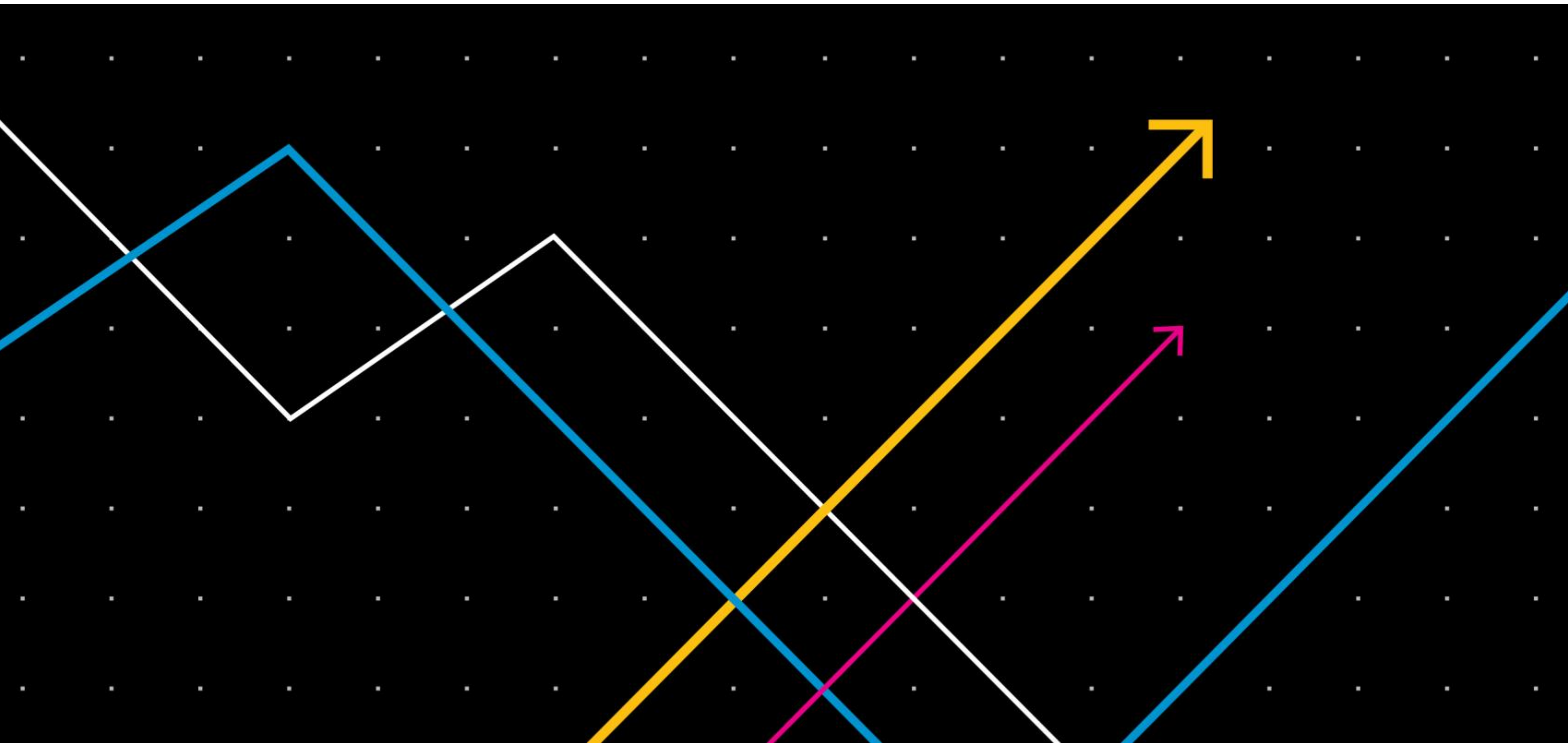

RESEARCH REPORT

Evidence of Disparities in Access to Mortgage Credit

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Evidence of Disparities in Access to Mortgage Credit

Homeownership is regarded as core to the American dream. For most homeowning households, their home is their most valuable asset and provides families the ability to pass on generational wealth. But many communities face barriers and inequities in access to mortgage credit. Special purpose credit programs (SPCPs) are authorized by the Equal Credit Opportunity Act to improve equal access to credit.

This report provides compelling evidence for the need for SPCPs, consistent with Consumer Financial Protection Bureau guidance regarding the need for a broad analysis as part of the required written plan.[1] Using data analyzed by the Urban Institute, the report provides comprehensive documentation of disparities in access to mortgage credit between households of color and white households, considering gaps along three dimensions of credit access (i.e., credit, collateral, and capacity) and their historical and societal causes. These trends are reflected nationally and in varying degrees at the market level.

Mortgage lenders and policymakers are encouraged to use this report as a resource to devise strategies aimed at extending credit to potential homebuyers who would otherwise be denied it or receive it on less favorable terms. By addressing these disparities, we can foster a more equitable lending environment and ensure that homeownership opportunities are accessible to all.

BOX 1

Leveraging Market-Level Data for Effective SPCP Development

This report presents national evidence of disparities in access to mortgage credit and explains the implications of the data. To access and use our market-level data in your written plan, most of the same data points for the 50 largest metropolitan statistical areas (MSAs) are accessible online.[a] You can leverage these data to substantiate the features of your special purpose credit program (SPCP) tailored to the markets you intend to serve. Additional MSA-level data can be used to fine-tune people-based and placed-based eligibility criteria.[b]

[a] See Jun Zhu, Daniel Pang, John Walsh, Aniket Mehrotra, Jung Hyun Choi, and Janneke Ratcliffe, "The Special Purpose Credit Program Data Toolkit," Urban Institute, March 7, 2024, https://www.urban.org/projects/special-purpose-credit-program-data-toolkit.

[b] Jun Zhu, Daniel Pang, John Walsh, Aniket Mehrotra, Jung Hyun Choi, and Janneke Ratcliffe, "Market and Disparity Data Analysis Toolkit," Urban Institute, March 7, 2024, https://www.urban.org/projects/market-and-disparity-data-analysis-toolkit.

State of the Gap: Homeownership Disparities by Race and Ethnicity

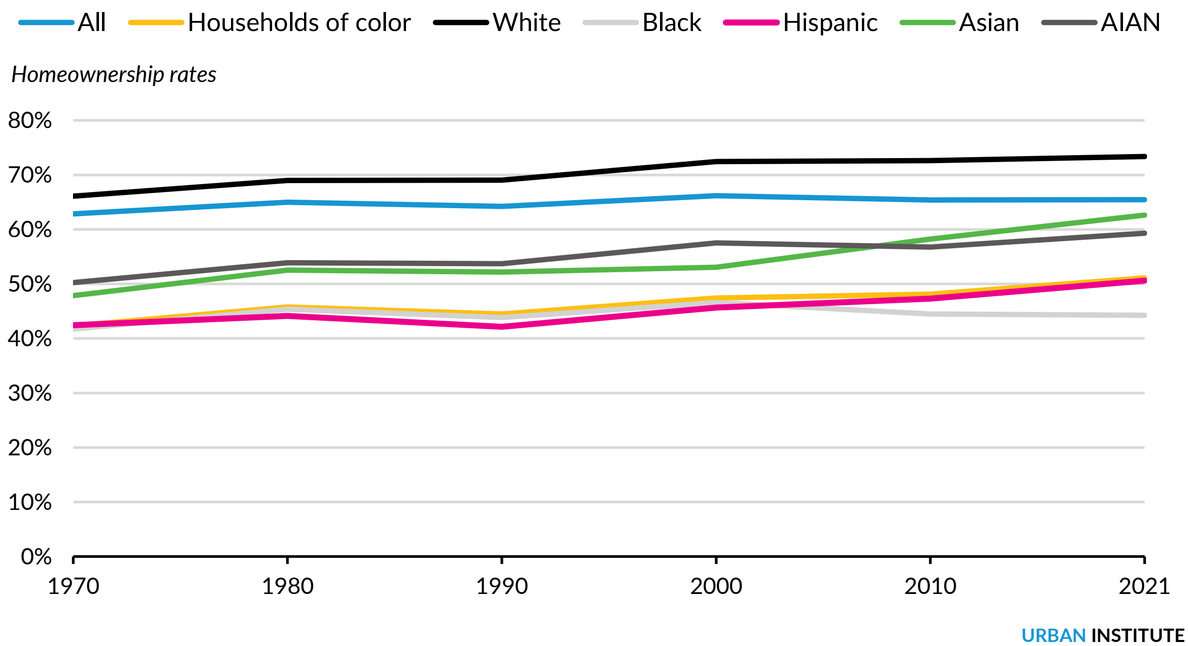
Large gaps in homeownership rates and wealth persist between racial and ethnic groups, as households of color face significant disadvantages relative to white households in both attaining and sustaining homeownership.

