RESEARCH REPORT

Before the Pandemic, Homeowners of Color Faced Structural Barriers to the Benefits of Homeownership

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Homeowners of Color Faced Barriers to the Benefits of Homeownership

Building up positive home equity is the primary financial benefit of homeownership and a key method of wealth accumulation. A homeowner has a positive housing equity position when the value of the household's primary residence exceeds any debt collateralized by the home. Positive equity gives homeowners the opportunity to make home improvements that may increase the home's value, invest in higher education to strengthen their or their children's human capital, and have seed money to start a business. Housing equity may also remain in the home for use during an emergency.

A comprehensive assessment of the financial framework of homeownership, relative to renting, extends beyond housing equity. Potential appreciation in home values along with the tax benefits of itemization are also benefits of homeownership. Rather than rent, homeowners pay the "user costs" of homeownership, such as mortgage interest payments, property taxes, and maintenance and insurance costs. Although homeownership guards against inflation,[1] as mortgage interest is locked in with a fixed-rate mortgage, the financial benefits of homeownership vary over time. For example, the Tax Cuts and Jobs Act of 2017 (TCJA) reduced the financial benefits of homeownership for many homeowners by reducing the tax benefits.[2] In contrast, the ability to lower mortgage payments through refinancing when interest rates fall increases the potential financial benefits of homeownership.

This report is the second in a series examining outcomes for Black and Hispanic homeowners in response to the economic downturn (Neal and McCargo 2020). The series intends to elevate the role of racial equity when examining economic cycles; promote equity-conscious federal, state, and local policies; bring forth relevant data and analysis; and create tools to accelerate equitable and inclusive recovery.

The first paper, *How Economic Crises and Sudden Disasters Increase Racial Disparities in Homeownership*, established a framework for the work to come (Neal and McCargo 2020). This report compares the benefits of homeownership between racial and ethnic groups before the crisis, making two points:

- First, since homeownership first became viable for Black families, who had historically been denied access to this asset, the benefits have been uneven and have not accrued equitably. Differences in household-level outcomes explain part of this gap.
- Second, a history of segregation and discrimination has reduced the financial benefits of homeownership for homeowners of color. Policy recommendations must address persistent disparities that have held back wealth building through homeownership for households of color and address how those impacts widen during economic downturns.

Homeowners of Color Have Less Housing Equity

Black households with housing equity have about half the median equity of white households, and Hispanic households have about 63 percent. These differences in housing equity reflect differences in underlying home values and the total amount of mortgage debt.

TABLE 1

Median Housing Equity among All Homeowners with Housing Equity, by Race or Ethnicity

	Median housing equity
White	$118,000
Black	$60,000
Hispanic	$74,000

Source: 2016 Survey of Consumer Finances.

All else equal, lower home values for homeowners of color relative to the values of homes owned by white homeowners contribute to lower housing equity for Black and Hispanic homeowners. The differences in home values, in turn, can partly be explained by disparities in income and access to financial assets.

Homeowners' equity is determined by the amount of the home mortgage. Greater mortgage debt, relative to a home's value, results in less housing equity, and, conversely, low or no mortgage debt boosts housing equity. The greater amounts of mortgage debt relative to the home's underlying value, referred to as a high loan-to-value (LTV) ratio, is often the result of fewer resources that homebuyers of color can draw on for a down payment and closing costs.

Differences in equity at the time of purchase and over the life of a loan are foundational to understanding why wealth outcomes are worse for homeowners of color and what policy levers can address these problems. Housing equity is a key component of a household's overall net worth and wealth accumulation.[3] Furthermore, homeowners of color have greater net worth than renters of color because of their home equity. Conditions that minimize housing equity growth have a disproportionate impact on overall wealth building for communities of color.[4]

