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Predatory Lending Practices and Foreclosures in Communities of Color

Between 2007 and 2009, the United States experienced one of the most devastating economic crises, known as the Great Recession of 2008, due to the collapse of the housing market. This economic crisis depleted the wealth of many Americans. Communities of color, in particular, experienced the brunt of the crisis. For years, real estate agents and banks disproportionately targeted black and Latino families with predatory lending practices. These families were offered subprime mortgages for their new homes. When the real estate market crashed, many of color families could no longer afford their mortgage and lost their homes to foreclosures. Now after the Great Recession, people of color have less wealth than they did before the recession. Predatory lending practices, a major contributor to the growing wealth inequality in the United States, is part of a long history of unjust targeting of people of color in the housing market.

WEALTH AND HOMEOWNERSHIP

Wealth is essential for the economic security of American families. It constitutes the long-term savings and investments of households. Wealth is measured by two important criteria: assets and debt. Assets are everything a household owns such as homes, cars, money in savings accounts, and investments in stocks and mutual funds. Debt is everything a household owes such as credit card debt, taxes, loans, and mortgages. A household's wealth is *the leftover amount* when the total debt amount in dollars is subtracted from the total asset amount in dollars. Families save this leftover amount for unexpected expenses and emergencies, for the education costs of the next generation, and potentially for retirement. Wealth is different from regular wages and salary.

Luis Garcia, a 75-year-old senior from Peru, who has limited understanding of English, at his home in San Bernardino, California, 2008. Garcia, a victim of the predatory lending company Lifetime Financial, discovered that Lifetime Financial had falsified almost all of his information, including his monthly income and work history. (AP Photo)

While wages and salary are used for everyday costs in the short term, wealth is reserved for the long term.

For the majority of American families, homeownership is one of their most important assets. In 2007, homeownership made up 33 percent of the total wealth portfolio of households (Wolff 2011). This number includes households across economic and racial backgrounds. When looking specifically at black families, however, housing wealth makes up closer to 63 percent of their portfolio. With housing being so important for families of color, those who do not own a home can then miss out on an important asset for building wealth. In addition to increase in wealth, homeownership can also bring other long-term benefits. Many families live in their purchased home for decades allowing children to grow up in stable environments. The value of the home can be used as collateral for loans from banks to open a business or pay for college tuition. Families can also pass down homes to their children or grandchildren. As can be seen, wealth can help families maintain economic security and help preserve advantages for generations to come.

WEALTH INEQUALITY AND THE GREAT RECESSION

Wealth is also an important factor that contributes to the racial inequality in the United States. Over the past three decades, there has been persistent and growing wealth inequality between whites and people of color (McKernan et al. 2013). The Great Recession of 2008 exacerbated the wealth–race gap in the United States.

In 2007, the U.S. housing market crashed causing many American families to lose portions of their wealth. Twenty-five percent of households lost the majority of their wealth and an additional 50 percent of households lost a quarter of their wealth (Pfeffer, Danziger, and Schoeni 2013). These households tended to be families of color. In fact, families of color experienced the greatest loss from the housing market crash and the resulting 2008 recession. Recent statistics released by the Pew Research Center show that the median wealth of Hispanic and black households dropped by more than half during the Great Recession (Kochhar 2011). In 2005, the median wealth of black households was $12,124 and in 2007, it was $5,677. For Hispanic households, the median wealth in 2005 was $18,359 and in 2007, it was $6,325. In comparison, the median wealth of white households declined by 16 percent during the same time. In 2005, the median wealth of white households was $134,992 and in 2007, it was $113,149. The deleterious impact of the economic crisis left 30 percent of black and Latino households in debt or with zero wealth. Without the reserve of wealth to fall back on, these families of color may struggle to survive financially and to help the next generation.

PREDATORY LENDING AND THE FORECLOSURE CRISIS

Why were families of color disproportionately impacted by the 2008 economic crisis? While the answer is multifaceted, much of the recession-related decline in wealth had to do with home equity (McKernan et al. 2013). In the years leading up to the Great Recession, bank agents targeted black and Latino families with predatory lending by offering more risky housing loans, known as subprime loans. Once the housing market collapsed, families of color with subprime housing loans could no longer afford their homes. Many families lost their homes to foreclosures resulting in widespread loss in housing wealth.

Multiple studies have shown that blacks and Latinos were disproportionately steered toward subprime loans compared to whites with similar economic backgrounds (Leigh and Huff 2007; Rugh and Massey 2010). The Joint Center for Political and Economic Studies found that 52.9 percent of blacks and 47.3 percent of Hispanics had subprime loans compared to 26.1 percent of whites during the recession (Leigh and Huff 2007). In fact, the unfair treatment of blacks and Hispanics by banks was commonly known. After the recession, a 2009 *New York Times* article exposed that many bank agents received monetary incentives to push subprime loans onto blacks (Powell 2009). The article cited Eric Halperin, the director of the Center for Responsible Lending: "We've known that African-Americans and Latinos are getting subprime loans while whites of the same credit profile are getting the lower-cost loans" (Powell 2009). The greater targeting of blacks and Latinos made owning a home disproportionately more risky for these groups. This practice also exposed black and Latino neighborhoods and low-income neighborhoods to more harm by increasing instability in homeownership. It is important to note that the targeted use of subprime loans is part of a long history of discriminatory practices that prevents communities of color from fully benefiting from the advantages of homeownership and wealth accumulation.