The Black-white homeownership rate gap is wider now than it was before the passage of the Fair Housing Act, when housing discrimination was still legal (McCargo and Choi 2020). In 1970, just two years after the passage of the Fair Housing Act, the white homeownership rate was 66 percent, which was 24 percentage points higher than the Black homeownership rate (42 percent), 23 percentage points higher than the Hispanic homeownership rate (43 percent), and 16 percentage points higher than the Asian homeownership rate (48 percent). As of 2021, the nationwide white homeownership rate is 73 percent, which is 29 percentage points higher than the Black homeownership rate (44 percent) and constitutes a larger gap today than in the 1970s.

Hispanic and American Indian or Alaska Native (AIAN) households have seen only modest reductions in the gap over 50 years. The gap between white households and AIAN households (59 percent) is 14 percentage points, while the gap between white households and Hispanic households (51 percent) is 22 percentage points. Asian households (63 percent) have closed their homeownership gap the most but still lag behind white households by around 10 percentage points (figure 1).

FIGURE 1

Homeownership Rates, by Race or Ethnicity, 1970–2021



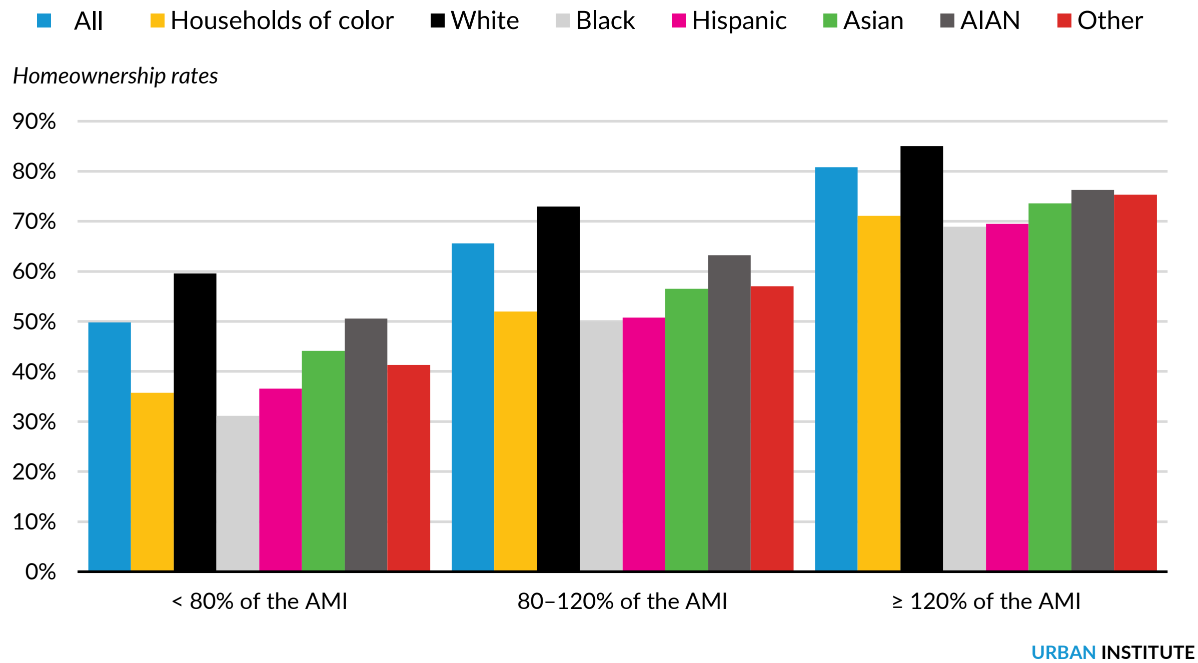
Source: 1970–90 Decennial Censuses and 2000–21 American Community Surveys.
Notes: AIAN = American Indian or Alaska Native. Homeownership rates are calculated by dividing the total number of homeowners by the total number of households. Households include the total number of both homeowners and renters.

Although homeownership rates rise with income and educational attainment for all groups, the gaps persist across various incomes and levels of educational attainment (figures 2 and 3). Additionally, once we control for household income and education, we find that the Asian-white homeownership gap widens.

Figure 2 shows that even after controlling for income, households of color have substantially lower homeownership rates than white households. We separated households into three groups by comparing their income with the area median income (AMI): below 80 percent of the AMI, 80 to 120 percent of the AMI, and at least 120 percent of the AMI. For all three groups, white households have a much higher homeownership rate than households of color, but larger gaps are shown in the lower-income group. For example, the Black-white homeownership gap stood at 28 percentage points for households earning below 80 percent of the AMI, 23 percentage points for those earning 80 to 120 percent of the AMI, and 16 percentage points for those earning at least 120 percent of the AMI. The Hispanic-white homeownership gap was 23 percentage points for the two lower income groups and was 15 percentage points for the highest income group.

FIGURE 2

Homeownership Rates, by Income as a Share of Area Median Income and Race or Ethnicity

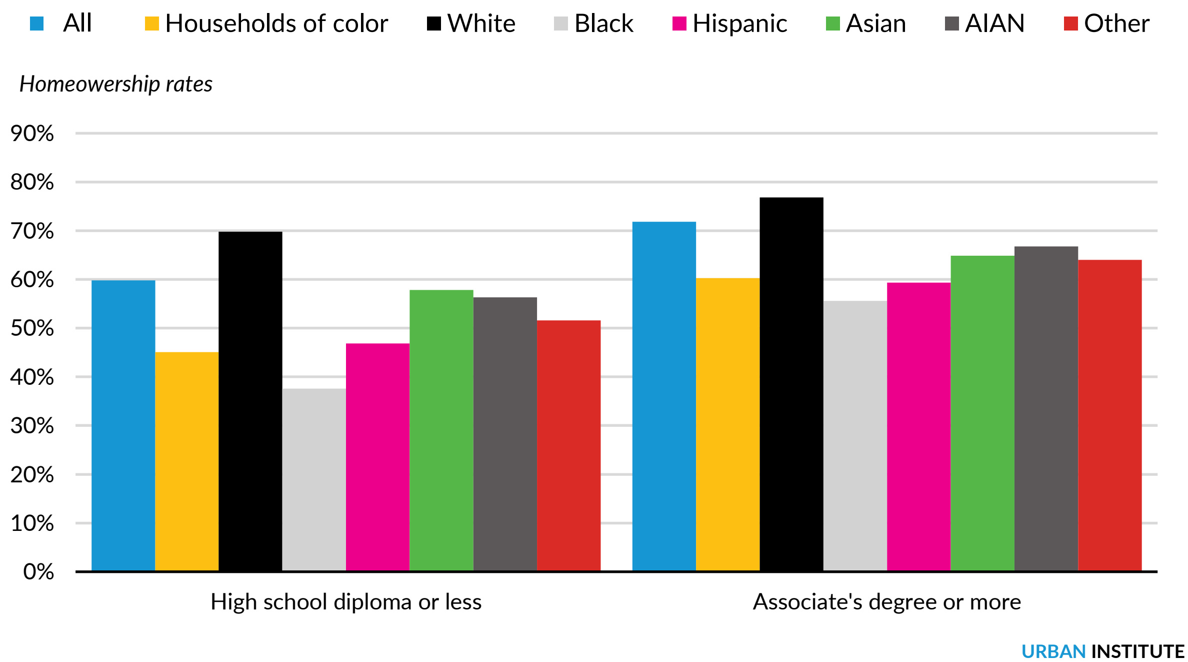


Source: 2021 American Community Survey.
Note: AIAN = American Indian or Alaska Native; AMI = area median income.