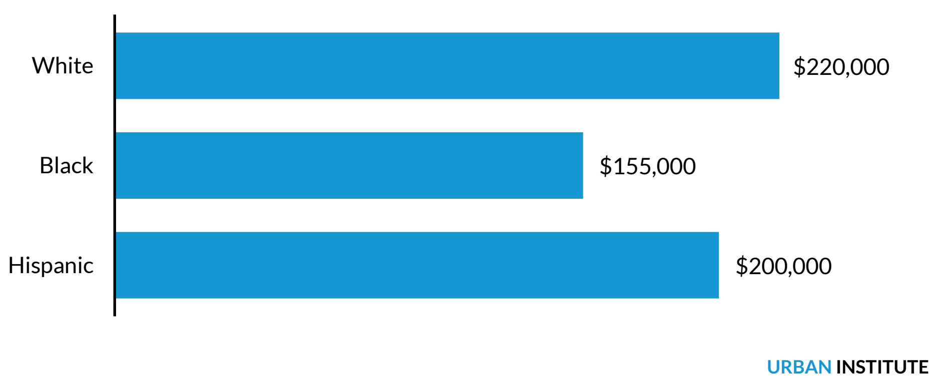
Lower Home Values and Higher Mortgage Debt Result in Less Housing Equity for Homeowners of Color

Homeowners of Color Typically Purchase More Affordable, Lower-Cost Homes with Bigger Mortgages

Heading into the current recession, the home values of Black and Hispanic homeowners were consistently below that of white homeowners. The median value of white-owned homes was $220,000 in 2018 compared with $155,000 for Black owners and $200,000 for Hispanic owners (figure 1). In virtually all large markets, the value of white-owned homes exceeded that of Black- and Hispanic-owned homes.

FIGURE 1

Median Home Values in 2018, by Race or Ethnicity

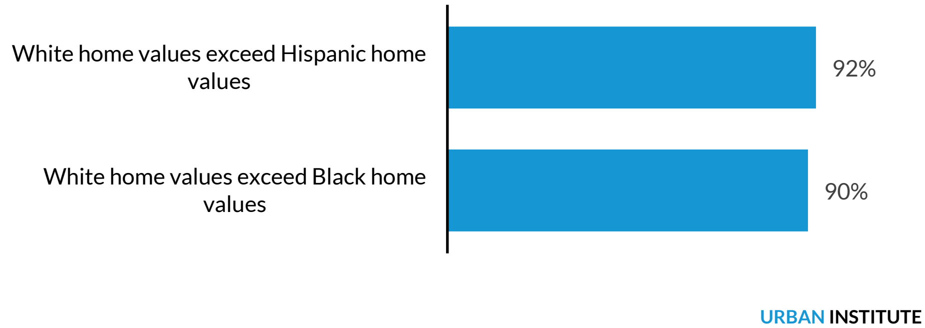


Source: American Community Survey.

Figure 2 shows that in 2018, the median value of white-owned homes exceeded the median value of Hispanic-owned homes in 92 percent of the 100 largest metropolitan statistical areas and exceeded the median value of Black-owned homes in 90 percent.

FIGURE 2

Share of the 100 Largest Metropolitan Statistical Areas Where Median Home Values for White Homeowners Exceed Those for Black and Hispanic Homeowners



Source: American Community Survey.

Homeowners of Color Have More Mortgage Debt

Homeowners without a mortgage have the most housing equity relative to their home's value. Figure 3 indicates that before COVID-19, Black and Hispanic homeowners were more likely to have a mortgage than white homeowners. The 2018 American Community Survey indicates that 67 percent of Black homeowners and 66 percent of Hispanic homeowners have a mortgage, compared with 61 percent of white homeowners.

FIGURE 3

Share of Homeowners with a Mortgage, by Race or Ethnicity

Source: 2018 American Community Survey.

Homeowners of color also have more mortgage debt relative to their home's value. For Black mortgage holders, the median LTV ratio was 66 percent, compared with 61 percent for Hispanic mortgage holders and 56 percent for white mortgage holders (figure 4).

