How Place-Based Special Purpose Credit Programs Can Reduce the Racial Homeownership Gap

By Jung Hyun Choi, Liam Reynolds, and Vanessa Perry, Urban Institute, February 1, 2022

Special purpose credit programs (SPCPs)—which allow banks to offer credit on favorable terms to borrowers who have suffered economic disadvantage and share common characteristics (e.g., race or income)—could provide the kind of homeownership boost to Black communities today that the New Deal provided to white people in the 20th century.

We have previously shown how the effects of generations of systemic racism and economic exploitation make credit less accessible and more expensive to Black borrowers. These conditions drive the 30 percentage-point homeownership gap between Black and white households, and they contribute to the higher costs and smaller returns Black homeowners experience.

SPCPs for Black homebuyers could alleviate some of the effects of historical unequal treatment in mortgage lending, improve access to credit in Black communities, and narrow the racial homeownership gap. But targeting programs to specific people can be difficult for lenders to implement, because they require significant outreach and engagement work and verification of eligible borrowers.

To avoid some of these challenges, lenders could implement place-based SPCPs, which target distinct geographic areas rather than specific people. Whether place-based SPCPs are more effective than people-based approaches will depend on the homeownership challenges unique to the location.

How do SCPCs work?

The Equal Credit Opportunity Act of 1974—which prohibits discrimination based on race, color, religion, national origin, sex, marital status, age, or receipt of public assistance—allows the provision of SPCPs. Federal or state governments, nonprofit organizations, community development financial institutions, and private lenders can offer these programs. Though the Equal Credit Opportunity Act explicitly permitted SPCPs nearly 50 years ago, few exist today. But with growing awareness of how systemic racism affects homeownership, more lenders are interested in implementing SPCPs.

To offer an SPCP, for-profit lenders must develop a written plan that identifies whom their program seeks to benefit and how they will make credit accessible to those borrowers. They must also demonstrate that the class of borrowers that benefits from the program probably would not receive credit—or would have to pay more for it—under traditional credit standards. To make these determinations, lenders can use their own research or use data from outside sources like research institutions or governmental agencies.

SPCPs could offer homeownership supports such as down payment assistance, income restriction exceptions, home rehabilitation loans, and streamlined refinance loans in addition to flexible underwriting standards and breaks on loan-level pricing.

Place-based SPCPs can improve access to credit in Black communities

Place-based approaches to addressing racial homeownership gaps are gaining traction and acceptance. The Consumer Financial Protection Bureau proposed lenders use Home Owners' Loan Corporation redlining maps to establish SPCPs, and the Federal Housing Finance Agency recently revised its affordable housing goals to expand lending in communities of color. JPMorgan Chase also announced that it will increase its housing grant program to serve predominantly Black neighborhoods.

