

RACE AND MORTGAGE LENDING IN METROPOLITAN CENTERS OF THE EASTERN UNITED STATES

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ABSTRACT: *Review of more than 500,000 mortgage applications in 30 metropolitan areas of the eastern United States reveals distinct differences in approval rates for black and white applicants. White applicants routinely receive loan approvals at a much higher rate than black applicants regardless of applicant income and loan amount requested. City size affects black approval rates as does location of housing units within metropolitan areas. However, distinct regional differences are less evident. The findings suggest the need for greater efforts on the part of lending institutions to meet the credit needs of minorities.*

INTRODUCTION

Concerns about minorities being denied mortgage credit by lending institutions and concerns that lenders have systematically avoided making mortgage loans in poor neighborhoods prompted the United States Congress to pass legislation aimed at insuring equal opportunity in access to credit for housing. The Fair Housing Act of 1968 and the Equal Credit Opportunity Act of 1974 prohibit racial discrimination by banks and other lending institutions. In addition, the Community Reinvestment Act (CRA) of 1977 requires that lenders meet the credit needs of the entire community in which they operate. The CRA is designed to prevent the practice on the part of some lenders of purposely avoiding investments in low-income minority areas, a tactic commonly referred to as redlining. The laws are important since home ownership is the primary vehicle by which people acquire equity. If minorities are unfairly denied credit they are also being denied the opportunity to

participate in this common process of capital accumulation

While these laws are intended to protect minorities, their enforcement has been difficult given that discriminatory practices are difficult to uncover. Thus, to assist in evaluating lenders' actions the Home Mortgage Disclosure Act (HMDA) was passed in 1975. This law, which was strengthened by amendments in 1989, requires lenders to keep records on the race, income, and loan amount requested by applicants seeking loans and to report on the action taken in each case. In addition, the approximate location of the property in question is recorded, permitting one to ascertain if some lenders are avoiding minority areas.

HMDA data in and of themselves cannot be used to determine if discrimination is taking place since the aggregate statistics do not provide detailed information on such things as applicants' employment and credit history. However, the data can be used to identify problem areas and they can serve as a starting point for further research.

A number of researchers have used HMDA data to identify racial disparities in mortgage lending and have concluded that race is a factor in the

decision-making process (see, for example, Dedman, 1981; Munnell, et al., 1992; Dymski and Veitch, 1994; Squires and Velez, 1996). Such practices tend to hinder economic development in some sections of cities and, for a segment of the population, hinder opportunities to become part of society's economic mainstream. However, some claim that widespread discrimination does not take place in the mortgage industry simply because market forces will not allow it to exist. It is argued that if some lenders refuse to make loans because of race then other lenders will capitalize on these racist actions by stepping in to meet the demand for mortgages. While these researchers agree that the disparity between minorities and whites is significant, it is argued that such factors as credit history or employment patterns account for the differences (Holmes and Horovitz, 1994; Perle et al., 1994; Malmquist et al., 1997). Others dispute this, saying that the evidence is simply too strong to ignore (Nesiba, 1996). In addition, it has been argued that race may affect lenders' decisions if they think that minorities are more likely to default on loans due to problems such as racism in the labor market (Ladd, 1998). Despite this, the government has not been very aggressive in promoting strict compliance with the laws (Canner and Passmore, 1995, p.74).

Although the issue remains unresolved, the studies make it clear that problems exist for minorities who seek loans for housing. Generally these studies have been limited to a single metropolitan area. Little has been done in terms of looking at a large number of metropolitan areas or comparing different regions of the country. The present essay considers lending patterns for several metropolitan areas throughout the eastern half of the United States to examine racial variation in lending vis-à-vis city size and regional setting. It also provides a look at the degree to which inequity persists decades after laws were passed to improve the lending situation for minorities.