FIGURE 4

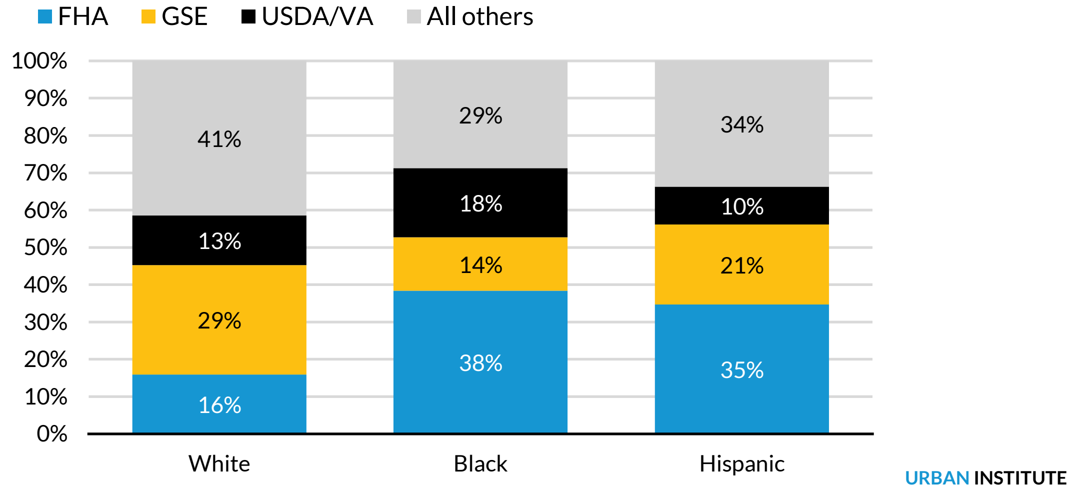
Loan-to-Value Ratios among Homeowners with a Mortgage, by Race or Ethnicity

Source: Survey of Consumer Finances.

The greater debt levels among homeowners of color may reflect more debt taken out when the home is purchased. The higher down payment percentages at purchase partly reflect the disproportionate use of Federal Housing Administration (FHA) mortgages by homebuyers of color (figure 5), because the FHA requires only a 3.5 percent down payment. But even across conforming conventional mortgages, homebuyers of color are more likely to have higher LTV ratios than their white counterparts, lowering their overall equity (figure 6).

FIGURE 5

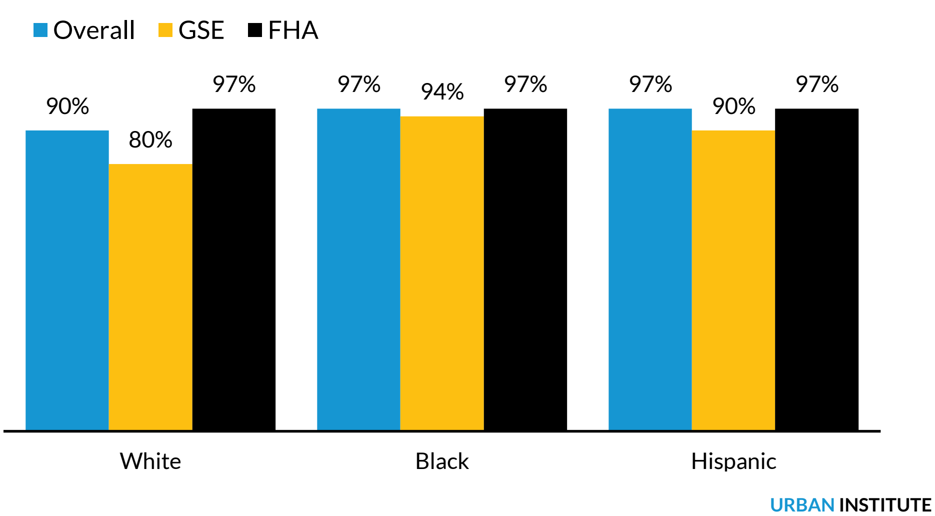
Composition of 2019 Purchase Mortgages, by Race or Ethnicity



Source: Home Mortgage Disclosure Act data.
Notes: FHA = Federal Housing Administration; GSE = government-sponsored enterprise; USDA = US Department of Agriculture; VA = US Department of Veterans Affairs. "All others" includes all non–federally backed mortgages, including those held in portfolio and in private-label securities.

FIGURE 6

Median Loan-to-Value Ratios at Purchase, by Race or Ethnicity and Channel



Source: 2018 Home Mortgage Disclosure Act data.
Note: FHA = Federal Housing Administration; GSE = government-sponsored enterprise.

A separate analysis confirms that households of color typically purchase less expensive homes and take on greater mortgage debt.[5] These differences at the outset of homeownership contribute to less housing equity accumulated over time for Black and Hispanic homeowners. At the same time, homeowners of color typically purchase their first homes later in life, while research indicates that buying a home at a younger age leads to greater wealth in retirement.[6]

Economics Is Only Part of the Reason Homeowners of Color Have Less Housing Equity

White Homebuyers Have Greater Access to Financial Assets That Can Boost the Amount of Home They Can Afford and Lower the Amount of Mortgage Debt Needed for a Home Purchase

The lower value of homes that Black and Hispanic households buy partially reflects more modest financial resources that limit what homebuyers of color can afford. For example, the typical household of color has less income and less wealth than the typical white household (table 2).