Homeownership rates are positively correlated with education levels. Yet this relationship alone does not fully account for the racial and ethnic disparity we observe. In figure 3, we separate households into two groups: (1) those who completed high school or left high school before earning a diploma, and (2) those who earned an associate's degree or more. Among households with no more than a high school diploma, the homeownership gap between white and black households stands at 31 percentage points. Although this gap diminishes for households with more educational attainment, it remains significant, at approximately 21 percentage points.

FIGURE 3

Homeownership Rates, by Educational Attainment and Race or Ethnicity



Source: 2021 American Community Survey.
Note: AIAN = American Indian or Alaska Native.

Historical Roots in Government Policies and Industry Practices

Households of color were excluded from homeownership and critical credit access programs afforded to white households, which led to persistent racial disparities in homeownership and household wealth (Rothstein 2017). In the early 20th century, racially restrictive covenants in neighborhoods across the US prohibited African American, Hispanic, Asian, and other nonwhite households from purchasing homes in certain communities (often white and affluent).[2] These local practices were enshrined at the federal level during the Great Depression when the Home Owner's Loan Corporation and the Federal Housing Administration were established to allow Americans to sustain homeownership and facilitate access to mortgage credit. But the benefits of affordable, long-term mortgage loans with amortized payments at favorable rates were explicitly and systematically denied to communities of color that were designated as "hazardous" on residential maps, a process known as redlining (Rothstein 2017).

Redlining was one of several policies that inhibited the potential of homeownership and wealth obtainment for households of color. When these households did build wealth, it was often vulnerable to destruction by private actors, such as in the Tulsa race riots, which cost more than $27 million in Black wealth, as well as government decisionmakers, who plowed through burgeoning Black and Hispanic communities with new midcentury interstate highway construction.[3]

More recently, driven by targeted lending of predatory products to borrowers of color, the 2008 foreclosure crisis had a greater negative economic impact on homeowners of color than it did on white homeowners. Black and Hispanic homeowners were 76 and 71 percent more likely to be foreclosed on than white homeowners, respectively (McCargo, Choi, and Golding 2019; Neal and McCargo 2020),[4] and prohibitively tight credit in the aftermath of the recession reduced lending to Black and Hispanic borrowers by 76 and 78 percent between 2005 and 2012 (Goodman, Zhu, and George 2014). Negative shocks like recessions and natural disasters still disproportionally affect homeowners of color, widening gaps and setting these households further back (Neal and McCargo 2020).

For a more detailed description of the historical and societal roots of racial disparities in credit access, see Young, Neal, and Ratcliffe (2022).

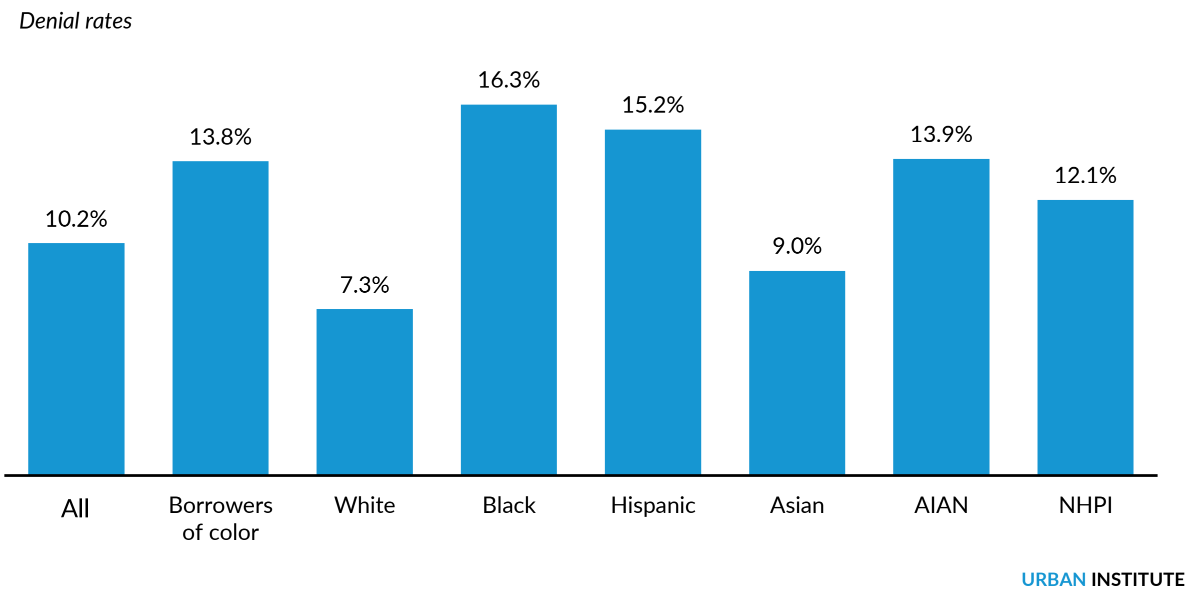
Present Circumstances

Despite the passage of the Equal Credit Opportunity Act in 1974, access to mortgage credit remains disparate. The largest legislation intended to remedy historic lending discrimination, the Community Reinvestment Act, has fallen short of creating equal access to housing credit. Majority-nonwhite communities receive less lending as a share of households than majority-white neighborhoods, and research shows that the “low- and moderate-income” designation that guides Community Reinvestment Act activity is not a strong proxy for race (Goodman et al. 2022). Upcoming changes, the first major changes to the act since 1995, still do not explicitly consider race.[5]

Home Mortgage Disclosure Act data show that it remains harder for households of color to attain mortgage financing. Because mortgage application numbers fluctuated largely with shifts in interest rates,[6] for some analysis using Home Mortgage Disclosure Act data, we aggregated five years of annual data (2018 to 2022) to smooth the time trend volatility.

FIGURE 4

Denial Rates, by Race or Ethnicity



Source: 2018–22 Home Mortgage Disclosure Act data.
Notes: AIAN = American Indian or Alaska Native; NHPI = Native Hawaiian or other Pacific Islander. Sample includes first-lien purchase loan applications in 2022. Denial rates are calculated by taking the total number of denials divided by the total number of applications. Applications include originated loans, applications that are approved but not accepted, denied applications, denied preapproval requests, and approved preapproval requests that were not accepted. Denials include denied applications and denied preapproval requests.

The persistence of these gaps, long after overtly discriminatory practices have been barred, is evidence of the systemic barriers that still prevent potential mortgage borrowers from receiving credit or receiving it on terms as favorable as they are for white borrowers.[7]

Ultimately, homeownership gaps will not be closed without improving equity in credit access. The route to achieve this begins with how mortgage lending decisions are made: based on the three Cs (i.e., collateral, capacity, and credit), the requirements of which disproportionately disadvantage households of color. Although blatant racial discrimination in mortgage underwriting has largely been eliminated, the three Cs that evaluate borrowers' eligibility are also outcomes of historical discrimination in the housing and labor markets and result in a continuous racial gap in access to credit:[8]

- Collateral: Disparities in wealth for down payment and closing costs
- Capacity: Disparities in evaluating income and ability to repay
- Credit: Disparities in assessing "creditworthiness"

SPCPs are designed to reduce these disparities in safe and sustainable ways. Below, we further examine racial disparities in each of the three Cs.

