The Subprime and Foreclosure Crisis: Ten Years Later

The Work of Financial Justice is as Important as Ever

By Jillian Olinger, Senior Research Associate

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This past month marked the ten year anniversary of the onset of the Great Recession. Beginning in September 2007, and continuing at a breathtaking pace, Lehman Brothers collapsed, setting off a chain reaction during which American International Group (AIG) came to the brink of failure, disruptions requiring the Federal Reserve and Treasury Department to take unprecedented steps to provide liquidity and support to a rapidly (and globally) destabilizing financial sector;[1] Fannie Mae and Freddie Mac were placed in conservatorship as their books of business reflected severe damage from deteriorating housing market conditions; and Congress passed the Emergency Economic Stabilization Act of 2008, which included a $700 billion Troubled Asset Relief Program.

The pain—even trauma[2]—inflicted on American households and workers as a result of this crisis cannot be overstated. With time, effort, and the installment of new rules and protections, many have been able to bounce back,[3] and the intensity of the crisis may be fading from our collective consciousness. The national unemployment rate peaked at 10% in October 2009 (and was significantly higher for workers of color);[4] today, it is 4.4%.[5] In 2009, a stunning 3 million homes had been foreclosed on in communities across the country.[6] Today, approximately 483,000 homes are in some stage of the foreclosure process.[7]

And yet, for too many Americans—especially people of color—this crisis has not ebbed. For some, and in many communities, it has instead grown. Recovery has been, and continues to be, extremely uneven. For example, analysis shows that Black median wealth never recovered from the 2001 recession, and Latino wealth has not recovered from the Great Recession. In contrast, white wealth was left untouched by the 2001 recession and rebounded after only two years from the Great Recession.[8]

Racial wealth gap reaches startling new levels

Research shows that the average wealth of white families has grown 84% over the past 30 years, which is 1.2 times the rate of growth for Latino households, and three times the rate of Black households. It is projected that by the year 2043, when people of color will become the majority of the population, the wealth divide will have doubled from $500,000 in 2013 to over $1 million.[9] By this measure, it will take 228 years to resolve this inequality for Black families, just 17 years shorter than the span of slavery. Likewise, it will take Latino families 84 years to reach the same amount of wealth that white families have today. If current trends continue, researchers predict that Blacks are on track to have zero median wealth by 2053, Latinos to have zero median wealth by 2073, and whites to have $137,000 in median wealth by 2053.[10] Researchers estimate that white families will have 31% fewer assets by 2031 than they would have had the Great Recession not happened, and Black families 40% fewer assets.[11]

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Wealth is about time. The Great Recession drained more than $17 trillion in wealth from American families. Black and Hispanic families lost a shocking 66% and 53% of their household wealth, respectively, harming their ability to save and invest in the future of their families, their communities, and our nation's economy. Without wealth, households have no foundation on which to build and leverage their hopes, for example for retirement, college savings, moving to take advantage of a new job opportunity, or opening a small business. The racial wealth gap continues to drive inequality in opportunity for Americans across the country, ensuring the crisis continues, and our national economy suffers because of it: the nation's median wealth decreased nearly 20% from 1983 to 2013 because of the growing racial wealth gap.[12]

Affordable housing crisis continues unabated

While an affordable housing crisis has been plaguing low-income households for generations, its reach has now ensnared many middle-income households—renter and owner alike. Foreclosures, tighter credit and housing markets, and economic challenges for workers have created tremendous housing burdens.[13] Today, a staggering one in five of all renting American households spends at least 30% of its income on housing.[14] The burden is more pronounced for renters of color: nearly 60% of Black renters and 57% of Latino renters spends more than 30% of their incomes on housing.[15] In nearly every state, rents (up 4% since 2007 nationally) have far outpaced growth in incomes (down 7% nationally) since before the recession.[16] Increasingly tenuous housing situations compounded by growing income volatility for our lowest income households have facilitated a growth in homelessness in our tightest housing markets.[17] Despite declines in foreclosures and delinquency rates, homeownership has remained relatively steady (or declined), reflecting the unaffordability of housing. Nationally, homeownership has held steady at 63%.[18]

Threats to federal protections place American households at risk of another fallout

Under the Trump Administration, threats to consumer protections have been repeatedly launched. In the aftermath of the subprime and foreclosure crisis, the federal government undertook prudent financial regulations to reinstate soundness to a financial system that had undergone substantial—and as we now know, devastating—deregulation. One key outcome of these efforts (known as the Dodd-Frank Wall Street Reform and Consumer Protection Act), was the creation of a new agency tasked with consumer protections, the Consumer Financial Protection Bureau (CFPB). In its first five years alone, the CFPB has returned nearly $12 billion to millions of victims of financial wrongdoing across the country.[19] It has written stronger rules governing mortgages, prepaid cards, payday loans, credit cards, student loans, auto loans, and more. Indeed, for every $1 of funding, the agency has returned $5 to victims of financial predation.[20] The CFPB is a critical antidote to the harms visited on vulnerable communities of color at the height of the subprime crisis. It must be protected.