TABLE 2

Median Family Income and Financial Assets among Renters and Homeowners in 2016, by Race or Ethnicity

	White	Black	Hispanic
Median family income			
Overall	$60,758	$35,442	$38,480
Renters	$35,442	$27,341	$29,366
Homeowners	$76,960	$50,632	$52,657
Median financial assets			
Overall	$50,700	$3,900	$2,520
Renters	$4,970	$1,580	$1,140
Homeowners	$96,850	$19,370	$9,270

Source: Survey of Consumer Finances.

The lower income and wealth reflect lower wages and salaries and fewer financial assets, including savings accounts, certificates of deposit, retirement accounts, and other liquid assets that could be used to purchase a home. Limited financial assets also increase the amount of mortgage debt needed for a home purchase.

Intergenerational wealth differences also affect access to financial resources. Young white college graduates are more likely to receive financial support from their parents to purchase a home than Black college graduates (Meschede et al. 2017).

Differences in income, financial assets, and intergenerational wealth contribute to the home equity gap between white homeowners and homeowners of color. Disparities in education and personal income account for 20 to 30 percent of both the Black-white and the Hispanic-white wealth gaps.[7] Greater wealth inequality makes excessive borrowing more prevalent (Kumhof, Rancière, and Winant 2013), which further exacerbates racial and ethnic gaps in housing equity.[8]

Discrimination Contributes to Home Equity Differences

Access to fewer financial resources does not fully explain differences in home equity between white homeowners and homeowners of color. Systemic discrimination, whether explicit or subtle, also contributes to this gap, in part by lowering home values for homeowners of color. For example, when looking to buy a home, minorities were significantly more likely to be steered toward more disadvantaged neighborhoods by their real estate agent, despite being virtually identical to white buyers.[9] These neighborhoods are often characterized as more segregated with higher rates of crime or poverty, which can create stigma for appraisals and limit home values (Turner et al. 2013).

In addition, racial bias in appraisals has also been shown to inform home value gaps in some regions of the country (Howell and Korver-Glenn 2018). Some appraisers use a neighborhood's racial and ethnic composition as a proxy for other measures used to determine home values, perpetuating structural barriers and racial disparities.[10] This suggests that variation in appraisal methods coupled with appraisers' racialized perceptions of neighborhoods perpetuates neighborhood racial and ethnic disparities in home values.[11]

The historical links between zoning and racial discrimination may limit home value appreciation in predominately minority neighborhoods (Shertzer, Twinam, and Walsh 2014). For example, zoning historically was used to steer industrial activity toward minority neighborhoods, leading to disproportionate toxic exposure and depressed land values (Shertzer, Twinam, and Walsh 2014, 13). Depressed land values weigh on broader home prices and contribute to the gap between white-owned homes and those owned by people of color.

Multigenerational discrimination has also limited the amount of wealth households of color accrue, which makes them more reliant on debt to attain homeownership. The violent massacre that decimated Tulsa, Oklahoma's Greenwood District (commonly referred to as "Black Wall Street") in 1921; discriminatory policies throughout the 20th century, including the Jim Crow Era's "Black Codes," strictly limiting opportunity in many southern states; the GI Bill; the New Deal's Fair Labor Standards Act's exemption of domestic agricultural and service occupations; and redlining limited the accumulation of Black wealth. Wealth was stripped from these communities before it had the opportunity to grow.[12]

Discrimination in other economic areas, such as the labor market, may indirectly contribute to these gaps as well. For example, discrimination in employment has been linked to the lack of minority workers in high-paying jobs.[13] Discrimination reinforces the income gap between white people and people of color, which limits the home prices that Black and Hispanic homebuyers can afford.

Homeowners of Color May Have Modestly Higher User Costs of Homeownership

Evidence indicates that heading into the COVID-19 crisis, the typical homeowner of color had less housing equity than the typical white homeowner, thanks to lower home values and higher loan-to-value ratios. Many Black homeowners were still recovering from negative equity caused by the Great Recession. In addition to mortgage payments, homeownership costs relative to the home's value includes property taxes, maintenance costs, and insurance. Separately, the depreciation rate also affects the user costs of homeownership. Homeownership benefits also include the value of the tax advantage from itemizing mortgage interest and property tax payments as well as any house price appreciation.