STUDY AREA AND METHODOLOGY

The study area consists of thirty metropolitan areas in the eastern United States (Figure 1). Population and location were considered

in selecting the cities examined in order to consider the impacts of city size and regional setting on lending decisions. Thus, ten of the metropolitan areas selected are small (250,000 to 500,000 people), ten are medium-sized areas (500,000 to 1,000,000 people), and ten are large metropolitan areas (1,000,000 to 1,500,000 people). In addition, half of the cities in each size category are located in the northern U.S. and half are located in the South. This permits examination of north-south differences given that the South has a more pronounced history of segregation and racial discrimination.

Nearly 520,000 loan applications filed by white and black applicants in 1996 are included in the study.¹ Forty-five percent of the applications are from northern cities. Approximately 14% of the applicants are black and 86% are white. No other minority groups are considered. Most of the black applicants (67%) are from southern cities. The study is limited to owner-occupied dwellings and loans for both the purchase of homes and for home improvements are included. Approval/denial rates based on race, income, and loan amount requested are examined by city size and by region.

In addition, intra-urban differences are studied with approval rates in majority-white areas compared to approval rates in minority areas. The purpose for this is to determine if there is any indication that lenders are systematically avoiding minority areas when making loan decisions. Examination of spatial variation by race is based on the racial composition of census tracts. For this purpose minority areas are considered to be those tracts whose populations are more than 80% black. White-majority areas are those tracts whose minority population is less than 20%.

MORTGAGE APPROVALS AND RACE

In considering the aggregate statistics for all cities, it is readily apparent that blacks are denied loans at a much higher rate than are whites. During 1996 Blacks obtained loans in 54% of the cases. Whites, on the other hand, received approval 71% of the time (Table 1). In addition, city size appears to have little impact on white approval rates. In small metropolitan areas whites gained approval 70% of the

Figure 1: Study sites

<u>NORTHERN METROPOLITAN AREAS</u>	<u>SOUTHERN METROPOLITAN AREAS</u>
<u>Small Centers (<500,000)</u>	
Charleston, WV South Bend, IN Erie, PA Rockford, IL Lancaster, PA	Savannah, GA Fayetteville, NC Montgomery, AL Pensacola, FL Jackson, MS
<u>Medium Centers (500,000-1,000,000)</u>	
Jersey City, NJ Springfield, IL Gary, IN Syracuse, NY Dayton, OH	Charleston, SC Mobile, AL Knoxville, TN Birmingham, AL Richmond, VA
<u>Large Centers (1,000,000-1,500,000)</u>	
Hartford, CT Buffalo, NY Milwaukee, WI Indianapolis, IN Cincinnati, OH	Jacksonville, FL Memphis, TN Nashville, TN Charlotte, NC Orlando, FL

time. For medium-sized areas the figure was 69% and in large cities whites had a 72% approval rate. However, for blacks city size does seem to matter. Blacks in small cities gained approval 52% of the time. Similarly, blacks in medium-sized cities had a 51% approval rate. In large cities, however, black approvals jumped to 57%, suggesting that a somewhat better lending environment exists for blacks in larger metropolitan areas (Table 1).

While the above data indicate that there are significant barriers to black home ownership, the aggregate statistics do not take into account the applicants' incomes and the requested loan amounts. These factors need to be considered when comparing and contrasting racial differences in mortgage approvals. For this purpose the requested loan amounts are divided into the following five categories: \$25,000 or less; \$26,000 to \$50,000;

\$51,000 to \$100,000; more than \$100,000. Similarly, applicant incomes are divided in five classes as follows: "very low-income" (<51% of the median income in the metropolitan area), "low-income" (51-80% of the area's median income), "moderate-income" (81-95% of the median), "medium-income" (96-120% of the median), and "high-income" (>120% of the median).

