HMDA

Home Mortgage Disclosure Act

New Pricing Data

In fall 2005, the Board of Governors of the Federal Reserve System published its first study of the new Home Mortgage Disclosure Act (HMDA) interest-rate data. The study included extensive national analyses of mortgage pricing patterns across racial and ethnic groups. The findings confirmed a commonly held belief about mortgage prices: Traditionally underserved minority groups were more likely than other populations to pay higher prices for mortgages. In general, the findings hold for New England.

The Subprime Market

Since the 1990s, the strong, rapid growth of subprime lending has dramatically changed the mortgage lending industry. Using risk-based pricing, lenders look at the characteristics of a potential borrower, estimate the chance of early termination of the loan (either through default or prepayment), and determine how to price the loan. To offset higher risks, lenders charge higher interest rates, fees, or both. With the flexibility of subprime lending, the industry can offer a wide variety of mortgage products to a wide range of households.

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Many people believe the growth of the subprime market played a role in increasing access to credit for traditionally underserved populations. However, there is concern that these populations are more likely than others to be overcharged for credit. Subprime borrowers may be charged unreasonably high interest rates or fees. Also, applicants who qualify for prime, less expensive mortgage products may be steered to subprime products or subprime specialty lenders. It is generally believed that those patterns disproportionately affect minorities.

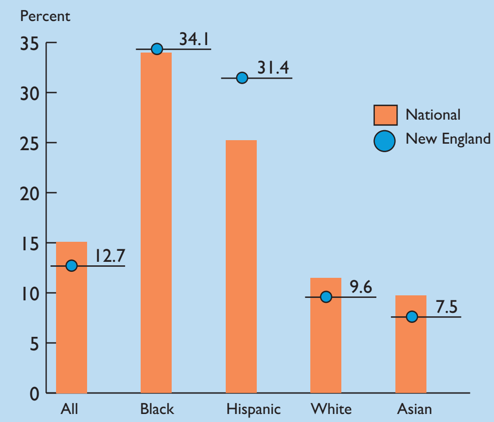
In evaluating overall access to credit, researchers and regulators have focused on denial rates. Historically, blacks have had much higher mortgage-denial rates than whites, and rates for Hispanics were somewhere in between. But as the subprime mortgage market grew, it became clear that this information was not enough. There was no information to show the price of loans, and there was concern that if there were discriminatory pricing practices, they were not being brought to light. By 1993, the Department of Housing and Urban Development (HUD) began compiling a list of lenders who specialized in subprime lending. Although the list showed that minority groups were more and more likely to receive loans from subprime specialty lenders, it did not necessarily show whether these groups were more likely to receive subprime loans. Furthermore, there were no data showing whether or not pricing differences existed across racial and ethnic groups.

In 2002, HMDA was amended so that data on pricing would start being collected in 2004. However, collection of the pricing data is not straightforward. The interest rate charged for each loan is compared with the yield on a comparable treasury security. If the spread exceeds a certain threshold, the lender must record the size of the spread in the HMDA data. The threshold depends on the type of lien on the loan. For loans with primary or first liens, the threshold is three points. For loans with junior or subordinate liens, the threshold is five points. These loans are often referred to as "higher-priced" or "high-cost."

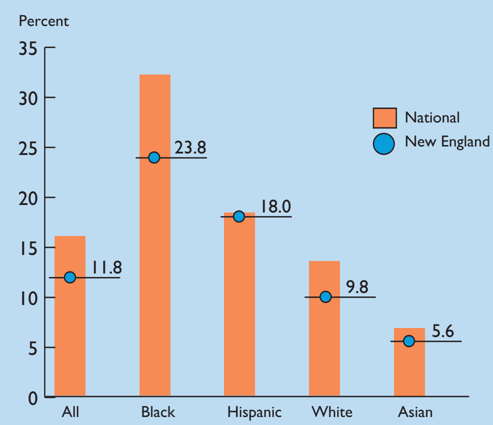
What We Have Learned So Far

The first analyses of the completed data set were published in September 2005 by Federal Reserve Board researchers. "New Information Reported under HMDA and Its Application in Fair Lending Enforcement" examined higher-priced loan originations (loan approvals) and the patterns across income, race and ethnicity, and gender.[1] The differences in patterns across racial and ethnic groups were significant—it was clear that most minority groups were much more likely to get higher-priced loans than whites.

