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Subprime Mortgages and Race: A Bit of Good News May Be Illusory

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Subprime mortgages have been linked to a meltdown in housing and questionable Wall Street practices, and they may have been the original domino that set off America's current economic crisis.

But the loans -- typically made to people with poor credit -- have long been hailed for one reason: They were thought to be a powerful way to increase homeownership rates among minorities, and to provide a mechanism to undo the "redlining" policies of past decades, in which some banks refused to extend loans in predominantly minority neighborhoods, even to applicants with good credit.

Intersecting lines of new sociological evidence, however, suggest that this silver lining may have actually been a part of the cloud: There is growing evidence that the subprime mortgage industry may have both benefited from and contributed to racial segregation in the United States.

The financial industry has strenuously argued that subprime loans were given to people with low incomes and poor credit -- regardless of race.

George Washington University sociologist Gregory D. Squires, however, has been looking at rates of subprime loans issued in about 350 U.S. metropolitan areas. Squires's preliminary findings show that subprime loans were indeed more likely to be issued to people with poor credit and those with limited incomes -- no surprise there. But when Squires holds income and credit factors constant in his analysis, he finds that subprime loans were more likely to be concentrated in areas with higher levels of racial segregation.

"We see these loans heavily concentrated in poor neighborhoods and targeted to minority neighborhoods," he said. "There is some evidence that these neighborhoods were actually targeted -- that lenders have gone after people whom they think are less sophisticated borrowers, including single women and the elderly."

"Credit rating and income would and does explain some of the patterns," Squires added. "But when you control for those, segregation is also a factor. . . . In those metro areas where segregation is highest, the share of loans that are subprime goes up."

The city of Baltimore recently decided to sue a bank over subprime lending practices and race issues. In a lawsuit filed in U.S. District Court, the city argued that it was facing an "unprecedented crisis of residential mortgage foreclosures" and argued that Wells Fargo, a prominent mortgage lender, ought to bear some responsibility for the growing numbers of defaults.

"In contrast to 'redlining,' which involves denying prime credit to specific geographic areas because of the racial or ethnic composition of the area, reverse redlining involves the targeting of an area for the marketing of deceptive, predatory or otherwise unfair lending practices because of the race or ethnicity of the area's residents" the city charged in its complaint.

In 2005 and 2006, according to the complaint and Brad Blower, a lawyer at the firm Relman & Dane that is representing the city, two-thirds of Wells Fargo's foreclosures in Baltimore were in areas that were more than 60 percent African American, whereas only 15.6 percent of the foreclosures were in areas that were less than 20 percent African American.

Wells Fargo rejects the charges and has said racial factors played no role in its lending. If larger numbers of subprime loans were issued in some neighborhoods, in other words, it was only because those neighborhoods tended to have poorer people with weak credit. Individual issues -- not racial patterns -- explains why some people defaulted while others did not, the company argued.

Disparities in lending by race, however, have been striking in many parts of the country: In New York City, for example, an analysis by the Furman Center for Real Estate and Urban Policy found that around 40 percent of subprime loans issued between 2004 and 2006 were made to blacks, and an additional third of such loans were given to Hispanics. Whites, by contrast, received around 10 percent of such loans, as did Asians.

In a rigorous national analysis based on data collected in the 1990s, researchers Carolyn Bond and Richard Williams found the same phenomenon nationwide. But in addition to demonstrating large racial disparities in who got such loans, Bond and Williams also found the loans -- far from reversing racial segregation -- may have actually contributed to increased levels of segregation in the United States.

"By 1999 the proportion of black borrowers receiving loans from subprime lenders was six times what it was in 1992," the researchers wrote in a paper they published in the journal Social Forces.

While the cheap loans did increase black homeownership rates, especially in predominantly minority neighborhoods, they simultaneously increased the risk that homeowners would default on their loans, send houses into foreclosure and drive down the value of entire neighborhoods, making them less attractive for people from other social classes and racial groups who might have once considered moving in.

"Many subprime borrowers are losing their homes, and the deteriorating and destabilized neighborhoods that result are unlikely to foster integration," Bond and Williams concluded. "In the absence of effective action, the findings suggest that persistent or even increasing levels of segregation may be one of the most important long-term consequences of the current home lending crisis."