In examining all cities by race, income, and loan amount it is clear that for most income categories and for most loan amount ranges whites were more likely to receive loans than blacks (Table 2). In some instances this gap is quite distinct. For example, high-income blacks seeking loans of \$25,000 or less received them 50% of the time. Whites in the same income and loan amount categories gained approval 71% of the time, a 21 point difference. Similarly, medium income blacks

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Table 1
Mortgage loan approvals/denials, by race, 1996

CITY SIZE	APPROVED		DENIED		OTHER		TOTAL	
	White	Black	White	Black	White	Black	White	Black
Small (<500,000)	70% (43,155)	52% (5,726)	19% (11,644)	39% (4,288)	11% (6,549)	10% (1,098)	(61,348)	(11,112)
Medium (500,000- 1,000,000)	69% (85,328)	51% (10,596)	19% (23,912)	37% (7,678)	11% (13,876)	12% (2,408)	(123,116)	(20,682)
Large (1,000,000- 1,500,000)	72% (188,467)	57% (21,772)	17% (43,911)	31% (11,706)	12% (31,203)	13% (4,956)	(263,581)	(38,434)
TOTAL	71% (316,950)	54% (38,094)	18% (79,467)	34% (23,672)	12% (51,628)	12% (8,462)	(448,045)	(70,228)

requesting loans of \$51,000 to \$100,000 received approvals 69% of the time while their white counterparts were approved in 81% of the cases. In general, the differences in black-white approval rates are greatest for high-income applicants regardless of the loan amount requested and for moderate/medium-income people seeking small loans (<\$25,000) or loans greater than \$50,000. For these categories the differences between black-white approval rates ranged from 9 to 21 points (Table 2).

However, in some instances the gap between blacks and whites is fairly small. For example, very low-income whites seeking loans of \$25,000 or less were approved 41% of the time. Their black counterparts were approved in 35% of the cases, a six-point difference. In addition, moderate-income whites applying for loans of \$26,000 to \$50,000 received them in 49% of the cases. Blacks in this same category had a 44% success rate, for a five-point difference. In fact, in two instances black approval rates slightly exceeded white approvals. Very low-income blacks and low-income blacks requesting loans of \$26,000 to \$50,000 were approved 51% of the time. Very low-income whites seeking like loan amounts were approved 47% of the time while low-income whites wanting such loans had a 50% approval rate (Table 2).

Clearly the distinct racial differences in approval rates for some income and loan amount categories raise legitimate questions regarding bias in

lending. While it is true that with respect to loans greater than \$50,000 blacks have higher approval rates than do blacks seeking lesser loan amounts, it is also true that lenders are much more likely to make such loans to white applicants than to blacks. For smaller loan amounts it can be noted that both whites and blacks have lower approval rates than do applicants for larger loans. One factor here may be that lenders tend to avoid making small loans to people regardless of race simply because there is less profit in such loans. However, the fact that for smaller loan amounts the black-white gap narrows and in some instances favors blacks is an interesting pattern. It may be that this reflects efforts on the part of lenders to make loans in minority areas where real estate values tend to be low despite the fact that such loans are not very profitable. At the same time these lenders may show little interest in making similar loans to whites since there is less regulatory pressure to do so. On the other hand, the lessened gap between black-white approval rates for small loans may reflect lenders' greater willingness to make many small loans to large numbers of black applicants while avoiding making larger loans to blacks. Such an approach would tend to increase lenders' minority approval rates, thereby appeasing regulators and at the same time lessen perceived risk.

Table 2
Approval rates by race, income, and loan amount
(in percentages)

<u>INCOME</u>	<u>LOAN AMOUNT</u>							
	0-\$25,000		\$26,000-\$50,000		\$51,000-\$100,000		>\$100,000	
	Black	White	Black	White	Black	White	Black	White
<u>ALL CITIES</u>								
Very Low	35	41	51	47	47	55	*	*
Low	37	47	51	50	67	76	57	65
Moderate	40	53	44	49	69	80	66	77
Medium	41	59	43	50	69	81	73	82
High	50	71	51	67	71	84	78	88
<u>SMALL CITIES</u>								
Very Low	33	43	45	48	50	58	*	*
Low	39	49	47	50	66	76	*	*
Moderate	40	55	37	49	70	80	*	*
Medium	41	63	36	51	69	81	65	84
High	51	71	37	65	68	82	77	87
<u>MEDIUM CITIES</u>								
Very Low	36	40	42	43	47	56	*	*
Low	40	48	41	48	65	77	*	*
Moderate	42	56	40	47	66	79	71	77
Medium	43	59	41	47	64	80	74	81
High	57	80	55	71	75	91	87	95
<u>LARGE CITIES</u>								
Very Low	34	40	57	48	46	54	*	*
Low	36	47	59	51	68	76	56	66
Moderate	39	52	51	50	71	80	64	76
Medium	40	58	49	51	71	81	73	82
High	46	68	56	66	70	82	75	85