Collateral: The Case for Programs and Products That Address Wealth Disparities

Because of a legacy of being barred from wealth-building opportunities, especially from the post–WWII housing boom that created the white middle class, Black and Hispanic families have a fraction of the wealth white families have (figure 5).[9] According to the 2022 Survey of Consumer Finances, the average white household had about six times the wealth as the average Black household and five times the wealth as the typical Hispanic household.[10]

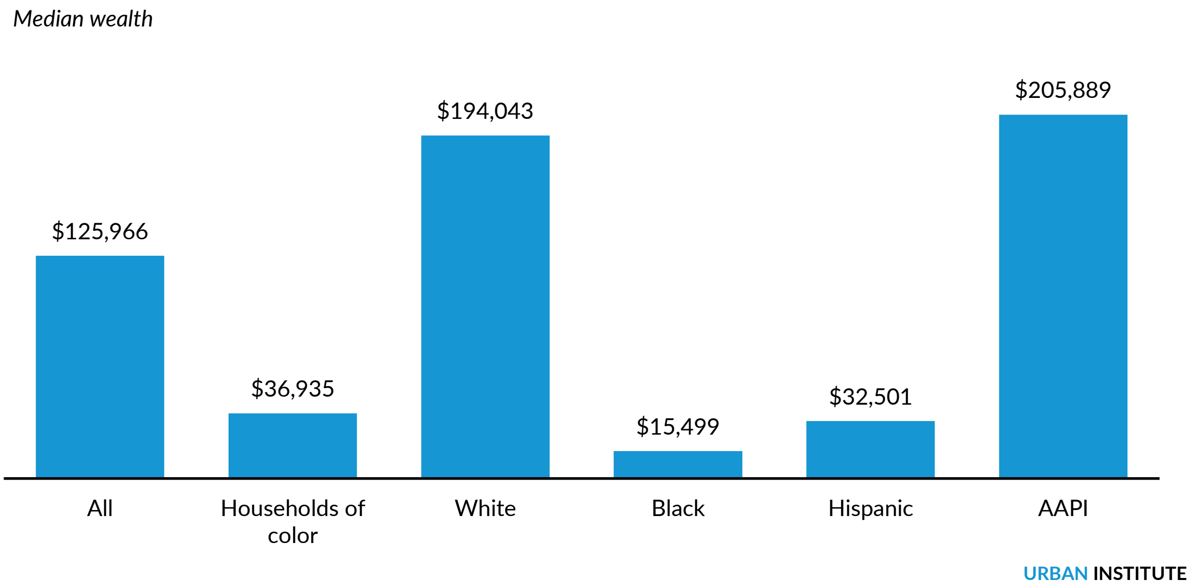
The wealth gaps continue to compound from generation to generation through intergenerational wealth transfers. Thirty percent of white families receive an inheritance or gift, compared with about 10 percent of Black families and 7 percent of Hispanic families.[11] These wealth disparities echo into all other areas of opportunity, across generations. For example, Black consumers are more likely to rely on student loans to access higher education and tend to borrow more and experience higher rates of default than white consumers, draining savings that may otherwise be put toward buying a home (Blagg et al. 2022). Wealth also affects the ability to have sufficient down payment and closing costs for potential homebuyers.

Down Payment

Renters consistently cite a lack of cash for a down payment and closing costs as the primary barrier to becoming homeowners (Goodman et al. 2018). For households of color, saving up for a down payment is a substantial task.

FIGURE 5

Median Wealth, by Race or Ethnicity

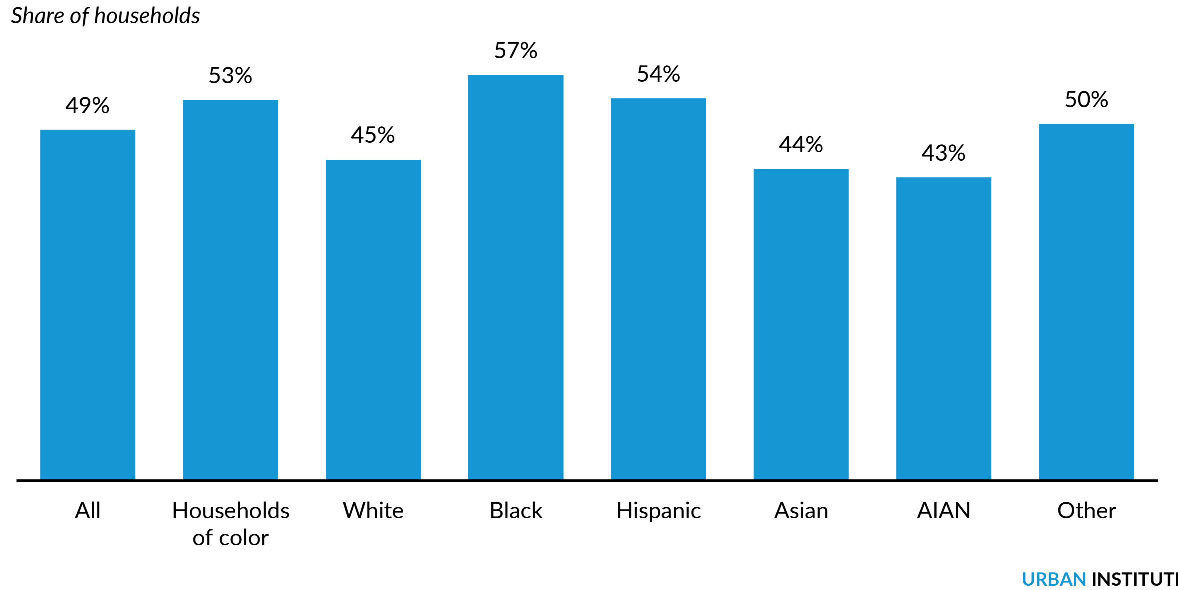


Source: Urban Institute Financial Health and Wealth Dashboard calculations using 2021 credit bureau data, 2018 Survey of Income and Program Participation data, and 2019 American Community Survey one-year data.
Note: AAPI = Asian American or Pacific Islander.

Increasing rental costs relative to income is also making it more challenging for households of color to save for a down payment. Because of their lower incomes, a large share of Black and Hispanic renters in particular pay more than 30 percent of their incomes on housing, which limits their capability to save for future home purchases (figure 6).

FIGURE 6

Share of Housing Cost–Burdened Renter Households, by Race or Ethnicity

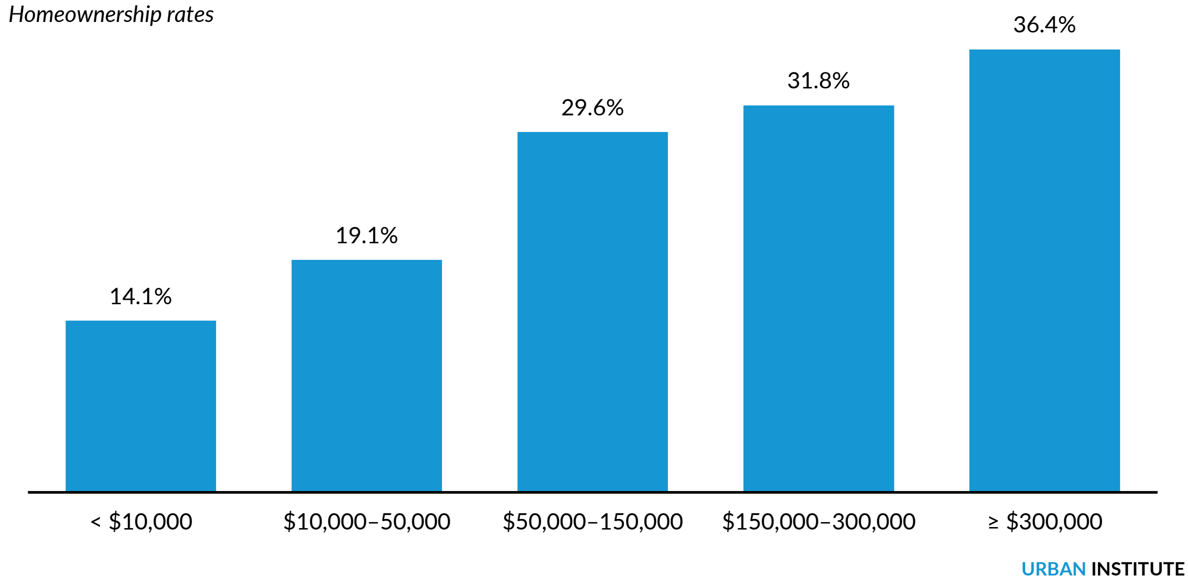


Source: 2021 American Community Survey one-year data.
Note: AIAN = American Indian or Alaska Native.