Implicit racial biases influence our financial decision-making, arbitrarily harming borrowers of color

Research is demonstrating how a broad range of implicit, invisible barriers affect very real and critical decisions in the housing landscape. Generations of racialized laws, policies, and practices (i.e. structural racialization) have imposed a racial bias on our collective normative values over time. Our minds are wired to automatically piece together information to make sense of the world around us. As part of this automatic process, people unconsciously internalize the patterns of inequity in our society in the form of implicit racial bias, or those attitudes or stereotypes that affect our behavior and decision-making without our conscious awareness. This translates to a pervasive implicit association of race with risk, or more precisely, blackness with risk, and whiteness with security and safety.[21] One example of this can be found in our credit scoring practices. Research consistently documents that current industry standards of credit scoring disadvantage borrowers of color, and that more promising practices of determining risk exist. For example, studies conducted by Experian have found the inclusion of utility payments in a credit scoring model could cut the number of borrowers considered subprime in half.[22] Importantly, this inclusion could be achieved without loosening credit standards. Despite the evidence to support re-working our credit scoring models, Fannie Mae and Freddie Mac, the two dominant players in our housing finance system, have decided to push off overhauling their credit scoring systems to 2019.[23] Not only does such a decision needlessly continue to disadvantage households of color, it harms our national economy.

Predatory practices on the rise again: land contracts & FinTech highlight emerging gaps in regulation

Homeownership remains a worthy goal of Americans across the country, and yet, thousands find themselves locked out of it (for example, due to stagnant incomes, or outdated credit scoring models). Recognizing a market ripe for exploitation, large scale investors have swooped in with high-interest, seller-financed deals that work as installment plans for housing. These too-good-to-be-true instruments—which are unevenly regulated—are known as "land contracts" and while these instruments are not new, they have always been predatory and designed to fail. In these contracts, the owner of the property promises to convey legal title of the home to the buyer after successful completion of payments towards the full purchase price of the home, often 30 years. During this time, the buyer is responsible for all aspects of "homeownership" and should the buyer at any time default on payments, the seller retains the right to cancel the contract, keep all payments, and evict the buyer. Historically, land contracts were the province of individual sellers, who owned one or two investment properties and who targeted redlined communities of color. Today, the exploitative nature of these instruments has taken on new urgency as large-scale investors buy up large numbers of foreclosed homes (many from GSE bulk sales), and market them to locked-out, would-be homeowners. Analysis finds problems or abuses with these instruments in 80% of states.[24] This practice not only depletes the precious resources of would-be homeowners (with little or no room for redress), it also stymies the revitalization of neighborhoods devastated by the foreclosure crisis.

A second emerging industry to keep an eye on is the rise of "FinTech." FinTech firms have been able to exploit a regulatory vacuum because they are not deemed "traditional banking entities" (and thus are not subject to oversight by the FDIC, for example). FinTech operates in much the same way that predatory payday lending does for individual consumers. This "fledgling" industry (representing an estimated $25 billion a year in loans)[25] promises faster loan application and approval processes, which is surely appealing, than traditional small business lending is able to offer. But as the subprime crisis revealed—when it comes to our financial system, faster is almost never better, especially when it comes at the expense of consumer protections. These firms have been found to violate the standards of fairness in lending, which includes straightforward and honest disclosure about the terms of the loan. Already, some firms have been brought to task for failing to deliver on promises of improved consumer outcomes,[26] hiding "junk fees", charging interest rates that run into the hundreds, changing the terms of the agreement, automatically debiting payments from consumer accounts (with no recourse for suspending the debit), or initiating prepayment penalties.[27] FinTech poses grave civil rights concerns. As they stand now, non-depository FinTech firms are beyond the reach of the Community Reinvestment Act, which opens the door to "digital (reverse) redlining." Unlike mortgages, which are tied to HMDA reporting requirements, business loans do not have the same transparency: banks are not required to report business loans they reject, or the characteristics of the borrower. Despite opposition from consumer rights groups, the Office of the Comptroller of Currency has been considering allowing FinTech firms to become chartered as “special purpose national banks,” a move that would preempt states’ rights to protect their consumers from abusive interest rates, for example, and avoid court-established protections against unfair lending practices. And because FinTech firms operate online, they can simply avoid setting up shop in unfriendly states, thereby avoiding any interest rate caps put in place by that state, and yet still market their products nationwide.

Advocates across the country continue to grapple with the challenges of pursuing financial justice, especially when it comes to making meaningful inroads on closing the racial wealth gap. The ever-evolving landscape of our financial system means that the work of civil rights and consumer protections is far from a done deal. If anything, recent developments with online lending and new predatory, minimally regulated instruments such as land contracts, means that tracking consumer protections and outcomes is all the more challenging. Meanwhile, households continue to struggle to make ends meet, to secure a financial foothold that will provide opportunity for them today, and the next generation. When it comes to achieving financial justice, we are challenging what it means to be middle-class in America, and the benefits associated with reaching middle class. For white households, reaching the “middle class” brings with it far different opportunities than it does for Black and Latino households. Indeed, “first-generation, even second-generation African-American and Latino households have professional jobs and are making ‘middle-income money’—but they have the wealth of a white high-school dropout.”[28] Middle-class status *should* mean financial stability, and the ability to weather economic shocks and invest in the future. For far too many Americans, this is simply not the case. This stark reality forces us to question our assumptions about housing and its purpose, and its role in pursuing the American Dream. This is no small task, ideologically or practically: “For the oppressed, housing is always in crisis…. Discrete moments when housing crises become acute tend to be interpreted away as exceptions to a fundamentally sound system. But this is an ideological distortion. Housing crisis is not the result of the system breaking down, but of the system working as it intended.”[29] The Subprime Crisis of 2007, and subsequent Great Recession, showed us many things about our housing and finance markets. It remains to be seen whether we have, in fact, internalized those lessons. ■

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