The user-costs-of-homeownership framework incorporates all these elements into a simple model that quantifies the benefits of homeownership relative to renting (Poterba and Sinai 2011). When user costs rise, the benefits of homeownership relative to renting falls, and when user costs fall, homeownership benefits improve. For example, higher maintenance costs, property taxes, or insurance costs relative to the home's value reduce the benefits of homeownership relative to renting. By adding these costs and adjusting for tax offsets, the user cost concept provides a measure of the real costs of homeownership.

This is important in part because "hidden costs," such as property taxes, maintenance, and insurance, are often not included when a homebuyer considers the value of homeownership.[14] These costs can be a surprise and a burden for homeowners and could have a big impact, particularly for homeowners with tight budgets.

Homeowners of color have higher user costs than white homeowners. Although the difference is small, these yearly numbers compound over time. The slightly higher user costs for Black and Hispanic homeowners indicate that the benefits of homeownership for homeowners of color relative to renting are smaller than for white homeowners.[15]

FIGURE 7

Median Direct User Costs as a Share of Median Home Values, by Race or Ethnicity

Source: American Housing Survey.
Note: User costs include mortgage, property tax, maintenance, and insurance.

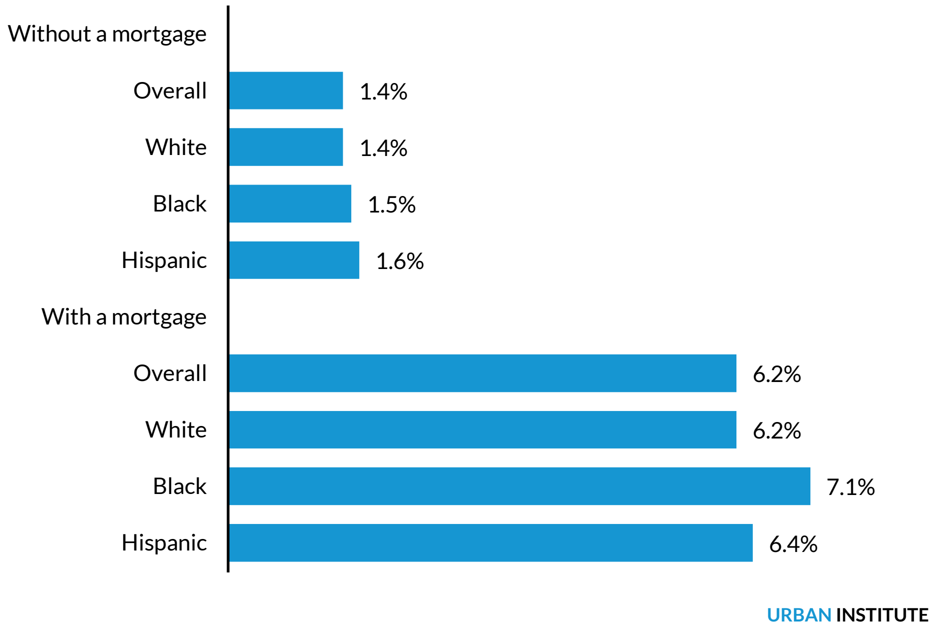
Why Are User Costs Higher for Homeowners of Color?

Differences in Direct User Costs Largely Reflect Homeowners with a Mortgage

The racial and ethnic differences in homeowners' direct user costs largely reflect the presence of a mortgage (figure 8). The direct user costs for Black homeowners with a mortgage are 90 basis points above the same for white homeowners. In contrast, the Black-white difference among homeowners without a mortgage is 10 basis points. The differences between white and Hispanic homeowners are similar: 20 basis points for homeowners with or without a mortgage. But homeowners of color are more likely to have mortgage debt than white homeowners. The greater incidence of mortgage debt among homeowners of color boosts the overall estimate of direct user costs.

FIGURE 8

Median User Costs as a Share of Median Home Values, by Race or Ethnicity



Source: American Housing Survey.