Homeownership is itself a wealth-building vehicle (Goodman and Mayer 2018), and the historic homeownership gap has limited wealth-building opportunities for households of color. Additionally, having parents who were homeowners and who had more than $200,000 in wealth greatly increases the likelihood of becoming an owner, and Black and Hispanic households are less likely to have these advantages (Choi, Zhu, and Goodman 2018) (figure 7). Black households are less likely to receive intergenerational wealth transfers (Neal et al. 2023), and gifts from relatives account for approximately 32 percent of down payments for first-time homebuyers (National Association of REALTORS® Research Group 2019).

FIGURE 7

Homeownership Rates, by Parental Wealth, Nationally

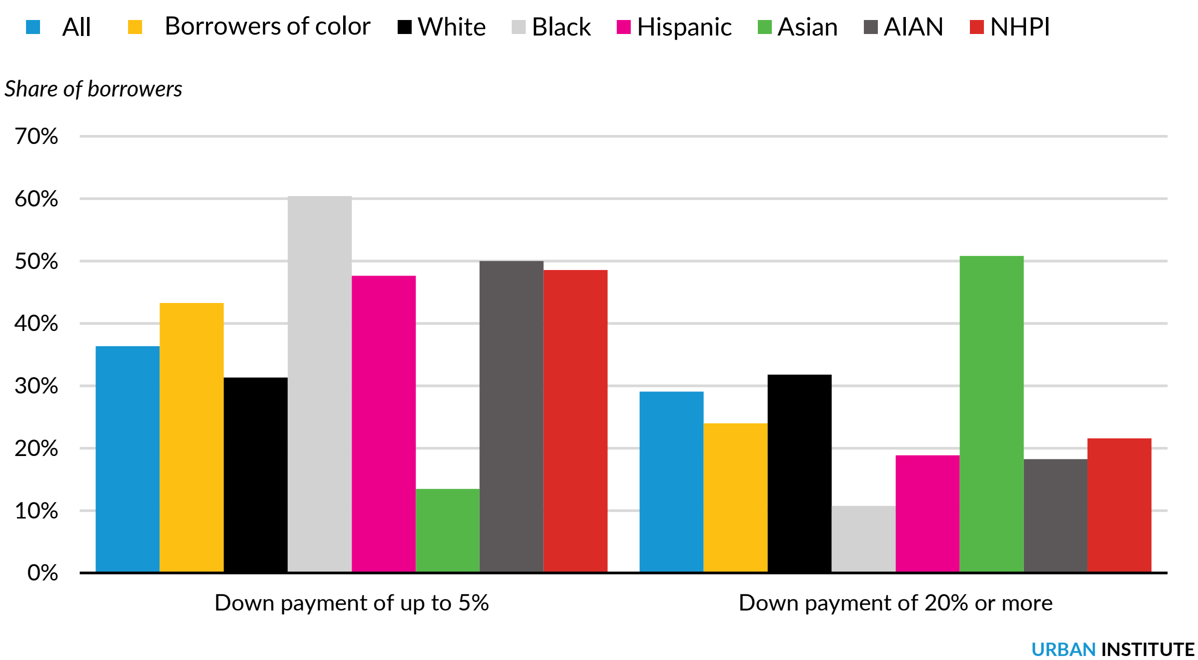


Source: Urban Institute calculations using 1999–2015 Panel Study of Income Dynamics data for ages 18 to 34.

With limited wealth, many mortgage borrowers of color can put down only a small amount of money when they purchase their homes, which lowers their home equity and increases their monthly payments. For example, only 11 percent of Black borrowers put down at least 20 percent on their home, compared with 32 percent of white borrowers (figure 8). Without family support, Black and Hispanic borrowers are more likely to rely on down payment assistance programs (figure 9).

FIGURE 8

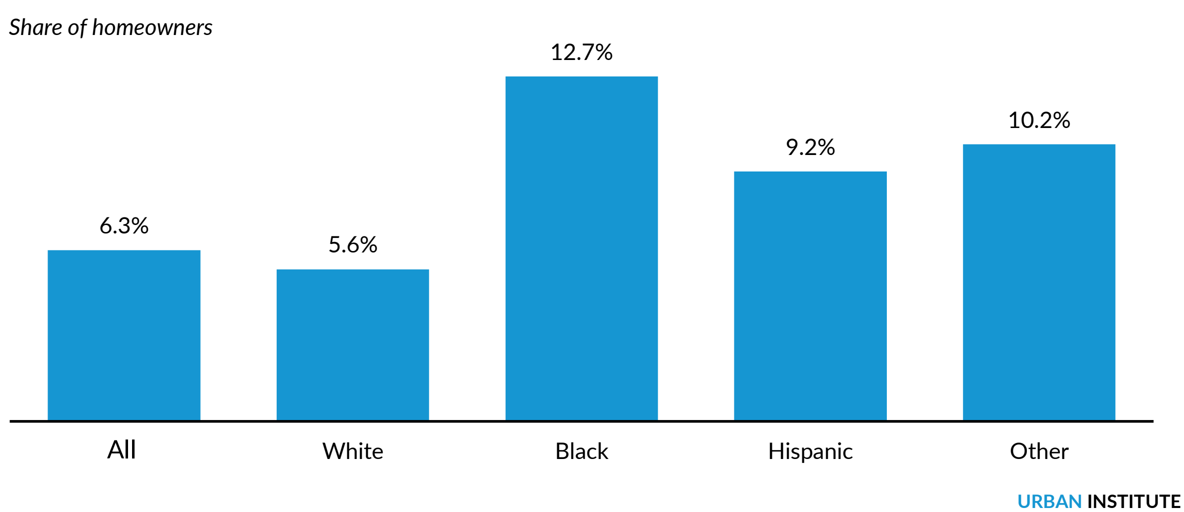
Share of Purchase Loan Borrowers, by Down Payment and Race or Ethnicity



Source: 2018–22 Home Mortgage Disclosure Act data.
Notes: AIAN = American Indian or Alaska Native; NHPI = Native Hawaiian or other Pacific Islander. Down payment shares are calculated by taking the share of borrowers with loan-to-value ratios below 80 percent for at least 20 percent down and loan-to-value ratios above 95 percent for 5 percent down or less. Data include purchase loans only.

FIGURE 9

Share of Homebuyers Using Down Payment Assistance



Source: 2020 National Survey of Mortgage Originations.

