Housing Finance: A Vestige of Systemic Racism?

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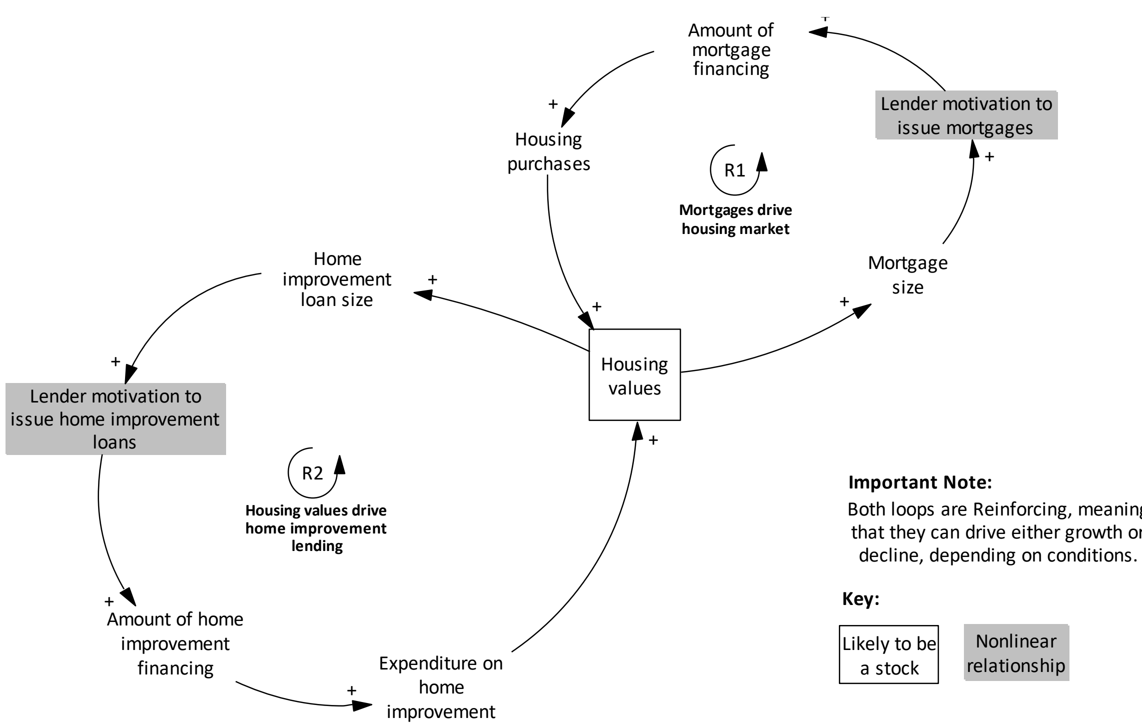
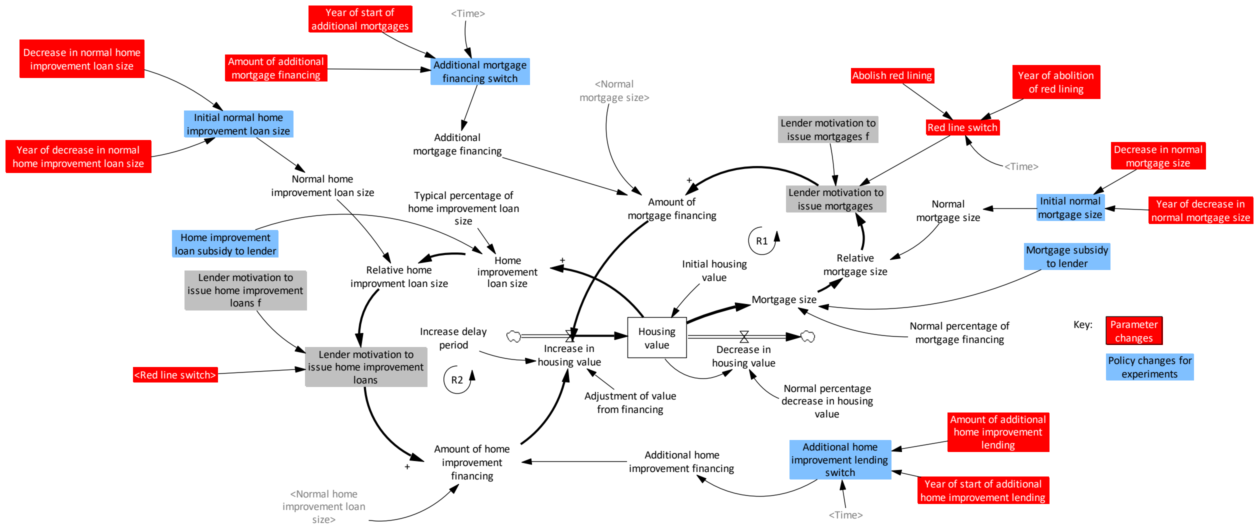
Extended Abstract

In recent months, there has been widespread discussion of "systemic racism," a situation under which members of minority races experience deleterious outcomes, such as higher arrest rates or greater wealth inequalities, stemming from explicit or implicit bias. Even though explicit bias is mostly illegal, systemic racism may still exist because of structures of policy or behavior that generate unnecessarily harmful outcomes. One such systemic structure involves how banks grant or deny financing for housing purchase or improvement. "Redlining," the depiction in red on "residential security maps" of supposedly high-risk lending areas, was an overtly discriminatory policy facilitated by a federal agency of the United States government, the Home Owners' Loan Corporation. Numerous studies have confirmed that these maps from the 1930s have led to low housing values *today* in those formerly redlined areas. Even though redlining has been illegal since 1968, traditional lenders nowadays decline loans in those areas because the loans are too small to be profitable.

A system dynamics model shows the systemic structure that leads to this situation.





The model simulates various policies for its solution. The most robust involve subsidies to lenders or lending from government or nonprofits, both of which could prove expensive. A less robust but potentially cheaper policy would require lenders to break from their usual policy and make small loans. Any of these policies would instill "pride of ownership" and "break the cycle" of the perverse reinforcing loop of declining housing, inability to get credit to improve the housing, and further housing decline.