

Loan Performance Problems by Subprime Status and Community Poverty

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Research and Assessment
October 2008

Some commentators assert that Community Reinvestment Act (CRA) requirements, which require lenders to make loans in the places where they take deposits, drove many lenders to originate subprime loans to high-risk borrowers in low-income areas, thereby fueling the foreclosure crisis. Aside from the fact that many subprime lenders were not covered under CRA, there are at least two obvious problems with this argument.

1. For many years, lenders have made CRA-qualifying loans without substantial harm to their balance sheets. Analysis of the performance of all outstanding residential first-mortgages to both owner-occupants and investors shows that what counts is not where the loan is made, but the kind of loan it is.
 - In March of 2007, just prior to the acceleration of residential mortgage delinquencies and foreclosures, the delinquency rate for **prime** loans in low-poverty areas was 2.29 percent; in high poverty areas, 3.73 percent. This spread reflects the moderately higher risk of borrowers most likely to reside in high-poverty neighborhoods. (See Table 1.)
 - In March of 2007, the **subprime** delinquency rate in low-poverty neighborhoods was 16.82 percent, substantially the same as the subprime delinquency rate in high-poverty neighborhoods and more than 14.5 percentage points higher than the rate for prime loans.
 - A similar pattern holds for foreclosure rates and for the percentage of all mortgaged properties that wound up in the inventory of real-estate-owned properties. The difference in the rate of foreclosures on **prime** loans between low-poverty and high-poverty areas is a mere .5 percent. (This modest difference was probably priced in the loan itself.)
 - The overall pattern displayed in March 2007 had not changed at all by March 2008, when the foreclosure crisis was in full swing. (See Table 2.) Although delinquency, foreclosure, and REO property rates increased dramatically over the period, the relative performance of loans in the lowest-poverty versus the highest poverty areas did not change.

2. Although a disproportionate share of subprime loans were made in the highest poverty areas of the United States, nearly two-thirds of all these loans went areas that probably did not qualify as lower-income under CRA.

- Tables 1 and 2 break all US zip codes into thirds based on their poverty rate. Zip codes in the high-poverty group have poverty rates over 14.6 percent; those in the low-poverty groups have rates under 7.8 percent. The high-poverty group roughly corresponds to the Federally-defined low-and-moderate income areas targeted by CRA.
- In March of 2007, nearly 20 percent of all **prime** loans were originated in high-poverty zip codes (9.5 million of a total 50.2 million loans). In the **subprime** lending market, about one third of loans went to these same areas (2.4 million of a total 7.5 million loans). This means, of course, that a disproportionate share of all loans in high-poverty areas was subprime, and this is what some observers have seized upon. But two thirds of subprime loans (5.1 million of 7.5 million) were **outside** these high-poverty communities, in areas that probably did not qualify as lower-income under CRA.

**Table 1: Delinquency, Foreclosure, and REO Status of Outstanding Mortgage Loans
By Type of Loan and Community Poverty, March 2007**

| Loan Status / Area Poverty | Loan Type | | | | | | | | | | | | | | | | | | | | |
|---|-------------------|------------------|---|---|--|--|--|-------|----------|--------------|-----------|-----------|----------------|------------|-----------|-------------|------------|-----------|--------------|-------------------|------------------|
| | Prime | Subprime | | | | | | | | | | | | | | | | | | | |
| Delinquent | | | | | | | | | | | | | | | | | | | | | |
| High Poverty | 3.73% | 17.98% | <table border="1"> <thead> <tr> <th colspan="3">Number of Loans by ZIP Code Poverty Level</th> </tr> <tr> <th></th> <th>Prime</th> <th>Subprime</th> </tr> </thead> <tbody> <tr> <td>High Poverty</td> <td>9,507,611</td> <td>2,370,837</td> </tr> <tr> <td>Medium Poverty</td> <td>15,415,963</td> <td>2,484,862</td> </tr> <tr> <td>Low Poverty</td> <td>23,325,821</td> <td>2,664,938</td> </tr> <tr> <td><i>Total</i></td> <td><i>50,249,395</i></td> <td><i>7,520,637</i></td> </tr> </tbody> </table> | Number of Loans by ZIP Code Poverty Level | | | | Prime | Subprime | High Poverty | 9,507,611 | 2,370,837 | Medium Poverty | 15,415,963 | 2,484,862 | Low Poverty | 23,325,821 | 2,664,938 | <i>Total</i> | <i>50,249,395</i> | <i>7,520,637</i> |
| Number of Loans by ZIP Code Poverty Level | | | | | | | | | | | | | | | | | | | | | |
| | Prime | Subprime | | | | | | | | | | | | | | | | | | | |
| High Poverty | 9,507,611 | 2,370,837 | | | | | | | | | | | | | | | | | | | |
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| Low Poverty | 23,325,821 | 2,664,938 | | | | | | | | | | | | | | | | | | | |
| <i>Total</i> | <i>50,249,395</i> | <i>7,520,637</i> | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 3.11% | 17.11% | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 2.29% | 16.82% | | | | | | | | | | | | | | | | | | | |
| Foreclosures | | | | | | | | | | | | | | | | | | | | | |
| High Poverty | 1.23% | 7.91% | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 1.00% | 6.92% | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 0.70% | 6.62% | | | | | | | | | | | | | | | | | | | |
| REO | | | | | | | | | | | | | | | | | | | | | |
| High Poverty | 0.36% | 3.69% | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 0.27% | 2.96% | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 0.17% | 2.69% | | | | | | | | | | | | | | | | | | | |