Share of Home-Purchase Loans That Were Higher-Priced



Share of Refianance Loans That Were Higher-Priced



Source: Author's tabulations of 2004 Home Mortgage Disclosure Act Data. Note: Excludes transition period records.

A much higher share of mortgages were higher-priced for blacks and Hispanics than for non-Hispanic whites or Asians. (See the exhibit "Share of Home-Purchase Loans That Were Higher-Priced.") The patterns held for home purchases, refinancing, and home improvement. Generally, non-Hispanic whites and Asians had the lowest likelihood of higher-priced loans, whereas African Americans had the highest. Rates for Hispanic whites were somewhere in between.

The findings matched most expectations. However, one pricing pattern did not. For the actual cost of the higher-priced loans, there was almost no difference across racial or ethnic groups. For some loan products, whites paid slightly more than minorities.

One significant finding of the Board of Governors report was that much racial and ethnic disparity in higher-priced lending stemmed from the choice of lending institution. Blacks and, to a lesser extent, Hispanics were much more likely than whites to apply to institutions that typically originated higher-priced mortgages to applicants of all races and ethnicities.

There are many possible causes for the wide variations in lender-choice patterns. The Board of Governors paper describes a few. Applicants may believe they need a subprime loan (because of a low credit score, for example, or a small down payment) and select a lender with that specialty. It is also possible that subprime lenders have stronger outreach in minority communities than other lenders—or that minorities are steered by friends, brokers, or institutions to subprime lenders, whether or not they qualify for prime credit.

How Did New England Compare?

Overall, higher-priced lending was less common in New England than in other parts of the country. However, for patterns across races and ethnicity, results differed sharply depending on whether the loan was for home purchase or refinance.

For home purchase loans, Hispanics were much more likely to received a higher-priced loan in New England than in any other region. The proportion of loans to blacks that were higher-priced in New England was similar to the national average. In fact, higher-priced loans were almost equally common for New England's Hispanics and blacks, which differed from the rest of the nation. For whites, higher-priced loans were less common than they were in all but one other region. Combined, this made for some of the greatest disparities in the country. The pattern was consistent across most of New England's metropolitan statistical areas.

The patterns for refinance loans in New England were a marked contrast. (See the exhibit "Share of Refinance Loans That Were Higher-Priced.") All of New England's groups were among the least likely in the country to receive higher-priced refinance loans.

Much of New England's differences across racial and ethnic groups stemmed from applicants' choice of lenders.

As in the rest of the country, much of New England's differences across racial and ethnic groups stemmed from applicants' choice of lenders. The most popular lenders among many minority groups (as measured by the number of applications received from each minority group) were often lenders that were very likely to make higher-priced loans—to applicants from any racial or ethnic group.

For example, in New England, 31 percent of home purchase loans to Hispanics were higher-priced loans. This share was 47 percent at the five lenders who received the largest numbers of applications from Hispanics. (Each received more than 1,200 applications from Hispanics, and, combined, the five lenders received 30 percent of all Hispanic home-purchase applications). At these same five lenders, whites also had an unusually high likelihood of getting a higher-priced origination. Twenty-nine percent of loans to whites were higher-priced loans (compared with only 10 percent on average).

In contrast, at the five most popular lenders for whites, only 19 percent of loans to Hispanics were higher-priced. Whites at these lenders were still less likely than Hispanics to receive higher-priced loans—only 9 percent of loans—but the gap was only 10 percentage points and was significantly smaller than the 19 percentage-point gap at the five top institutions among Hispanics.

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Endnote

[1]Robert B. Avery, Glenn B. Canner, and Robert E. Cook, "New Information Reported under HMDA and Its Application in Fair Lending Enforcement," *Federal Reserve Bulletin* (summer 2005): 344-394, www.federalreserve.gov/pubs/bulletin/2005/3-05hmda.pdf.