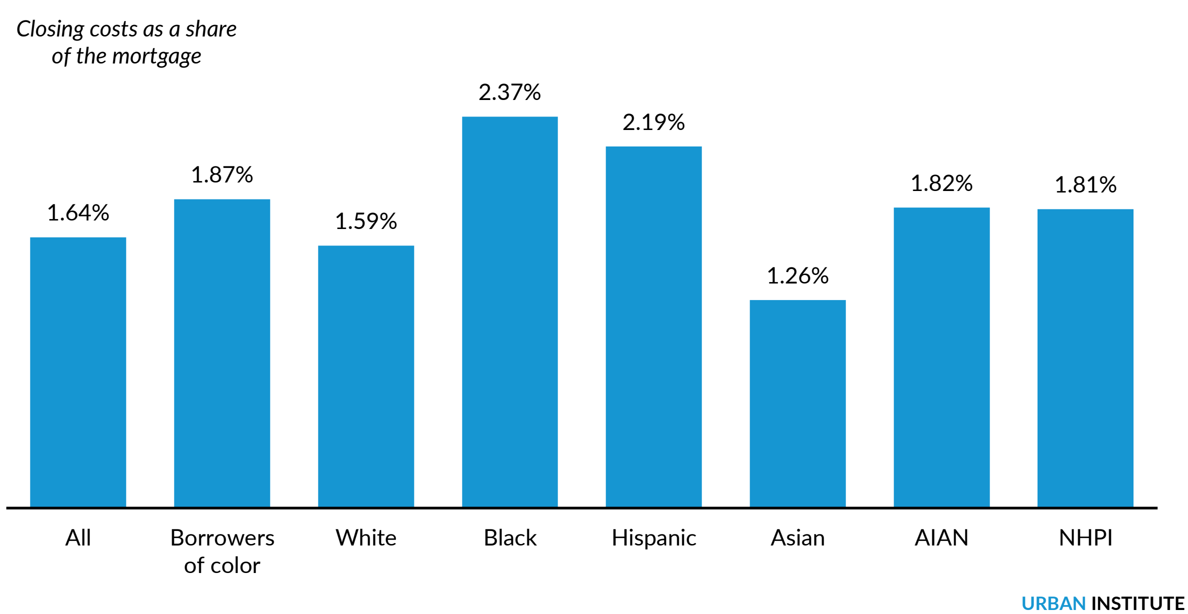
Even when they become homeowners, households of color often do not reap the same wealth-building benefits as white households. Evidence shows that homes owned by households of color and homes located in majority-nonwhite communities are systematically undervalued by appraisers (by $48,000 per home, on average), and these homes are susceptible to larger valuation errors even in automated valuations (Neal et al. 2020; Perry, Rothwell, and Harshbarger 2018). In 2019, households of color accounted for 32 percent of all households but held only 24 percent of primary-residence housing assets (Neal et al. 2021).[12]

Closing Costs

Up-front costs needed at closing can also be a burden to households with low incomes and wealth. Borrowers of color pay a greater share of their mortgage on closing costs, which tend to be regressive (figure 10).

FIGURE 10

Median Closing Costs as a Share of the Mortgage, by Race or Ethnicity



Source: 2018–22 Home Mortgage Disclosure Act aggregated one-year data.
Note: AIAN = American Indian or Alaska Native; NHPI = Native Hawaiian or other Pacific Islander.

Ultimately, products and programs that reduce the up-front payments needed for a mortgage will particularly support households who were historically excluded from homeownership and wealth building. Down payment and closing cost assistance in particular can help level the playing field.

Capacity: The Case for Products and Programs That Close Income Disparities

To obtain a mortgage, borrowers must generally not exceed a set ratio of debt payments (including the proposed mortgage payment) to income. These requirements present greater barriers to households of color.

In addition to wealth gaps, households of color have faced persistent income disparities and suppressed income growth compared with white households for decades, a product of occupational segregation, opposition to unions, and lack of antidiscrimination enforcement.[13] At the same time, borrowers of color often pay more for mortgage financing through higher interest rates (figure 12), producing two barriers to homeownership only worsened by a third: rising home prices as a share of wages, especially among entry-level homes.

These three factors—debt-to-income (DTI) ratios, high costs of borrowing, and the rising costs of entry-level homes—have made affording monthly mortgage payments more difficult, particularly for households of color. This is illustrated by looking at the gaps among households who do succeed in qualifying for a mortgage in figure 11.

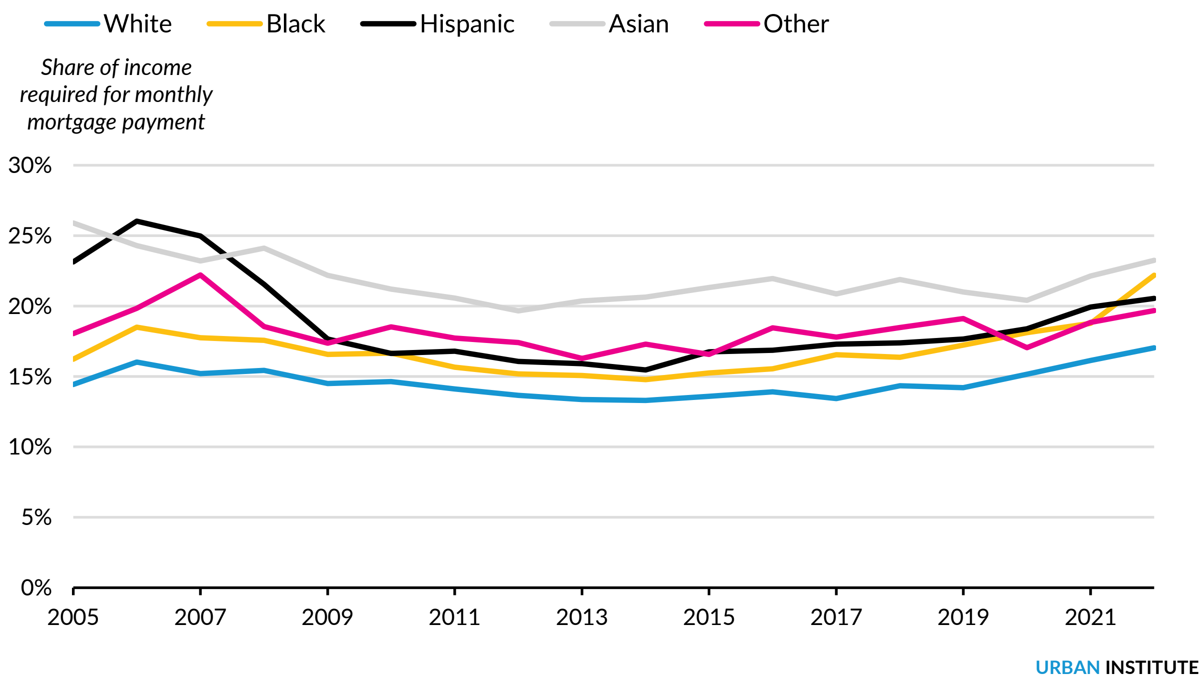
Mortgage affordability is calculated by determining the proportion of the median household income required to cover the median monthly mortgage payment. The monthly payment is based on median home values, segmented by race or ethnicity, and incorporates the average Primary Mortgage Market Survey rate as the interest rate, assuming a 20 percent down payment.

Mortgage affordability, therefore, differs by household income and changes with the shifts in home prices and interest rates. The recent increase in interest rates has worsened mortgage affordability for all households. We assume all households put 20 percent down and pay the same interest rate to show how shifts in home prices and interest rates relative to income affect mortgage affordability. But the differences in down payment and interest rates further worsen mortgage affordability for households of color. Except for Asian households, households of color have a substantially lower share of those who put 20 percent down (figure 8), which also increases the mortgage payment relative to income.