Unlike lower-cost loans, subprime mortgage loans have higher interest rates and are more likely to be unstable. Banks offer housing loans (mortgages) to individuals to help pay for a house. A prime mortgage loan has a low interest rate that is fixed over a long-term period (usually 30 years). Families can take that period of time to pay off their house through monthly mortgage payments. During that time, their low interest rate will not increase. In contrast, subprime mortgage loans have higher interest rates that may not be fixed. Some subprime mortgage loans can start at a higher interest rate compared to the interest rate of traditionally low-fixed prime loans. Other subprime loans can start with an introductory rate that is small but can jump in percentage points after the introductory period is over. The overall higher interest rate of subprime mortgage loans can increase monthly mortgage payments by hundreds of dollars. Over the life of a subprime loan, a borrower can pay as much as $100,000 extra in interest.

With the burst of the housing market, many homeowners with subprime loans defaulted on their mortgage payments due to escalating interest on their loans. They could no longer afford to pay the higher monthly mortgage payments. In addition, housing values depreciated in lower income neighborhoods resulting in high levels of foreclosures in those neighborhoods. To demonstrate, in 2005, a family buys a home valued at $150,000 in a low-income neighborhood. In 2007, because the housing market declined, the same house is now valued at $90,000. However, the family still owes the bank $150,000 in principal plus thousands of dollars in interest due to the subprime loan. By the time the family pays back the subprime mortgage loan with the high interest rate, they will have paid many times over the $90,000 amount. Even if the family sells the house for $90,000, they would still owe the bank the remaining $60,000 as part of their loan plus the growing interest amount. With no other choice, many families defaulted on their subprime loans and lost their homes to foreclosure. Foreclosure occurs when a bank repossesses a home from the owner, who cannot afford to pay the monthly mortgage payments. It has been estimated that foreclosures are 8 to 10 times more likely to occur in subprime markets than in prime markets (Leigh and Huff 2007).

During the recession, families of color were two times more likely to lose their home to foreclosure than white families (Shapiro Meschede, and Osoro 2013).

The reduction in home values and high interest rates on loans pushed many families of color into foreclosure and debt. Latinos sustained the greatest loss in home values due to the sharp decline in housing values during the recession. They lost 50 percent in housing values (McKernan et al. 2013). Many Latino families were younger and had just purchased property before the recession. Blacks lost 25 percent in housing values but also lost retirement assets by 35 percent (McKernan et al. 2013). Black families facing hard times due to the recession withdrew money from retirement funds to help with living costs. White families, while also losing 25 percent of their housing wealth, were able to sustain through the recession because they were less likely to have subprime loans. Their monthly mortgage payments were lower due to the low interest rates. As a result, they were less likely to take money out from retirement assets. After the recession, the U.S. stock market bounced back and whites saw an increase in their retirement assets (McKernan et al. 2013).

The impact of the subprime loans and the foreclosure crisis extended beyond individual households. As more and more homes foreclosed in lower income and of color neighborhoods, the values of the remaining homes declined even further causing more families to default and lose their homes. These patterns led to higher levels of foreclosures in minority communities (Immergluck 2011). The large number of foreclosures in concentrated areas can cause instability in communities. Fewer businesses are willing to open up in neighborhoods with boarded up and foreclosed homes. The lower proportions of homeowners in a neighborhood can also impact the quality of schools. Homeowners pay property taxes that help fund local public schools. In addition, with zero to very little housing wealth, families of color cannot transfer wealth to their children to cover tuition for a college education. Community members are also less likely to invest in the local community through businesses, neighborhood watch, and local councils if they are not homeowners. Ultimately, "Hispanic and black neighborhoods bore the brunt of the foreclosure crisis" (Rugh and Massey 2010, 645).

CONCLUSION

Predatory lending practices such as subprime loans targeted at black and Latino communities disproportionately expose them to harm as they try to secure economic security. Families of color lost higher portions of their housing wealth compared to their white counterparts. One statistic places the cumulative wealth loss for people of color due to subprime loans in the billions of dollars (Oliver and Shapiro 2008). Now in the postrecession era, black and Latino families are further behind than they were before the recession. The impact of such discriminatory practices is widespread and has consequences for years to come. This is because wealth is related to many important life outcomes including ones for the next generation. With significant losses in wealth among communities of color, there is less to pass on to children and grandchildren. Middle-class black parents struggle to secure middle-class status for their children (Shapiro 2004). In contrast, white families are more likely to pass on their wealth to the next generation giving their children a head start compared to children of color. In addition, this unjust and unequal predatory practice exacerbated wealth inequality between people of color and whites. The wealth divide between whites and blacks and whites and Latinos is wider now than it has ever been.

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See also: Affordable Housing; The Federal Housing Administration; Wealth Inequality: Perpetuation and Persistence; Perspectives and Debate Section: What Can Be Done about the Wealth Gap for People of Color?

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