* insufficient data

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When one takes city size into account race again appears to be a factor (Table 2). In general, blacks in small cities fared less well than blacks in medium and large centers. However, the differences appear to depend on the loan amount sought. For instance, in small cities blacks seeking loans of \$26,000 to \$50,000 were approved 36 to 45% of the time depending on their incomes. In medium and large cities black approval rates for these loan amounts ranged from 40 to 59%. However, for loan amounts greater than \$50,000 black approval rates were similar regardless of city size. In addition, there is little variation in black approval rates for lower income blacks seeking small loans.

LENDING IN MINORITY VERSUS NON-MINORITY AREAS

The other major issue associated with mortgage lending is the degree to which lenders invest in minority areas. In considering this question, lending in minority areas is compared with lending in largely white areas. For this purpose minority areas are defined as census tracts that are more than 80% black. Non-minority areas are those tracts that are more than 80% white. Income and loan-amount requested are considered. However, city size is not examined since the number of loans in minority areas of small metropolitan areas is too small to be meaningful.

The results are mixed when one considers loans to blacks in minority versus non-minority areas (Table 3). For example, blacks seeking loans of \$50,000 or less were generally more likely to receive them if they lived in a minority areas than if they lived in a white areas. For instance, 52% of moderate-income blacks seeking loans of \$26,000 to \$50,000 for houses in minority tracts received them. Only 42% of blacks with the same income requesting similar loans for houses in white areas received them. However, when the loan amount requested exceeded \$50,000 blacks seeking loans in white areas were favored over blacks requesting loans for houses in minority tracts (Table 3).

Further, it is interesting to note that in minority areas blacks are more likely to be granted loans than are whites who live in minority areas

(Table 3). In some instances the differences are quite sharp. For example, 58% of low-income black applicants seeking loans of \$26,000 to \$50,000 received approval. However, whites in the same category received approval only 33% of the time. Similarly, 56% of high-income blacks applying for loans of \$51,000 to \$100,000 were approved while their white counterparts were approved 46% of the time. Similar differences are found for all categories except high-income applicants seeking loans of \$100,000 or more. However, in this category white applicants were favored by only one percentage point, with white and black approval rates of 73% and 74% respectively. Not surprisingly, when one looks at white areas this situation is reversed. For all income and loan amount categories shown blacks were less likely to receive loans than were whites.

The differences in lending practices between minority and non-minority areas raise some interesting questions. Further research is needed to determine why some black applicants in minority areas are favored over black applicants in white areas and why blacks in minority areas are favored over whites in these areas. In the first instance one needs to determine in which predominantly white areas blacks are seeking loans. In the second one needs to determine who the whites are in order to understand why they are being rejected at higher rates than blacks.

REGIONAL VARIATION IN APPROVAL RATES

Examination of the data on a regional basis does reveal North-South differences in lending practices, despite the fact that the aggregate data suggest that blacks in both regions receive loan approvals at approximately the same rate. As indicated in Table 4, northern blacks received approvals 54% of the time. For southern blacks the overall approval rate was just one point higher. However, one element that does stand out is the regional gap between black-white approval rates. Southern whites were approved 67% of the time while southern blacks won approval 55% of the time, a 12 point difference. In the North a 76% approval

Table 3
Approval rates for minority and non-minority areas
(in percent)

<u>MINORITY AREAS</u> (>80% minority)									
<u>LOAN AMOUNT</u>									
		0-\$25,000		\$26,000-\$50,000		\$51,000-\$100,000		>\$100,000	
<u>INCOME</u>	Black	White	Black	White	Black	White	Black	White	
Very Low	37	32	57	45	*	*	*	*	
Low	39	31	58	33	64	51	*	*	
Moderate	41	34	52	43	65	54	*	*	
Medium	41	32	53	29	63	58	*	*	
High	46	38	55	38	56	46	73	74	
<u>NON-MINORITY AREAS</u> (<20% minority)									
Very Low	34	42	40	48	40	55	*	*	
Low	38	50	43	53	67	77	56	66	
Moderate	42	56	42	52	72	81	65	77	
Medium	40	61	43	53	72	82	72	83	
High	53	70	51	66	72	83	76	85	
* insufficient data									

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rate for whites and a 54% approval rates for blacks results in a black-white approval gap of 22 points.