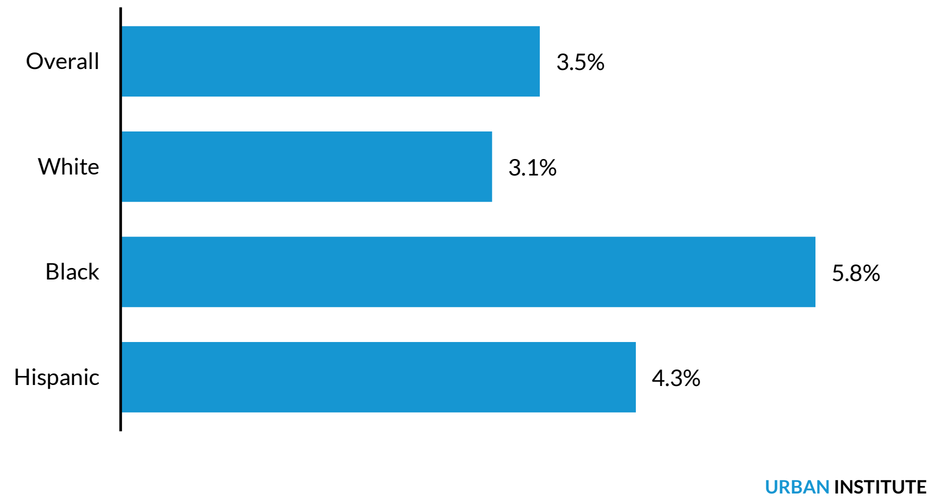
Homeowners of color tend to pay higher mortgage interest rates than white homeowners on similar loan products. But the differences are small (Liu et al. 2019). The variation by race or ethnicity likely reflects differences in credit scores, with homeowners of color having lower credit scores and higher LTV ratios and debt-to-income ratios than white homeowners.

Homeowners of Color Are More Likely to Live in Inadequate Housing

Few homeowners live in moderately or severely inadequate housing. But homeowners of color are more likely than white homeowners to live in inadequate housing. Figure 9 shows that 3.1 percent of white homeowners indicated that they lived in inadequate housing conditions. Meanwhile, 5.8 percent of black homeowners and 4.3 percent of Hispanic homeowners live in inadequate housing. This suggests that a modestly larger share of homeowners of color live in lower-quality housing, which requires more repairs and maintenance that increase user costs.

FIGURE 9

Share of Homeowners Living in Moderately or Severely Inadequate Housing, by Race or Ethnicity



Source: American Housing Survey.

Federal and Local Taxes May Have Disparate Impacts

Historically, a major benefit of homeownership was the ability to increase tax deductions by "itemizing" property taxes and mortgage interest paid over the year. But the TCJA significantly reduced the benefits of itemization by limiting property tax deductions. In addition, homeowners are restricted to deducting mortgage interest paid on only the first $750,000 worth of principal[16]. The law also raised the standard deduction that a filer can take in lieu of itemizing. The result is less itemizing overall, which lowers the tax benefits of homeownership for all homeowners. According to the Tax Foundation, the share of taxpayers itemizing in 2019 is expected to be 13.7 percent, significantly below the share estimated to have itemized in 2019 under pre-TCJA law (Eastman and Tyger 2019).

The TCJA appears to have broadly reduced the benefits of homeownership. And Black and Hispanic homeowners may be disproportionately impacted by the TCJA, but the full effect is not clear. On the one hand, the near doubling of the standard deduction could more severely limit itemization by homeowners with lower-valued homes. On the other hand, given that they itemize, lower-income homeowners have likely experienced a smaller reduction in their housing-related tax deductions relative to higher-income homeowners[17].

Recent studies show that many county tax assessors routinely saddle Black and minority residents with property tax bills that are too high relative to the value of their homes.[18] The higher property taxes may burden some homeowners of color, leading to property tax delinquency or foreclosure. Programs targeting these homeowners can keep them from losing their homes through tax foreclosure auctions.[19]

Discriminatory Practices May Lessen Homeownership Benefits for Homeowners of Color

Several structural barriers reduce homeownership benefits for households of color.[20] Research suggests that racial and ethnic disparities in mortgage costs have not declined (Quillian, Lee, and Honoré 2020). In addition, the promise held by financial technology (fintech) with respect to racial and ethnic disparities has only been partially fulfilled. Although fintech has lowered borrower costs and borrowing rates, these benefits have largely accrued to affluent households, and racial and ethnic differences persist (Barlett et al. 2019; Choi, Kaul, and Goodman 2019).[21]

