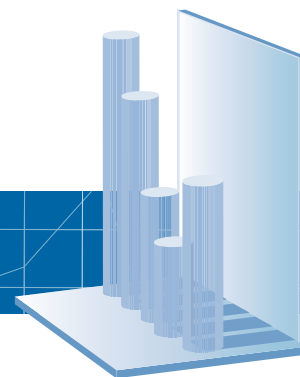




# RESEARCH IN FOCUS

SUPPORTING SCHOLARSHIP IN HOUSING  
AND COMMUNITY DEVELOPMENT



VOLUME 2/ISSUE 1

## Subprime Foreclosures Spotlight Concerns of Predatory Lending

**F**orty-one percent. That's how much home foreclosures increased during the first quarter of 2007 as compared to the same period the year before. And the foreclosures, most of which occurred in the subprime mortgage market, are continuing to negatively impact a housing market already facing declining home prices and sales. This has caused mortgage markets to tighten underwriting criteria and capital markets to pull back from mortgage securities backed by subprime loans. It is also reshaping communities which are now dotted by abandoned properties undergoing foreclosure. Consumer groups are also expressing concern that many of the households facing foreclosure may have been targets of predatory lending.

Subprime lenders target consumers who do not qualify for conventional mortgages due to poor or limited credit histories. These loans carry higher interest rates and less favorable terms because of the higher risk associated with lender origination. Subprime mortgages often are adjustable rate mortgages (ARMs) or require balloon payments at maturity, while the majority of conventional mortgages are fixed-rate loans.

The rise of the subprime market during the 1990s put homeownership within reach of more Americans, often serving consumers located in low-income and minority communities. The growth was fueled by legislative changes allowing for a greater variety and availability of mortgage products and the development of a secondary market for nonconforming loans. Between 1998 and 2005, the subprime market grew from \$35 billion to \$665 billion. And in 2006 subprime loans accounted for 23 percent of all mortgage originations (Center for Responsible Lending, *Losing Ground: Foreclosures in the Subprime Market and Their Costs to Homeowners*, December 2006).

*Subprime Foreclosures continued on page 2*

## For Rutgers Student, DDRG is a Perfect Fit

**I**n 2004, Kristen Crossney was a second-year Ph.D. student at Rutgers University. She had previously completed a scholarly manuscript for the U.S. Department of Housing and Urban Development's (HUD's) Early Doctoral Student Research Grant (EDSRG) program and now wanted to dedicate a large amount of time to her dissertation. Funding was a priority for Crossney, and she soon realized that there were few funding sources that would allow her to focus her research efforts on her dissertation in the field of housing and community development.



*Kristen Crossney*

Then, in October 2005, while presenting her EDSRG at the Association of Collegiate Schools of Planning (ACSP) annual conference in Portland, Oregon, Crossney discovered that she had been awarded a 2-year HUD Doctoral Dissertation Research Grant (DDRG). She was elated.

"It seemed a perfect fit for my interest in housing finance and its relationships to neighborhoods," she says. "The program allowed me to focus on my research, and I was able to complete my dissertation in a timely manner." Her DDRG grant also supported travel to conduct research and to present that research at two scholarly conferences: the 2005 annual meeting of the ACSP and the 2006 annual meeting of the Urban Affairs Association. "If I did not have the support of the EDSRG and DDRG programs, I likely would have had to narrow or change the focus of my dissertation or push my graduation date back," says Crossney.

*For Rutgers Student continued on page 3*



But the rapid increase in the subprime market and the drastic increase of subprime delinquencies and foreclosures make some wonder: *at what costs?* The Center for Responsible Lending estimates that 2.2 million households that purchased loans on the subprime market between 1998 and 2006 will lose their homes to foreclosure. The foreclosures are having a ripple effect beyond the consumer. Home prices are falling further in communities in which foreclosure activity has been most active. Mortgage companies are folding or have stopped subprime lending programs. And foreclosures are causing liquidity to dry up in other capital markets amid investor concerns of too much risk taking.

Many factors are at play in the increased foreclosure activity. As mentioned earlier, subprime loans are most often ARMs. As loan rates are reset, consumers face higher interest rates on properties that have lost value during the market downturn, making refinancing or selling a home to repay a loan more difficult. Lack of diligent underwriting standards in recent years has also contributed to the increased foreclosure numbers with even the riskiest consumers receiving loans that required little or no downpayment.

Predatory or abusive lending practices may also be contributing to the increasing numbers of foreclosures. Subprime borrowers, who by definition have difficulty obtaining traditional home financing, may be at risk of deceptive loan practices especially if they do not fully understand their loan's terms and costs. Predatory practices may include:

- \* Loan flipping, which occurs when a mortgage originator refinances a borrower's loan repeatedly in a short period of time, often charging higher fees and stripping a borrower's equity.
- \* Excessive fees being charged and packed into the loan amount without the borrower understanding the costs.
- \* Lending without regard to a borrower's ability to repay.
- \* The use of deceptive sales tactics, which can result in consumers losing equity in their homes.

Two Office of University Partnership grantees have looked more closely at the relationship between predatory lending and the subprime lending market.

Both profiles lay the groundwork for future research on current events shaping the housing market. In *The Paradox of Predatory Lending: An Examination of Mortgage Lending in Philadelphia, Pennsylvania*, Doctoral Dissertation Research Grant (DDRG) recipient Kristen B. Crossney of Rutgers University examines the occurrence of predatory lending in Philadelphia, drawing on public mortgage and property data. The results of her research indicate that predatory lending could have the most devastating effects on those who have struggled the most to access the benefits of homeownership, and that predatory lending could be an unintended consequence of federal housing and mortgage policy. Subprime lenders were also most active in the census tracts containing predatory mortgages.



A study titled *Is Subprime Lending Leading to Reverse Redlining and Price Discrimination?* is research conducted by Early Doctoral Student Research Grant (EDSRG) recipient Abhishek Mangain from the University of Southern California. In spite of all the concerns regarding the reverse redlining in subprime markets, very little empirical work has been done to assess the existence and prevalence of this form of discriminatory practice. This study fills this gap in the literature and also investigates the presence of reverse redlining and price discrimination in the Los Angeles County region by evaluating a pool of Home Mortgage Disclosure Act microlevel data for 2004 in conjunction with the U.S. Department of Housing and Urban Development list of subprime lenders and 2000 Census data.







