

September 27, 2007

### **Federal Reserve Releases HMDA Analysis and Credit Scores Report**

The Federal Reserve Board has released its annual analysis of the aggregate Home Mortgage Disclosure Act (HMDA) data for the previous calendar year. The 2006 HMDA data analysis, which will be published in the Federal Reserve Bulletin, can now be viewed at <http://www.federalreserve.gov/pubs/bulletin/default.htm>.

The report, authored by economists in the Fed's Division of Research and Statistics analyzes the data from the nearly 8,900 lenders that reported HMDA data in 2006. The Federal Financial Institutions Examination Council (FFIEC) has released national aggregate data, summary tables pertaining to each lender and lending activity in each metropolitan statistical area (MSA). The FFIEC tables can be found at <http://www.ffiec.gov/infosystem.htm#HMDA>.

The Fed's analysis focuses primarily on the pricing information in the HMDA data, and differences across lending institutions, geographic areas, and population groups. Some of the key findings are:

In 2006, 28.7 percent of reported loans were "higher priced" (i.e. over the HMDA rate threshold), up from 26.2 percent in 2005. The report discusses the continuing impact of the flat yield curve on the data.

Regarding the incidence of higher-priced lending by race and ethnicity, the report finds that, as in previous years, the 2006 data show black and Hispanic borrowers more likely and Asian borrowers less likely than non-Hispanic whites to have higher-priced loans—for both home purchases and refinancings. The authors control for borrower-related factors (income, loan amount, MSA, presence of co-applicant and sex) and the specific lending institution. When the results are modified, the gap is substantially reduced, but not eliminated.

For home-purchase loans in 2006, for example, the gross mean incidence of higher-priced lending was 53.7 percent for blacks and 17.7 percent for non-Hispanic whites, a difference of 36 percentage points. After controlling for lender- and borrower-related factors, the remaining gap was 12.6 percent. In 2005, the same figure was 10 percent. For refinancings, the gap in 2006, after controlling for these factors, was reduced to 7.3 percent (6.2 percent in the previous year). The results for Hispanics were similar.

Denial rates continue to vary by applicant race and ethnicity, as in previous years. For the 2006 home-purchase and refinance loans, unmodified, American Indians, blacks and Hispanic whites had higher denial rates than non-Hispanic whites; blacks had the highest rates, and Hispanic whites had rates between the two. The differentials were similar to, in some cases slightly higher

than, previous years. Although control factors were able to reduce those disparities, unexplained differences remain.

The report identifies many of the possible explanations for the remaining differences in the incidence of higher-priced lending and denial rates (measures of credit history, loan-to-value ratios, debt-to-income ratios, and differences in choice of loan product). “Differential costs of loan origination and the competitive environment also likely bear on the differences in pricing; so may differences in financial literacy, which can lead to differences in credit-shopping activities and negotiating.” The report notes that discrimination may also play a part, but that further research is needed.

### *Geographic Distribution of Scores*

The report plows new ground this year by including a study of the national distribution of credit scores. The study, which considers the distribution of credit scores across census tracts nationwide, suggests that individuals in higher-income census tracts tend to have higher credit scores; as do individuals in predominantly nonminority census tracts. Regionally, the South and Southwest and portions of the Midwest have relatively low mean credit scores, compared with other parts of the country. The data also show that census tracts with larger shares of mortgage borrowers who have relatively low credit scores have larger shares of individuals who receive higher-priced loans. Finally, the report finds a statistical relationship between the incidence of higher-priced lending and loan performance, but the authors conclude that the nature of the relationship needs to be studied further.

### **Fed Study on Credit Scores**

In related news, the Fed has also released its 300 page Report to Congress on Credit Scoring and its Effects on the Availability and Affordability of Credit. The report was one of the many lingering requirements of the FACT Act, which amended the Fair Credit Reporting Act and called for numerous studies on various subjects. A sister report, released by the Federal Trade Commission, looked at the use of credit scores in insurance, and generated some controversy and a congressional hearing.

The Fed report concluded that credit scores are predictive of credit risk for the population as a whole and for all major demographic groups and that credit characteristics included in credit history scoring models do not serve as proxies for race, ethnicity or sex. The authors also concluded that “[d]ifferent demographic groups have substantially different credit scores, on average. For example, on average, blacks and Hispanics have lower credit scores than non-Hispanic whites and Asians, and individuals younger than age 30 have lower credit scores than older individuals. Also, for given credit scores, credit outcomes—including measures of loan performance, availability, and affordability—differ for different demographic groups.” (S-2) A copy of the report can be found on CBA’s web site.

CBA will also be hosting its [Fair Lending Conference](#), November 4-6, 2007, at the Ritz Carlton Pentagon City, Arlington, Virginia. **Federal Reserve Board Governor Randall S. Kroszner** will speak. **Glenn Canner**, Senior Advisor, Federal Reserve Board, will discuss the HMDA data and will examine geographic variation in loan performance, and his colleague at the Federal Reserve, **Robert Avery**, will discuss the Credit Scoring Study. Information on the program and how to register may be found at CBA’s web site, [www.cbanet.org](http://www.cbanet.org) or by calling 703-276-1750.