Further, city size appears to be a factor only in the South. In small and medium-sized southern cities blacks received approval 51% of the time. However, in large southern cities blacks were approved in 59% of the cases. City size appears to have little impact in the North where small, medium, and large cities had black approval rates of 56%, 53%, and 54% respectively. Interestingly, blacks in large southern cities fare better than do blacks in northern cities and, overall, there is little evidence that blacks have more difficulty getting loans in the South than in the North.

However, in looking at approvals based on income and loan amount requested sharper differences can be noted. For example, southern blacks seeking loans of \$25,000 or less were more likely to have received them than northern blacks seeking similar loan amounts (Table 5). However, this is the exception. For all other loan amounts and income groups the northern black approval rate is greater than the black approval rate in the South (Table 5). In some of these instances the differences are slight. For example, in five income/loan amount categories the differences between the higher northern approval rates and lower southern rates range from one to five points. However, in other cases the differences are considerable. This is especially true for blacks requesting loans of \$26,000 to \$50,000. Northern blacks in this category received approval 62 to 67% of the time regardless of income. Southern blacks seeking these loan amounts were approved only 38 to 48% of the time (Table 5).

In considering these differences, however, it is important to note that whites in the South were also less likely to gain approval than whites in the North. For example, northern whites seeking loans of \$26,000 to \$50,000 obtained them 61 to 76% of the time. Southern whites wanting the same loan amounts gained approval 40 to 56% of the time. Thus, regional differences are relative and it is perhaps better to consider the gap between black-white approvals in the North versus black-white approvals in the South. When one looks at loan differences from this perspective the South shows a much higher degree of equality than does the North (Table 5). The black-white difference in loan approvals in the South ranges from a ten-point advantage for blacks in gaining approvals to one

where whites have a fourteen-point advantage over blacks. Of the 19 loan amount/income categories shown in Table 5 the gap between blacks and whites exceeds ten points in only four instances. In the North, however, the black-white gap is as high as 25 and of the 19 loan-amount/income categories the black-white gap exceeds ten more than 50% of the time.

Finally, in looking at regional differences associated with lending in minority areas versus non-minority areas distinct differences can be found. For example, southern blacks in minority areas seeking loans of \$25,000 or less are more likely to be approved than are minority-area blacks seeking small loans in northern cities (Table 6). Depending on their income, blacks seeking small loans for houses in southern minority areas received approval 43 to 54% of the time. For blacks in northern cities these approval rates ranged from 34 to 41%. With increasing loan amounts, however, blacks in northern cities tended to do better than southern city blacks.

Some regional differences are also apparent for whites who sought loans for houses in minority areas. Whites seeking loans of \$25,000 or less were approved at approximately equal rates in the North and the South. However, as loan amounts increased whites in the North tended to have more success than whites in the South. For example, northern whites seeking loans of \$26,000 to \$50,000 in minority areas were approved 49 to 70% of the time depending on income while their counterparts in the South gained approval only 25 to 36% of the time (Table 6).

Further, in most instances blacks seeking loans in southern minority areas were more likely to obtain them than were southern blacks seeking loans in non-minority areas. In the \$26,000 to \$50,000 loan category, for example, southern blacks seeking loans for minority-area houses were approved 46 to 56% of the time. However, when blacks sought the same loan amounts for white areas in southern cities the approval rates fell to 36 to 48% (Table 6). In the North, however, black approval rates were roughly equal for most loan- amount/income regardless of whether applications were for minority or non-minority areas, although blacks in non-minority areas were favored somewhat.