Explicit forms of historical discrimination have likely contributed to housing deterioration in many majority-minority neighborhoods.[22] For Black households, segregation limited the amount of investment flowing into these communities, causing the housing stock to deteriorate. Although redlining is now illegal, thanks to the Fair Housing Act of 1968, recent investment trends in some cities, such as Chicago and Baltimore, still track those same red lines.[23] Hispanic households, as well, have experienced discrimination that has coincided with reduced access to adequate housing.[24]

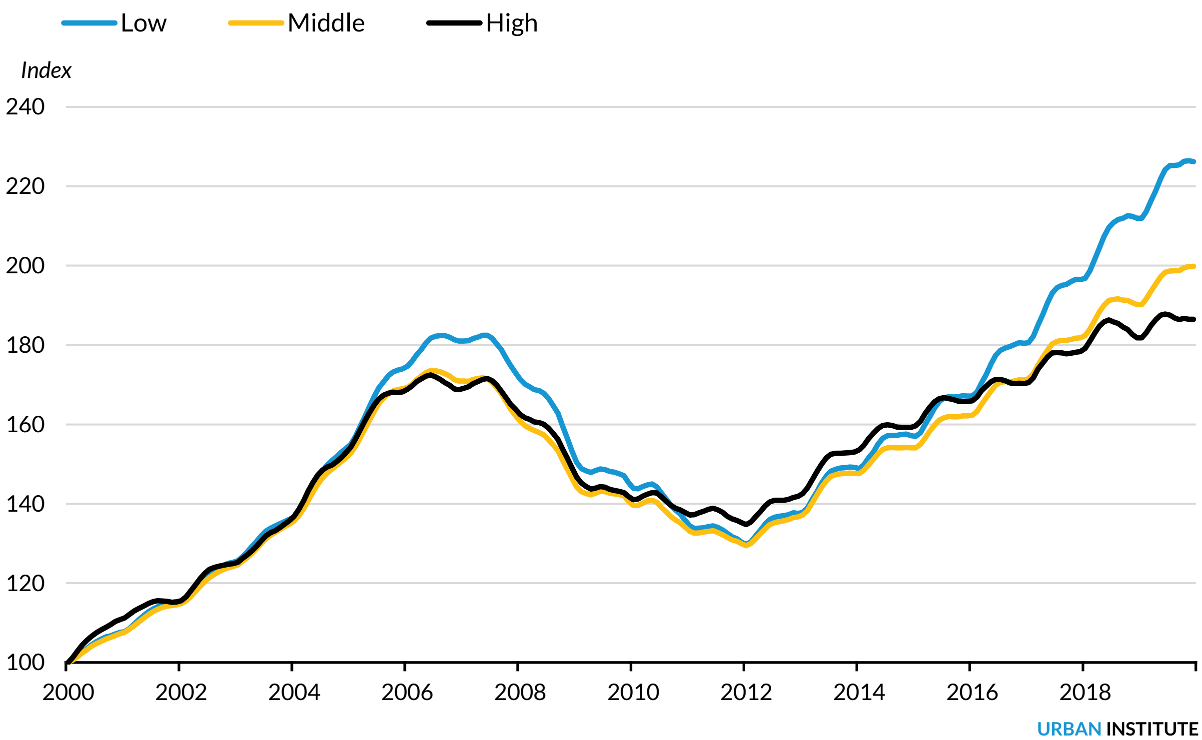
Although laws such as the Fair Housing Act were created to reverse housing segregation, enforcement of the rules designed to implement these laws has been uneven. And the Affirmatively Furthering Fair Housing rules, implemented in 2015 to push local governments to track poverty and segregation, were recently eliminated, reducing tools available to enforce the Fair Housing Act.[25]

Home Price Appreciation May Be a Bright Spot for Homeowners of Color

The home values of homeowners of color are persistently below those of white homeowners. But home price appreciation, particularly for Black homeowners, has surpassed that of white homeowners in some parts of the country since 2012 (Immergluck, Earl, and Powell 2019). Faster house price growth for some Black homeowners partly reflects the shortage of low-price homes. Although faster house price growth worsens housing affordability and access to homeownership, it lowers user costs and increases homeownership benefits for current homeowners, all else constant.[26]

FIGURE 10

Home Price Changes, by Tier (National Index)



Source: Urban Institute calculations of data from Black Knight.

