



The Myth of the Risky Sub-Prime Borrower

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Money lending institutions have tarred entire segments of the population as credit unworthy through the mortgage industry's own discriminatory, irresponsible -- and now reckless -- behavior.

Every major paper is running some variation of the same major story: the sub-prime, "exotic" mortgage market is in trouble.

High priced mortgages that include funky gimmicks -- like adjustable rates or no verification of borrower income -- have resulted in record setting foreclosures and a rush by Wall Street to divest from the sub-prime market. Sub-prime loans comprise only 13% percent of outstanding mortgages, but they contribute to over 60% percent of foreclosures.

Some analysts suggest that sub-prime lenders are being punished for giving high-risk loans to borrowers in low- and moderate-income neighborhoods and communities of color, people, they say, who perhaps never should have received a loan in the first place. After all, their logic follows, not every American can handle the responsibility of credit and owning a home.

This is a convenient, yet misguided, conclusion to draw from the sub-prime mortgage debacle. In truth, sub-prime lending is just the latest example of how lenders have tarred entire segments of the population as credit unworthy through the mortgage industry's own discriminatory, irresponsible -- and now reckless -- behavior.

This recklessness begins with the way the sub-prime industry has built into it financial incentives that defer risk, and liability, along a long chain of sub-prime role players. This marks a sharp departure from the past, when loans were typically originated and held by a single bank that assumed any and all of the risk.

Now, actors in sub-prime lending treat these loans like they are radioactive hot potatoes, making a tidy profit with every hand-off. Take for example the mortgage brokers who legally receive kickbacks for hiking up the price of the mortgage; the lending institution which will most likely sell the poorly underwritten, garbage mortgage as soon as it touches its books (last year 80% of all predatory loans were sold on the secondary market); the secondary market which generates billions in fees and commissions by shuttling around these mortgages in Wall Street securitization deals. Throughout this process the guiding spirit is close the deal, damn the consequences.

Ironically, because savings and loans and commercial banks over generations systematically failed to address the credit needs of low and moderate income communities and communities of color -- despite the passage of the Community Reinvestment Act and fair lending laws -- mortgage companies and sub-prime bank affiliates swooped in and aggressively peddled sub-prime mortgages to areas starving for credit.

The term sub-prime is engendered with the belief that certain communities represent a lower order of customer species. As a result, sub-prime lenders justify their predatory pricing by claiming that African Americans and Latinos are higher credit risks. In other words, they deserve whatever horrific loans they get.

Not surprisingly, more than 50% of African-American and 40% of Latino mortgage borrowers have sub-prime loans. While of course many of these folks do in fact have poor credit histories, many of them, often targeted by hyper-aggressive marketing campaigns, would otherwise be eligible for low-cost, "prime" loans. A study by the Center for Responsible Lending documented that African Americans and Latinos get high-priced mortgages far more frequently than whites -- even when they are equally qualified for prime loans.

For proof of this, all one has to do is go to South Queens, where blacks have higher incomes than their white Queens counterparts, but pay more for credit and are losing their homes through foreclosure at epidemic rates. Or in Maryland's Prince George's County where the middle-class, majority black, residents have credit scores that on average are higher than the state average and national averages, but refinanced their homes in 2005 using high-cost loans at almost twice the rate as homeowners nationwide, according to a recent Washington Post article.

Sub-prime lending often works as self-fulfilling prophecy. The most efficient way to ruin a person's credit, and thus make him or her truly eligible for a sub-prime loan, is to make a loan unaffordable, or indiscriminately jack up the price of the loan after a few years, to a person who has a good credit history, but whose income is unlikely to rise along with the payments. For those of us involved in anti-predatory lending organizing and advocacy, we talk to people everyday who never missed a loan payment in their lives until they received a sub-prime mortgage.

The only way to avoid a new era of redlining is if banks take back the market they have ceded to the sub-prime players, using affordable loans designed and underwritten with the best interests of the borrower in mind, not the best interests of Wall Street investors. In doing so, these lenders will discover a deep market of responsible borrowers who are indeed deserving of the right loan, at the right price.

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