76%)
 - ▶ Hispanics, twice as likely (63%)
 - ▶ Whites actually less likely get subprime loans (only 46%)
- ▶ → U.S. foreclosure rate quadruples from 2006 to 2009

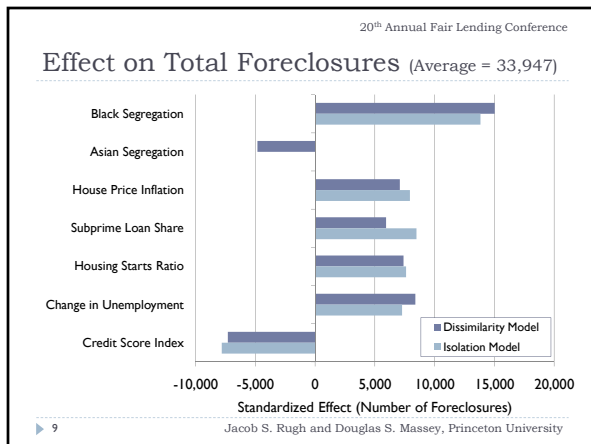
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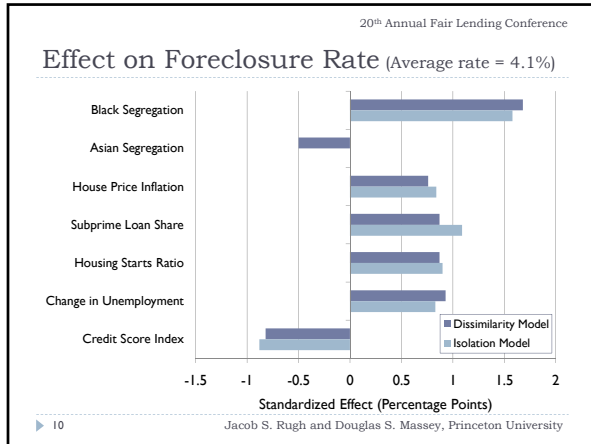
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A Model of Differences in Foreclosures

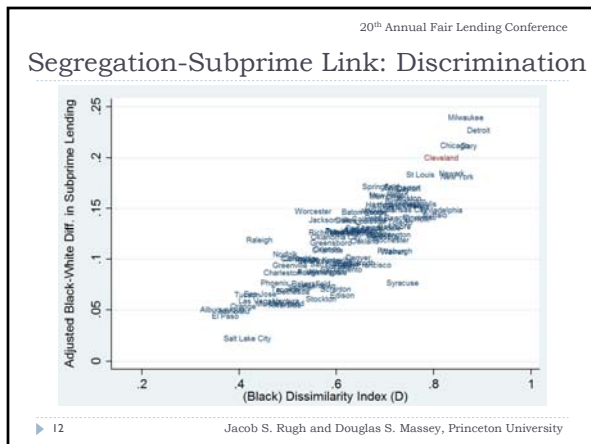
- ▶ Regression model of differences in foreclosures
 - ▶ Number, rate foreclosures: Top 100 metro areas, 2006-2008
 - ▶ Two measures of residential segregation (Black, Hispanic, Asian)
 - ▶ Dissimilarity index (D) and Isolation index (P*)
 - ▶ Control variables at metro area level:
 - ▶ Census: Pop., race, income & education levels, age of housing stock
 - ▶ Ratio of 2000-2006 house price change to 1980-2000 change
 - ▶ Ratio of 2000-2006 housing starts to 2000 housing units
 - ▶ HMDA: % of 2004-2006 loans: - Subprime - Covered by CRA
 - ▶ Average consumer FICO credit score
 - ▶ Wharton Land Use Regulation Index
 - ▶ Change in unemployment rates, 2000-2006
 - ▶ Region, Coastal location, Rio Grande border

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- ### The Segregation-Subprime Link
- ▶ Causal mechanism whereby segregation affects foreclosures
 - ▶ Unexplained racial and ethnic differences in subprime lending
 - ▶ Estimate discrimination in subprime lending for 2004-2006
 - ▶ 5.3 million prime and subprime mortgage loans in HMDA
 - ▶ Calculate probability of receiving subprime loan given:
 - Loan amount • Income • Type of units • Age of units
 - Loan purpose • Purchaser • Area Income • % minority
 - Lien status • Occupancy • Pop. Density • MSA Credit Score
 - ▶ Calculate Black-White and Hispanic-White differences by Metro
 - ▶ Black-white gap: 12% (2% to 24%) Hispanic-white gap: 8% (1% to 18%)
 - ▶ Cleveland: More than half of racial gap remains unexplained
 - ▶ Two-stage regression analysis confirms causal role of segregation
 - Even stronger effect of black segregation & potential effect for Hispanics
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Conclusions for Fair Lending

- ▶ Unequal lending combined with price collapse to cause crisis
 - ▶ New form of discrimination based on race and space
 - ▶ Subprime lending did not promote housing integration
 - ▶ Residential stability for all groups undermined instead
 - ▶ Risky lending and securitization practices fueled the housing boom
 - ▶ Blame does not lie with Community Reinvestment Act

- ▶ Systematic failure to enforce basic civil rights laws
 - ▶ Stronger legislation needed to protect all borrowers
 - Audit studies to measure discrimination
 - Improved HMDA data collection

- ▶ Persistent segregation and discrimination demonstrate the need for stronger reform to prevent another crisis

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“Segregation and the American Foreclosure Crisis” *American Sociological Review* 75(5): 629-651. (October 2010)

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