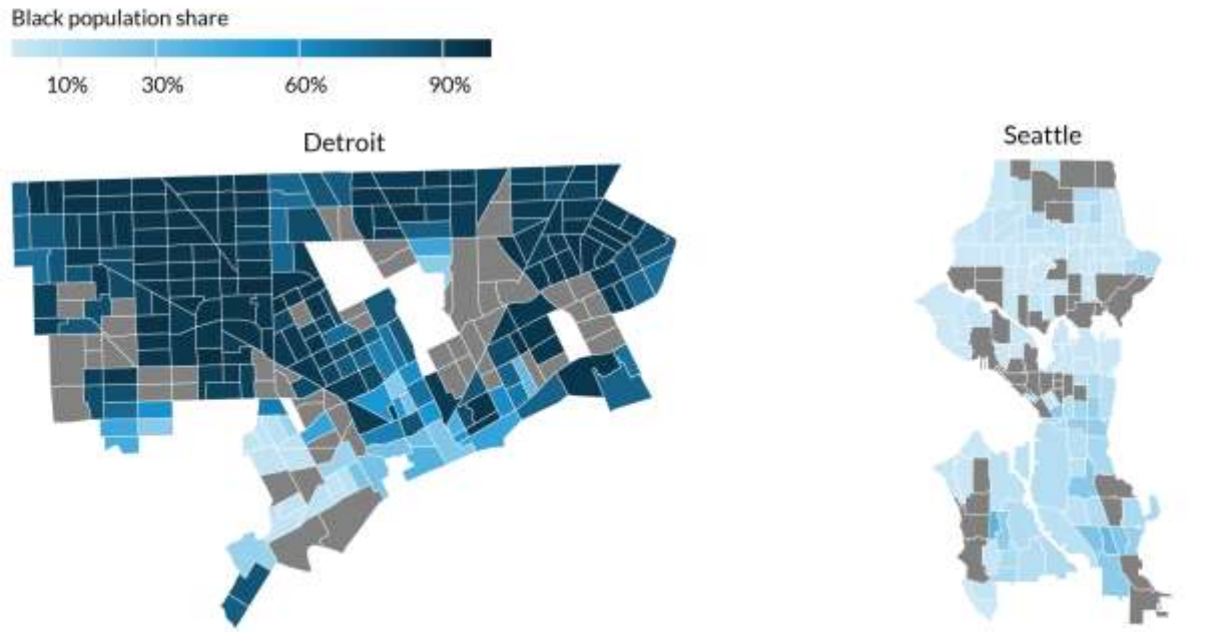
By targeting areas based on racial composition, SPCPs could effectively address the racial homeownership gap in some areas of the country. Our analysis of 2015–19 American Community Survey data finds that Black households living in moderate-income (earning between 80 and 120 percent of the area median income, or AMI) Black neighborhoods have a homeownership rate of 57 percent, similar to the homeownership rate of white households living in low-income (earning below 80 percent of the AMI) white neighborhoods. The Black homeownership rate in low-income Black neighborhoods was 35 percent, significantly lower than white households in low-income white neighborhoods (57 percent).

But the effectiveness of place-based SPCPs could vary across locations. US cities and metropolitan areas remain segregated—the average white household lives in a neighborhood that is 71 percent white, and the average Black or Hispanic household lives in a neighborhood that is 62 percent Black or Hispanic—but there are variations across areas.

A city's racial composition and degree of segregation may shape how effectively programs reach the intended community. For example, more than 75 percent of Detroit's population is Black, and the city is one of the most segregated places in the country. Thus, programs that extend special purpose credit to majority-Black neighborhoods there would likely serve mostly Black borrowers.

In contrast, only 7 percent of Seattle's residents are Black, and Black households aren't concentrated geographically, making it difficult to design a place-based SPCP that mainly benefits Black borrowers. This suggests that place-based SPCPs would likely be more effective in reaching Black households in places like Detroit than in places like Seattle.

Place-Based SPCPs Would Likely Be More Effective in Reaching Black Households in Cities with a Large Share of Majority-Black Neighborhoods



Source: Urban Institute analysis using 2020 Census data.

URBAN INSTITUTE

Weighing the additional considerations of different place-based SPCP approaches

The two broad types of place-based SPCPs require different considerations and additional data analysis.

The first type extends credit to people who currently live in designated economically disadvantaged areas. These programs could allow borrowers to purchase anywhere or require them to purchase in their current neighborhoods, increasing investment and homeownership in these areas. But restricting borrowers' mobility may also limit the wealth-building potential of homeownership, as property values in low-income neighborhoods tend to appreciate more slowly than those in affluent areas.

Developers of these programs should be aware of unintended consequences. For example, limiting Black homebuyers to the neighborhoods where they currently live may compound the effects of generations of forced neighborhood racial segregation. Black homebuyers could also be constrained to buy homes in areas with limited education and employment opportunities. Further, in areas like Seattle, those who have been affected by systemic racism may live outside the program's target geography.

The second type extends credit to buyers who currently live anywhere but are required to purchase in a designated economically distressed community. These programs may effectively spur investment in targeted areas, but they could also invite affluent borrowers to take advantage of relatively low property values and cheap credit, which could initiate gentrification and displacement. To prevent this result, the SPCP could be limited to borrowers with low or moderate incomes, borrowers who don’t qualify for conventional loans, or first-generation homebuyers.

In either approach, place-based SPCPs can be more effective if lenders work with local partner organizations from the beginning to understand the local context and determine how to design the SPCP to maximize community benefit. An SPCP should be based on thorough analyses that examine the area’s racial distribution and the challenges Black borrowers face in specific markets. This process is essential to designing a program that works to unwind the impacts of decades of racial and spatial disinvestment.

We will continue to publish research in the coming months on how to leverage SPCPs to create a more equitable housing finance system.