Table 4
Regional variation in loan approvals by city size
(in percent)

<u>CITY SIZE</u>	APPROVED		DENIED		OTHER	
	Black	White	Black	White	Black	White
<u>NORTHERN CITIES</u>						
Small	56	73	35	17	9	10
Medium	53	75	35	16	12	9
Large	54	76	34	14	13	10
TOTAL	54	75	34	15	12	10
<u>SOUTHERN CITIES</u>						
Small	51	68	39	21	10	11
Medium	51	66	38	22	11	13
Large	59	68	28	19	13	13
TOTAL	55	67	33	20	12	13

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Table 5
Approval rates by region, income, and loan amount

<u>INCOME</u>	<u>LOAN AMOUNT</u>							
	0-\$25,000		\$26,000-\$50,000		\$51,000-\$100,000		>\$100,000	
	Black	White	Black	White	Black	White	Black	White
<u>NORTHERN CITIES</u>								
Very Low	33	44	62	61	59	60	*	*
Low	37	51	67	66	71	80	62	73
Moderate	38	57	66	65	73	84	68	79
Medium	40	62	62	66	75	85	75	84
High	46	71	65	76	76	87	76	87
<u>SOUTHERN CITIES</u>								
Very Low	36	38	48	38	43	51	*	*
Low	38	43	47	41	65	72	54	54
Moderate	42	47	39	40	68	76	64	73
Medium	43	54	38	42	67	77	72	80
High	52	66	44	56	66	78	75	84
* insufficient data								

Table 6
Regional variation in approval rates for minority and non-minority areas
(in percentages)

INCOME	LOAN AMOUNT							
	0-\$25,000		\$26,000-\$50,000		\$51,000-\$100,000		>\$100,000	
	Black	White	Black	White	Black	White	Black	White
<u>MINORITY AREAS</u>								
<u>NORTHERN CITIES</u>								
Very Low	34	29	55	68	*	*	*	*
Low	37	31	64	49	*	*	*	*
Moderate	39	34	67	70	*	*	*	*
Medium	39	31	62	48	*	*	*	*
High	41	32	69	58	68	60	*	*
<u>SOUTHERN CITIES</u>								
Very Low	43	35	56	35	*	*	*	*
Low	44	31	56	28	63	48	*	*
Moderate	45	33	46	36	61	48	*	*
Medium	46	32	49	25	62	58	*	*
High	54	43	49	34	51	41	74	73
<u>NON-MINORITY AREAS</u>								
<u>NORTHERN CITIES</u>								
Very Low	36	45	56	62	61	60	*	*
Low	42	53	61	66	74	81	*	*
Moderate	38	59	68	65	76	84	66	79
Medium	42	63	61	66	80	85	74	84
High	50	72	59	76	78	87	77	87
<u>SOUTHERN CITIES</u>								
Very Low	34	39	36	38	34	50	*	*
Low	35	46	39	44	65	72	54	54
Moderate	45	50	36	43	71	77	65	73
Medium	38	57	40	45	70	78	72	80
High	55	67	48	59	70	80	75	70
*insufficient data								

CONCLUSIONS

Since the data do not include information about applicants' credit and employment histories, it is not possible to definitively state that discrimination is taking place. However, distinct racial differences in loan approvals remain common decades after laws were passed to reduce inequities in lending. In relative terms this problem does not appear to be more serious in the South versus the North, although regional differences can be found. Clearly the lending industry needs to do more to make credit available to minorities. Outreach efforts, intra-urban office location, and policies aimed at creating affirmative action in the lending process merit consideration by lending institutions. Further, the federal government needs to become more assertive in promoting compliance with the letter and spirit of the laws. Increased vigilance and the exertion of greater pressure on lenders will serve to improve the situation. Even if greater risk is taken on in many cases, increased efforts by government and the lending industry ultimately will have a positive economic impact on urban areas. Conversely, the systematic denial of credit to individuals or to parts of a city will eventually be detrimental to the economic development of the entire metropolitan area.

NOTES

1. The data are collected and disseminated by the Federal Financial Institutions Examination Council (FFIEC). Data for this study were obtained through The Right-to-Know Network (www.rtk.net/).

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