**Table 2: Delinquency, Foreclosure, and REO Status of Outstanding Mortgage Loans
By Type of Loan and Community Poverty, March 2008**

| Loan Status / Area Poverty | Loan Type | | | | | | | | | | | | | | | | | | | | |
|---|-------------------|------------------|---|---|--|--|--|-------|----------|--------------|-----------|-----------|----------------|------------|-----------|-------------|------------|-----------|--------------|-------------------|------------------|
| | Prime | Subprime | | | | | | | | | | | | | | | | | | | |
| Delinquent | | | | | | | | | | | | | | | | | | | | | |
| High Poverty | 4.66% | 24.22% | <table border="1"> <thead> <tr> <th colspan="3">Number of Loans by ZIP Code Poverty Level</th> </tr> <tr> <th></th> <th>Prime</th> <th>Subprime</th> </tr> </thead> <tbody> <tr> <td>High Poverty</td> <td>9,814,863</td> <td>2,227,451</td> </tr> <tr> <td>Medium Poverty</td> <td>15,780,095</td> <td>2,308,116</td> </tr> <tr> <td>Low Poverty</td> <td>25,864,404</td> <td>2,423,877</td> </tr> <tr> <td><i>Total</i></td> <td><i>51,459,362</i></td> <td><i>6,959,444</i></td> </tr> </tbody> </table> | Number of Loans by ZIP Code Poverty Level | | | | Prime | Subprime | High Poverty | 9,814,863 | 2,227,451 | Medium Poverty | 15,780,095 | 2,308,116 | Low Poverty | 25,864,404 | 2,423,877 | <i>Total</i> | <i>51,459,362</i> | <i>6,959,444</i> |
| Number of Loans by ZIP Code Poverty Level | | | | | | | | | | | | | | | | | | | | | |
| | Prime | Subprime | | | | | | | | | | | | | | | | | | | |
| High Poverty | 9,814,863 | 2,227,451 | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 15,780,095 | 2,308,116 | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 25,864,404 | 2,423,877 | | | | | | | | | | | | | | | | | | | |
| <i>Total</i> | <i>51,459,362</i> | <i>6,959,444</i> | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 3.93% | 23.87% | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 2.94% | 23.59% | | | | | | | | | | | | | | | | | | | |
| <i>Total</i> | | | | | | | | | | | | | | | | | | | | | |
| Foreclosures | | | | | | | | | | | | | | | | | | | | | |
| High Poverty | 1.92% | 13.22% | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 1.54% | 12.03% | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 1.14% | 11.76% | | | | | | | | | | | | | | | | | | | |
| REO | | | | | | | | | | | | | | | | | | | | | |
| High Poverty | 0.58% | 6.79% | | | | | | | | | | | | | | | | | | | |
| Medium Poverty | 0.40% | 5.54% | | | | | | | | | | | | | | | | | | | |
| Low Poverty | 0.30% | 5.39% | | | | | | | | | | | | | | | | | | | |

Source: Compiled by Local Initiatives Support Corporation, Research and Assessment, from data supplied by McDash Analytics.

Note: Loan counts from McDash Analytics are weighted to reflect estimated mortgaged unit counts from the US Census and the share of prime and subprime mortgages from the Mortgage Bankers Association's March 2008 National Delinquency Survey.