Policy Recommendations

The gaps in homeownership's financial benefits by race and ethnicity existed before COVID-19. They can increase vulnerability among homeowners of color during an economic downturn. Four policies could eliminate these differences in homeownership's benefits for people of color. These proposals, which are rooted in the broader Five Point Framework for Reducing the Black Homeownership Rate Gap,[27] target persistent structural barriers in homeownership's financial benefits, regardless of whether the economy is shrinking or expanding (McCargo, Choi, and Golding 2019).

Reform Local Land Use, and Revisit Zoning Laws and Regulations

Several communities, such as Minneapolis, are rethinking zoning laws to improve access to affordable housing.[28] But some areas continue to create or perpetuate exclusionary barriers that reinforce regional racial and economic segregation. Local zoning and land-use laws should put racial equity at the center of their development. This will ensure that safe and affordable housing is equitably available in areas that optimize the benefits of homeownership.

Expand Down Payment Assistance

Robust down payment assistance (DPA) would support sustainable homeownership, especially for communities of color. For potential homebuyers that would otherwise qualify for homeownership but lack the necessary down payment, DPA would help them access homeownership and build their household's wealth. For homebuyers that have savings but would use a significant amount of it for a down payment, DPA allows them to keep more of their savings following a home purchase. The extra cash following a home purchase could instead serve as an important reserve for necessary repairs, helping homeowners of color maintain homeownership and build wealth over time.

Strengthen Pre-purchase and Post-purchase Counseling

The costs needed to maintain homeownership often come as a surprise, especially to new homeowners. These costs can be sizeable to homeowners on a tight budget and, if they are not met, can result in delinquent mortgage payments or even foreclosure. Borrower pre-purchase counseling that helps shoppers buy or qualify to buy a home and manage homeownership after closing will boost homeownership benefits for people of color. This includes quantifying these unexpected costs before home purchase so homebuyers are better prepared to enter and sustain homeownership.

Develop Financial Products for Home Maintenance, Repair, and Improvement

Home renovations and maintenance are a natural part of homeownership that factor into a home's value. The ability of homeowners of color to maintain and improve their home may be more difficult because they typically have less housing equity and fewer liquid assets. Maintenance costs, such as repairing a roof, fixing plumbing, or replacing a hot water heater, may reduce homeownership benefits directly and indirectly if the homeowner uses a home equity line of credit or cash-out refinancing to finance the improvements. Improving access to small-dollar home improvement loans for renovation and repair would help (McCargo, Bai, and Strochak 2019). Getting access to financing for smaller repairs (e.g., up to $10,000) is difficult but could create value in the property, which translates to equity and wealth. Providing affordable repair and renovation financing can help bridge the gap in homeownership benefits for homeowners of color.

Another potential proposal would be to create escrow savings accounts for homebuyers to help them meet major maintenance or repair needs. This insurance account could be funded through a borrower contribution in lieu of a larger down payment on the home. The fund would then function as an operating reserve. Such an insurance fund would prevent one channel of mortgage delinquency by providing an operating reserve to homeowners with fewer financial assets and would help families build long-term wealth.

Conclusion

The financial benefits of homeownership for homeowners of color are lower than the benefits for white homeowners. The typical homeowner of color, compared with the typical white homeowner, has a less valuable home, higher relative mortgage debt, and potentially modestly higher user costs of homeownership. These differences are particularly important amid an economic recession because they leave homeowners of color in a vulnerable position.

For example, less housing equity held by homeowners of color translates into fewer resources that can be used to weather a crisis. As we will explore in future analyses of economic downturns, tighter credit standards amid an economic downturn, particularly refinancing mortgages, may disproportionately restrict the ability of homeowners of color to access their housing equity or reduce their mortgage payments. A reduction in mortgage payments in response to lower mortgage rates would free financial resources for other needs.

Public policies developed to address the racial and ethnic disparities in homeownership's benefits are correct to respond to the current recession's impact. But policies must go further to eradicate the structural barriers in place before the recession. Our four policy recommendations focus on eliminating these systemic gaps, lessening how much economic downturns affect homeowners of color, and increasing the likelihood of recovery during economic expansion. Advancing these policies should minimize the volatile experiences of homeowners of color while sustainably reducing the racial and ethnic housing wealth gap.

Notes

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