Affordability

FIGURE 11

Mortgage Affordability, by Race or Ethnicity, 2005–22

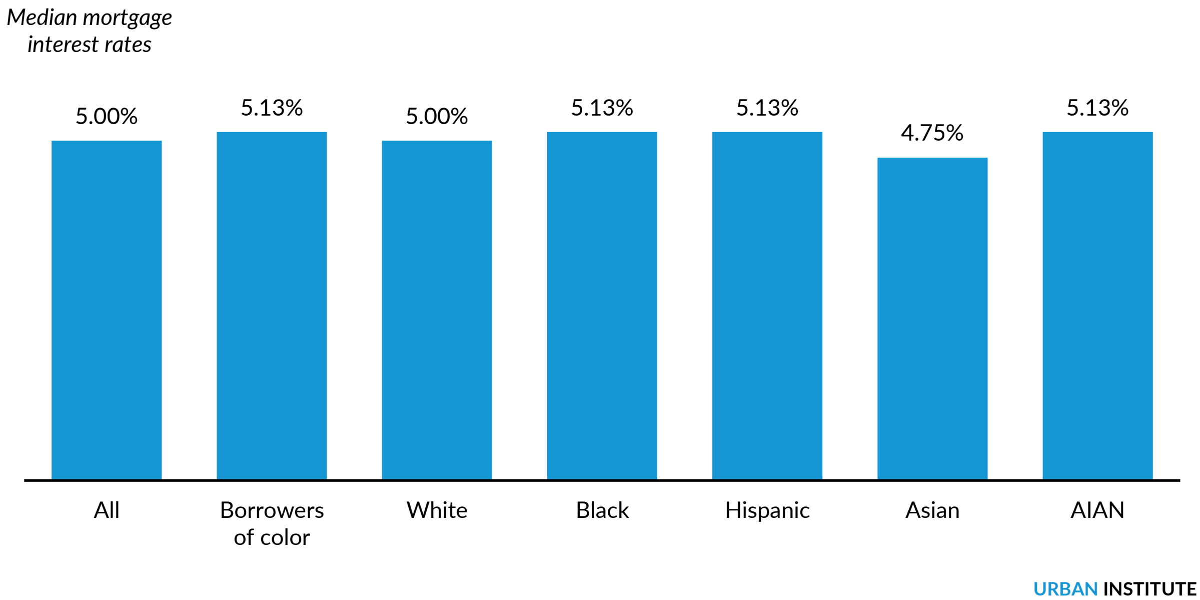


Sources: 2005–22 American Community Survey one-year data and the Freddie Mac Primary Mortgage Market Survey.
Notes: A higher percentage indicates lower affordability. The chart shows national-level mortgage affordability. Asian households face the lowest affordability levels. This is mainly because of the high concentration of Asian households residing in expensive markets, such as California.

In part because of loan-level pricing adjustments (or risk-based pricing), which adds a premium to a borrower's interest rate to account for higher loan-to-value ratios and lower credit scores, Black, Hispanic, and AIAN mortgage borrowers pay higher interest rates than white borrowers do (figure 12). Higher interest rates further worsen mortgage affordability for households of color.

FIGURE 12

Median Mortgage Interest Rates, by Race or Ethnicity



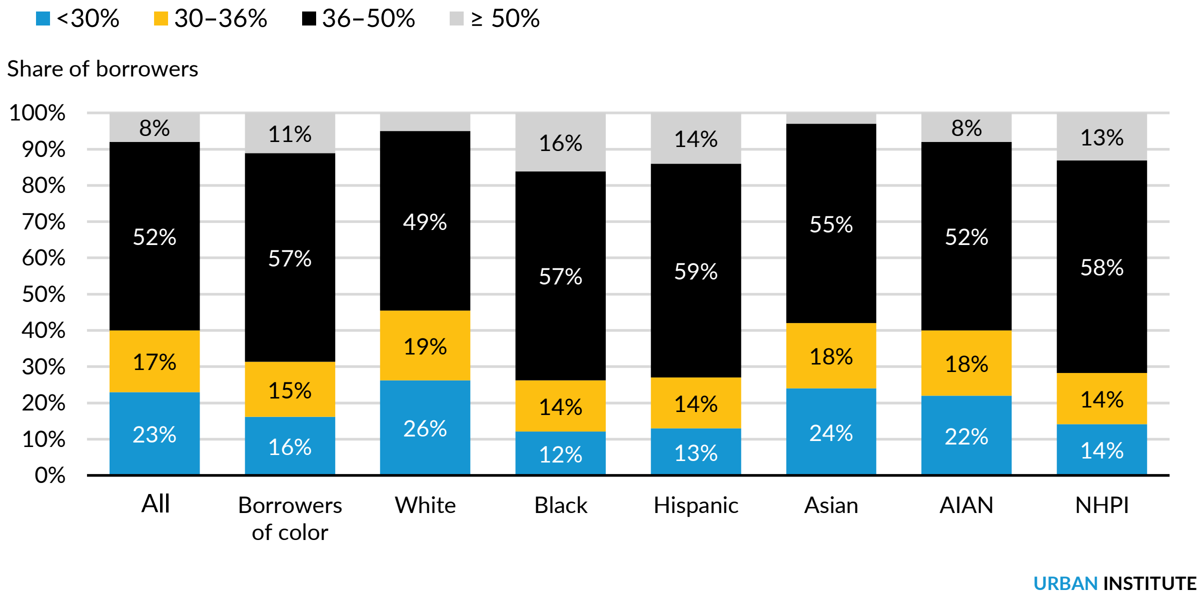
Source: 2022 Home Mortgage Disclosure Act one-year data.
Note: AIAN = American Indian or Alaska Native.

Debt-to-Income Ratio

Lower incomes also yield higher DTI ratios, which translate into a greater likelihood of credit denial (illustrated in figure 13 among households who succeed in getting into homeownership with mortgages). High DTI ratios are the most common reason for the denial of a mortgage application for all households between 2018 and 2022.

FIGURE 13

Debt-to-Income Ratios, by Race or Ethnicity



Source: 2018–22 Home Mortgage Disclosure Act aggregated one-year data.
Note: AIAN = American Indian or Alaska Native; NHPI = Native Hawaiian or Pacific Islander.

Products and programs that help borrowers overcome DTI barriers and ease affordability burdens will enable households of color in particular to access and sustain homeownership.

Credit: The Case for Products and Programs That Close Credit Disparities

Applicants must generally meet minimum credit score requirements to qualify for a mortgage. These scores are based on one's history of borrowing from mainstream credit. But because of government-sponsored redlining, households of color in segregated neighborhoods had less access to mainstream financial services—such as 30-year mortgages, revolving credit, and Federal Deposit Insurance Corporation–backed bank accounts—that underpinned the growing middle class. In their absence, costlier, riskier, and less-regulated alternative financing filled the void. For example, absent conventional financing, Black homebuyers in the 1950s and 1960s were disproportionately subject to risky home contract sales, in which borrowers accumulated no equity in their homes until they had paid it off and paid high interest rates, but they lost their entire investment if they missed a payment (Brown, Montes, and Hassani 2019; George et al. 2019).

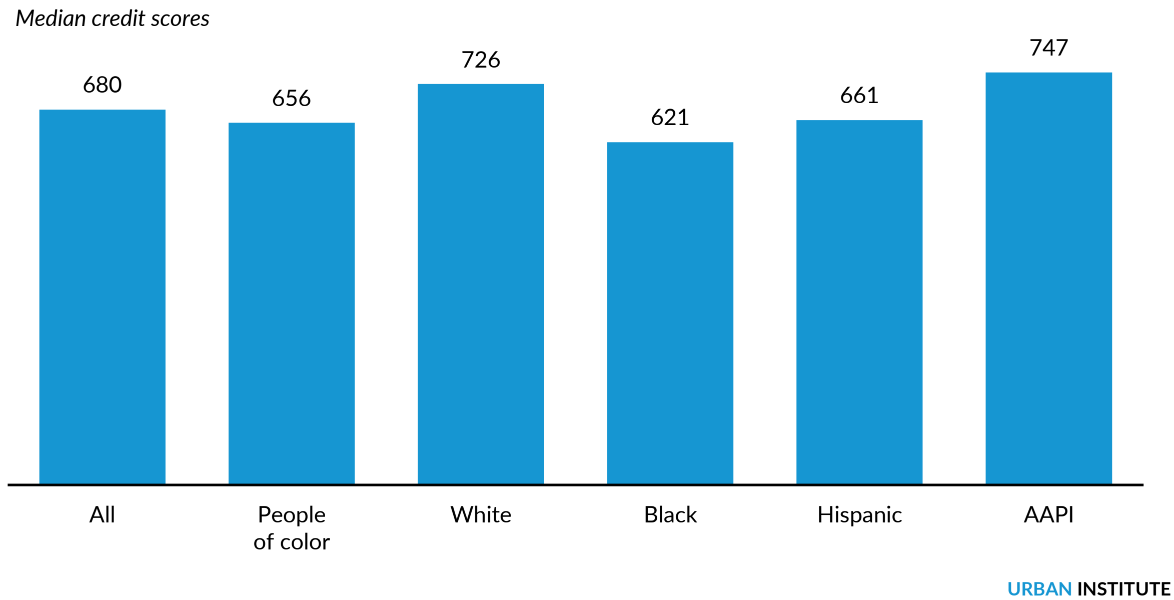
Even after the 1968 Fair Housing Act outlawed housing discrimination, neighborhood segregation persists, and households of color remain in a disparate financial environment.[14] Today, nearly a quarter of Black, Hispanic, and AIAN households are underbanked or use nonbank financial services, which are less protected and make it more difficult to build credit, compared with 9.3 percent of white households (FDIC 2022; Zinn et al. 2023).

Ultimately, the factors considered in credit scoring—including payment history, amounts owed, length of credit history, and types of credit used—cannot be separated from the environment in which borrowers access financial services. Borrowers of color, particularly Black and Hispanic borrowers, have been disproportionately targeted for subprime loans and are more likely to receive financing from smaller, fringe institutions that are less likely to report positive credit data to credit bureaus. As a result, traditional credit scoring models in a segregated financial ecosystem yield disparities in assessed creditworthiness, a key component in qualifying for mortgage financing (Rice and Swesnik 2012).

Figures 14 and 15 illustrate the median credit scores for all households and specifically for mortgage borrowers. Notably, mortgage borrowers typically exhibit higher credit scores. Interestingly, there are narrower gaps among mortgage borrowers. This suggests that a considerable number of households of color with lower credit scores may be either facing mortgage denial or opting not to apply for mortgages altogether.

FIGURE 14

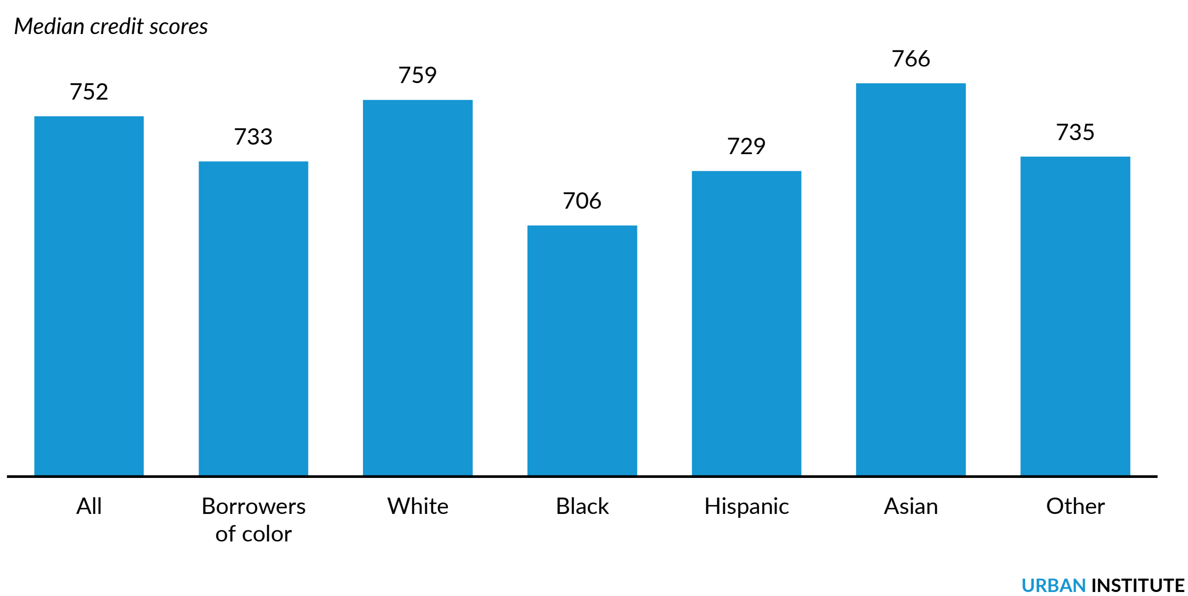
Median Individual Credit Scores, by Race or Ethnicity



Source: Urban Institute Financial Health and Wealth Dashboard calculations using 2021 credit bureau data, 2018 Survey of Income and Program Participation data, and 2019 American Community Survey one-year data.
Note: AAPI = Asian American or Pacific Islander.

FIGURE 15

Median Household Credit Scores among Purchase Loan Borrowers, by Race or Ethnicity



Source: Urban Institute calculations using 2022 Home Mortgage Disclosure Act–Black Knight McDash merged data.

Products and programs that mitigate systemic credit disparities will enable households of color in particular to access and sustain homeownership. For example, incorporating alternative data, such as rental payment history, into credit scores or evaluating rental payment data separately in the mortgage underwriting process through cash-flow underwriting could help qualify more otherwise creditworthy households for mortgage credit.[15] Cash-flow underwriting could be combined with SPCPs to further enhance access to credit and lower the cost of credit among those with no or low credit scores.

Conclusion

Because of intentional government policies and industry practices, racial and ethnic disparities in access to credit persist today. Homeownership gaps between white households and households of all other racial and ethnic groups are just as wide, if not wider, than they were when racial segregation was permitted under law. These disparities persist regardless of educational attainment or income level. Ultimately, a robust, targeted credit access program is needed to address these inequities in the same way credit was allotted on favorable terms to white households during the New Deal.

Special purpose credit programs fit the bill. In this report, we illustrate the key disparities in access to credit along the three criteria to qualify for a mortgage (i.e., collateral, capacity, and credit) to demonstrate the significant need for SPCPs. Because of persistent wealth gaps, households of color are less able to afford the down payment and closing costs needed to buy a home or to secure collateral. Similarly, demonstrating sufficient capacity to sustain monthly payments is also more difficult for households of color because of systemic differences in income and thus higher DTI ratios. And traditional models to assess creditworthiness tend to disadvantage households of color, who have lower credit scores, on average, than white households.

Ultimately, SPCPs that offer credit on more favorable terms (e.g., by lowering down payment requirements or offering more flexible underwriting requirements) to borrowers from groups who have been historically disadvantaged in our housing finance system are crucial to closing racial and ethnic homeownership gaps.

Notes

[1] The Consumer Financial Protection Bureau issued guidance documents for SPCPs. The bureau issued an advisory opinion in January 2021 outlining the content of a written plan that must be included in a for-profit organization that establishes and manages an SPCP under the Equal Credit Opportunity Act and Regulation B. In this case, lenders, under the Equal Credit Opportunity Act, need to establish and administer in accordance with a written plan that outlines the class of persons to whom it is intended to extend credit in accordance with the procedures and standards applicable to the program. For more information see Equal Credit Opportunity (Regulation B): Special Purpose Credit Programs, 86 Fed. Reg. 3762 (Jan. 15, 2021).

[2] Margery Austin Turner and Solomon Greene, "Causes and Consequences of Separate and Unequal Neighborhoods," Urban Institute, accessed February 20, 2024, https://www.urban.org/racial-equity-analytics-lab/structural-racism-explainer-collection/causes-and-consequences-separate-and-unequal-neighborhoods.

[3] Liam Dillon and Ben Poston, "The Racist History of America's Interstate Highway Boom," *Los Angeles Times*, November 11, 2021, https://www.latimes.com/homeless-housing/story/2021-11-11/the-racist-history-of-americas-interstate-highway-boom; and Yuliya Parshina-Kottas, Anjali Singhvi, Audra D S Burch, Troy Griggs, and Mika Gröndahl, "What the Tulsa Race Massacre Destroyed," *New York Times*, May 24, 2021, https://www.nytimes.com/interactive/2021/05/24/us/tulsa-race-massacre.html.

[4] See also "Foreclosures by Race and Ethnicity: The Demographics of a Crisis," Center for Responsible Lending, June 18, 2010, https://www.responsiblelending.org/research-publication/foreclosures-race-and-ethnicity-demographics-crisis.

[5] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies Issue Final Rule to Strengthen and Modernize Community Reinvestment Act Regulations," press release, October 24, 2023, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231024a.htm.

[6] John Walsh and Jung Hyun Choi, "Rising Interest Rates Put the Brakes on the Mortgage Market for Borrowers with Low Incomes," *Urban Wire* (blog), Urban Institute, August 24, 2023, https://www.urban.org/urban-wire/rising-interest-rates-put-brakes-mortgage-market-borrowers-low-incomes.

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